STATE OF NEW HAMPSHIRE
PUBLIC UTILITIES COMMISSION

DG 13-086

NORTHERN UTILITIES, INC.

Petition for Permanent Rate Increase

Order Approving Settlement Agreement

O R D E R N O. 25,653

April 21, 2014

APPEARANCES: Gary M. Epler, Esq., for Northern Utilities, Inc.; 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.

This Order approves a settlement agreement allowing Northern Utilities, Inc., a permanent rate increase resulting in a 12% increase to an average residential customer's bill, to meet the Company's goals of investments in safety and reliability, increased investments in expansion of the Company's customer base, and to bring distribution revenues in line with current operating costs.

I. PROCEDURAL BACKGROUND

On March 15, 2013, 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 3, 2013, 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 April 15, 2013, the Company filed its proposed rate schedules seeking: (1) a permanent rate increase of approximately $5.2 million in annual revenues, effective May 15, 2013, (2) implementation of a multi-year alternative rate plan, which included a capital cost recovery mechanism, (3) a number of

miscellaneous rate design changes, and (4) a temporary rate increase expected to produce an increase of $2.5 million in annual revenues commencing with service rendered on July 1, 2013, and applied until a final Commission Order establishing permanent rates would be issued. *See* Hearing Exhibit 2. The Company applied a test year for the 12 months ending on December 31, 2012. With its filing, the Company submitted the pre-filed testimony of Mark H. Collin, Thomas P. Meissner, Jr., David L. Chong, George E. Long, Jr., Douglas J. Debski, James D. Simpson, 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 May 6, 2013, the Commission issued Order No. 25,504, which suspended the Company's proposed tariff revisions and scheduled a prehearing conference and technical session for June 5, 2013. On May 30 and May 31, 2013, C. Alexander Cohen of Dover filed two e-mailed comment letters in opposition to the Company's rate proposal. No one filed a motion to intervene. At the June 5, 2013, prehearing conference, the Commission approved the Company's motion for confidential treatment. *See* Transcript of June 5, 2013, Prehearing Conference at 8. The Commission approved a procedural schedule recommended by the parties by secretarial letter on June 10, 2013. Commission Staff (Staff) and the OCA made oral data requests regarding the Company's temporary rate request, and the Company provided responses on June 12, 2013.

On June 13, 2013, the Company, Staff, and the OCA executed and filed a settlement on the Company's temporary rate increase request, allowing the Company to apply a uniform,

per-therm surcharge of $0.0421 to all of the Company's current rate schedules for service rendered on or after July 1, 2013. *See* Hearing Exhibit 1. After hearing on June 17, 2013, the Commission approved the settlement on temporary rates. *See* Order No. 25,529 (June 26, 2013).

From mid-2013 until early 2014, the Company, Staff, and the OCA engaged in discovery, met in technical sessions, and held settlement discussions. As a result of those discussions, the parties agreed to the terms of a Settlement Agreement which they contend resolves all of the issues in this case. The Settlement Agreement was executed on March 4, 2014, and filed on March 5, 2014. *See* Hearing Exhibit 3.

On March 11, 2014, Staff filed the testimony of Stephen P. Frink to provide Staff's explanation of, and support for, the Settlement Agreement's terms. *See* Hearing Exhibit 4. On March 13, 2014, a hearing was held regarding the Settlement Agreement, at which Messrs. Collin, Meissner, Debski, and Frink provided additional oral testimony in support of the Settlement Agreement.[1] In addition, the Company and Staff jointly filed a schedule summarizing the distribution revenue changes contemplated by the Settlement Agreement. *See* Hearing Exhibit 6.

II. OVERVIEW OF SETTLEMENT TERMS AND BILL IMPACTS

The relevant terms of the Settlement Agreement, executed by the Company, Staff, and the OCA (Settling Parties), are asset forth below.[2] Staff's explanations of the technical features of this Settlement Agreement may be found within Mr. Frink's testimony, at Hearing Exhibit 4.

[1] On March 28, 2014, pursuant to the terms of the Settlement Agreement, the Company filed its rate case expense filing, with an accompanying motion for confidential treatment of billing information of the Company's service providers.

[2] The Settlement Agreement, adopted as Exhibit 3 at the March 13, 2014, 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 $4,573,098, effective May 1, 2014, on the basis of the 12-month test year ending on December 31, 2012. Of this increase, $4,359,117 would be collected within permanent distribution rates, and $213,981 would be collected within the Cost of Gas clause as a component of indirect gas costs.[3] Also pursuant to Section 2.1 of the Settlement Agreement, the Settling Parties agreed that, except as provided for in the Settlement Agreement, the Company's next filing of a distribution base rate case would be based on an historic test year of no earlier than twelve months ending December 31, 2016, *i.e.*, a so-called "stay-out" provision.

In Section 2.2 of the Settlement Agreement, the Settling Parties indicated their application of the following capital structure, including a 9.50 percent return on equity:

	Component Percentage	Cost	Weighted Cost
Common Equity	51.76%	9.50%	4.92%
Preferred Stock Equity	0.0%	0.00%	0.00%
Long-Term Debt	47.56%	7.05%	3.35%
Short-Term Debt	0.69%	2.01%	0.01%
Total	100.00%		8.28%

Pursuant to Section 2.3 of the Settlement Agreement, the Settling Parties agreed, for the purposes of this specific Settlement Agreement, that the Company's annual distribution revenue requirement associated with the revenue increase described in Section 2.1 would be allocated to

[3] With this increase to the Cost of Gas clause, total annual revenue collected related to the Company's indirect gas costs would be $933,344.

the Company's customer classes as indicated in Attachment 3 to the Settlement Agreement.[4] As agreed by the Settling Parties, the residential classes' customer charges would be set at $19.00 per month (low income rate customer charges would then be adjusted in the same manner as the Company's original proposal) and no residential classes' revenue increase percentages would exceed 150% of the overall average percentage increase or be less than 50% of the overall percentage increase.

In Section 2.4 of the Settlement Agreement, the Settling Parties agreed that, in addition to the annual revenue increase stipulated by Section 2.1, there would be two future step increases to revenue and rates: (1) a Step 1 adjustment, effective May 1, 2014, to recover the revenue requirement associated with the Company's investments in its Gas Main Extensions, New Hampshire Main Replacement Program, and Gas Highway Projects City State (collectively, "Eligible Facilities"), which are additions to utility plant during calendar year 2013 (the costs of these investments total $8,983,772), and (2) a Step 2 adjustment, effective May 1, 2015, to recover the Eligible Facilities revenue requirement associated with the Company's investments in additions to utility plant during calendar year 2014, subject to a cost cap of $12 million on such investments. (Additional technical details, including those relating to the Return on Equity (ROE) applied to the Step 1 and Step 2 adjustments, and supporting schedules, may be found within the various subsections of Section 2.4 of the Settlement Agreement, and Attachments 4 and 5 of the Settlement Agreement).

[4] The term used within the Settlement Agreement for the labeling of the attached schedules was "Exhibit." To avoid confusion with the official hearing exhibits, of which the Settlement Agreement is Exhibit 3 in this case, we use the term "Attachment." For future submissions, we request that parties consistently use the label "Attachment" for supporting schedules appended to settlement agreements, discovery, and other materials.

Pursuant to Section 2.5 of the Settlement Agreement, the Settling Parties agreed that the Company would be allowed to adjust its then-existing distribution rates up or down, subject to the Commission's review and approval, due to "Exogenous Events," as defined by the various terms presented in the subparts of Section 2.5. At the hearing, the parties agreed to a revision of Subsection 2.5.1 of the Settlement Agreement so that it would read as follows:

> 2.5.1. For any of the Exogenous Events defined as a State Initiated Cost Change, Federally Initiated Cost Change, Externally Imposed Accounting Rule Change, or Force Majeure during the term of this Settlement Agreement, the Company will be allowed to adjust distribution rates upward or downward (to the extent that the revenue impact of such event is not otherwise captured through another rate mechanism that has been approved by the Commission) **if the distribution revenue impact (positive or negative) of any such event exceeds $200,000 (Exogenous Events Rate Adjustment Threshold) in any calendar year beginning with 2014.** (Emphasis added; *see* Transcript of March 13, 2014 Public Hearing (Tr.) at 71-72.

Pursuant to Section 2.6 of the Settlement Agreement, for calendar years 2014, 2015, and 2016, the Settling Parties agreed that the Company would be allowed to retain all earnings up to and including an ROE of 10 percent. Under the terms of this so-called "Earnings Sharing" provision, the Company's earnings in excess of an ROE of 10 percent and up to and including 11 percent would be shared equally between firm tariffed customers[5] and the Company; earnings in excess of an ROE of 11 percent would be returned to firm tariffed customers.

In Section 2.7, 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, 2014, through an equal per therm Reconciliation of Permanent Changes in Delivery Rates (RPC) charge for all customer classes, in accordance with the provisions of the Company's Local Delivery Adjustment Clause (LDAC) tariff. This

[5] Special contract customers are not eligible for earnings sharing, as they are not "firm tariffed" customers.

recoupment would be calculated based on the difference between temporary rates and permanent rates and the resulting LDAC charge would be subject to reconciliation. (Additional technical details regarding this provision related to reconciliation are presented in Attachment 6 of the Settlement Agreement).

With regard to rate case expenses, the Settling Parties agreed, in Section 2.8, that the Company's prudently incurred rate case expenses would be recovered over a 12-month period via a Rate Case Expenses charge, as approved by the Commission. The Settlement Agreement contemplates that recovery of rate case expenses would begin on May 1, 2014, at $0.0042 per therm, as outlined in Attachment 7 of the Settlement Agreement.

Under Section 3.1 of the Settlement Agreement, the Settling Parties agreed that the Company's Farm Taps would be replaced on an "as-needed" basis due to physical deterioration, or else in accordance with the identification and prioritization of the risks in the Company's Distribution Integrity Management Plan. Under Section 3.2 of the Settlement Agreement, the Settling Parties agreed to certain modifications of the Customer Service Metrics established in Order No. 24,075(Oct. 28, 2002), and modified in Order No. 24,906 (Oct. 10, 2008). Under Section 3.3 of the Settlement Agreement, the Settling Parties agreed that the Company would amend its Line Extension Policy and Tariff Page 16 to provide that it will install, at no charge to its customers, up to 100 feet of service pipe, under normal conditions as determined by the Company, from a gas main to service residential customers with amended Tariff language presented within Attachment 10 of the Settlement Agreement.

In Section 3.5 of the Settlement Agreement, the Settling Parties agreed that before the Company begins preparation of one or more new cost of service studies for a future rate case, it

would meet with Commission Staff and the OCA to discuss whether new cost of service studies are necessary, and if necessary, the format and requirements of the studies to be filed.

The rate increases and other charges stipulated by the Settlement Agreement, including the May 1, 2014, step adjustment and the adjustment to recover the difference between temporary and permanent rates, are expected to increase bills by $142 annually for a typical residential heating customer of the Company using 747 therms per year, an approximate 12 percent increase over current bills. *See* Hearing Exhibit 3, Attachment 8, at Page 24; Tr. at 42-53.

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. According to the Company's filing, as of December 31, 2012, its overall weather-normalized earned rate of return was 5.8 percent, as opposed to the 9.5 percent overall return authorized by the Commission in the Company's last rate case, *see Northern Utilities, Inc.*, Order No. 25,352 (April 24, 2012). In its filing, the Company claims that its earnings would have further eroded absent some form of rate relief. Staff and the OCA, as Settling Parties, have indicated their 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 recommends an increase in 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 an arbiter between the interests of customers and those of regulated utilities. *See* RSA 363:17-a, *see also* Order No. 25,352 (April 24, 2012) at 7.

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 Admin. Rules Puc 203.20(b) requires that, prior to approving a settlement, the Commission determine that the settlement results are just and reasonable and in the public interest. Because 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 initial revenue increase of approximately $4.6 million to be recovered through permanent rates, compared to the Company's proposed revenue increase of $5.2 million. In addition to the initial rate increase, the Settlement provides for a first step adjustment, effective May 1, 2014, that will increase revenues by approximately $1.4 million, comparable to the revenue increase that would have been expected under the Company's proposed alternative rate plan involving a capital investment tracker mechanism. The May 1, 2014, revenue increase (permanent rate increase and step adjustment) will provide Northern the opportunity to earn an overall rate of return of 8.28 percent, based upon a return on equity of 9.5 percent, and the application of the Company's actual capital structure of 52%

equity and 48% debt. We find this rate of return and return on equity to be reasonable and within the scope of recent precedent. *See, e.g.*, Order No. 25,352 at 8 (approving a return on equity of 9.5 percent). Further, the amount of the revenue increase represents a negotiated amount that provides the Company the revenues necessary to operate safely and reliably. Thus, we find that the Settlement Agreement is reasonable and in the public interest.

The Settlement Agreement provides for a 12-month surcharge to recover the under-recovery resulting from the reconciliation of temporary and permanent rates and rate case expenses, effective May 2014. The Settlement Agreement also provides for a second step adjustment effective May 1, 2015, expected to increase annual revenue requirement by $1.4 million, or roughly the same amount, to be recovered through the surcharge that expires on April 30, 2015. Because the termination of surcharge and implementation of the second step adjustment coincide, there should be a negligible impact on customer bills at that time. Consequently, customer's non-supply costs should remain fairly constant through at least mid-2017.

Regarding the issues of rate design (including the Step 1 and Step 2 rate adjustments), volumetric rates, and ancillary features and 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 also approve, on the basis of evidence presented by the Settling Parties and the supporting materials filed with the Settlement Agreement (including the Attachment 6 of the Settlement Agreement), the proposed

rate reconciliation surcharge of $0.0161 per therm, pursuant to RSA 378:29. This rate shall be subject to the additional reconciliation called for by the Settlement Agreement's terms. We will also approve the rate case expense recovery surcharge of $0.0042 per therm, subject to any reconciliations resulting from our final review of the Company's rate case expense filing, as discussed below.

To conclude, we approve the Settlement Agreement and incorporate its terms and conditions into this order, as just and reasonable and in the public interest. We commend the Company, Staff, and the OCA for their collaborative efforts in developing the Settlement Agreement, and particularly welcome the innovative Earnings Sharing provision, the "Stay-Out" provision, and the adjustment to the Company's Line Extension Policy. These provisions offer considerable potential benefits to the Company's customers. Our approval of this Settlement Agreement does not limit our disposition of similar matters in future cases.

To facilitate the efficient administration of the Settlement Agreement, we authorize the Company, Staff, and the OCA to modify the Settlement Agreement so long as any modification is mutually agreed upon and non-substantive, such as a clerical or ministerial amendment that involves timing or scheduling. The parties shall file any such modification with the Commission and provide a copy to all parties on the service list. In this instance, we will rule on the Company's rate case expense filing, and the Company's accompanying motion for confidential treatment separately to allow Staff and the OCA to propound discovery on the Company regarding the rate case filing materials, and to allow for continued review of that matter. To the extent the rate case expenses we approve for recovery via the rate case expense surcharge differ from the estimated expenses contained in the Settlement Agreement, the revenue collected

through the surcharge will be reconciled with the approved expense amount, and any under- or over-recovery treated accordingly, either credited or charged to ratepayers.

Based upon the foregoing, it is hereby

ORDERED, that the Settlement Agreement filed on March 13, 2014, as amended by the bench ruling pertaining to Subsection 2.5.1, is APPROVED; and it is

FURTHER ORDERED, that permanent rates, and related surcharges commence on May 1, 2014, on a service-rendered basis.

By order of the Public Utilities Commission of New Hampshire this twenty-first day of April, 2014.

Amy L. Ignatius	Robert R. Scott	Martin P. Honigberg
Chairman	Commissioner	Commissioner

Attested by:

Lori A. Davis
Assistant Secretary