STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 5701/5724

Investigation into the existing rates of Central Vermont Public Service Corporation AND Tariff filing of Central Vermont Public Service Corporation, requesting an 8.9% rate increase, to take effect 4/1/94	)	Hearings held at Montpelier, Vermont July 5-8, 18-19, 1994, August 16-19, 29, 31, 1994 September 1-2, 6-9, 12-13, 1994 Public Hearing at Middlebury, VT August 17, 1994

Order Entered: 10/31/94

PRESENT: Richard H. Cowart, Chairman
Suzanne D. Rude, Board Member
Leonard U. Wilson, Board Member

APPEARANCES: Joseph M. Kraus, Esq.
Morris L. Silver, Esq.
Kenneth C. Picton, Esq.
Kimberly K. Hayden, Esq.
for Central Vermont Public Service Corporation

Harriet A. King, Esq.
King & King
for Vermont Yankee Nuclear Power Corporation

James Volz, Esq.
Geoffrey Commons, Esq.
Robert V. Simpson, Esq.
for the Department of Public Service

Lewis Milford, Esq.
for the Conservation Law Foundation

TABLE OF CONTENTS

I. INTRODUCTION 4

II. THE "CEILING ADJUSTMENT" 7

III. PROCEDURAL ISSUES 9
A. Procedural History 9
B. The Nadel Paper and Demand-Side Management ("DSM") Annual Reports 11
C. Identifying Commercial and Industrial Recipients of Incentives 12
D. CV's First Amendment Claims 14

IV. RATE BASE ISSUES 15
A. Rate Base/Cost of Service Agreement 15
B. Uncontested Revisions 16
C. Pittsford Penstock 18
D. Cavendish Breaker 19
E. FERC Hydro Projects 20
F. Section 225 Objection 20
G. Sunderland Service Center 24
H. Springfield Service Center 25
I. Capital Expense 26
J. Working Capital Allowance 27
K. Accumulated Deferred Income Taxes ("ADIT") 28
L. FAS 112 Unfunded Accruals 29
M. FAS 106 Unfunded Accruals 29
N. "Interim Period" Depreciation Reserve Growth 33
O. Other Depreciation Reserve Adjustments 38

V. COST OF SERVICE ISSUES 39
A. Power Cost Stipulation 39
B. Other Post-Employment Benefit Expenses (FAS 112) 40
C. Management Incentive Program Expenses 42
D. Distribution Contract Tree Trimming 45
E. Expense Savings - Sunderland and Springfield Service Centers 47
F. O&M Expense Savings Associated with Basic Records and Work Order Management 47
G. Account 931 Rent Expenses 50
H. Advertising Expenses 52
I. Trade Show Expenses 61
J. Community Relations Expenses 63
K. Edison Electric Institute ("EEI") Dues 63
L. Expenses Related to the Docket No. 5546 Executive Compensation Proceeding 64
M. Gain on Sale of Utility Property 65
N. Depreciation Expenses 66
O. Income Taxes 68
P. Uncollectibles 71
Q. Restructuring 73
R. The Ceiling Adjustment 77
S. Cost of Service Adjustment for Services Provided to SmartEnergy Services, Inc. ("SES") 78

T. Salary and Wages 88
U. ACE-Cost of Service and Rate Base Impacts 88
V. C&LM-Cost of Service and Rate Base Impacts 90

VI. COST OF CAPITAL 91
A. Capital Structure 91
B. Cost of Equity 94

VII. RESOURCES AND COST MANAGEMENT 98
A. Power Supply Management 99
B. Demand-Side Management Programs 127
C. Conclusion Re: Resources and Cost Management 171

VIII. CONCLUSION 175

IX. ORDER 175

I. INTRODUCTION

In this rate proceeding an electric company faces the consequences of its past commitments to sharply increasing purchase power costs. Those consequences must be faced under market and economic conditions that now call for lower, rather than higher, customer bills.

Central Vermont Public Service Corporation ("CVPS", "Company", or "Central Vermont") has presented this case in a somewhat ambiguous way. The Company publicly announced that it was seeking an 8.9 percent rate increase, while filing documentation that it asserted would support an increase of 12 percent, and arguing that any adjustments must be set off against that higher starting point. The Department of Public Service ("DPS" or "Department"), on the other hand, asserts that the Company should actually reduce rates by almost 1.0 percent. After extensive review and analysis, we conclude that the Company is entitled to an overall rate increase approximating $8,575,000 million or 4.27 percent.[1]

CVPS faces one financial problem that is more significant than all others. This is an overcommitment to increasingly expensive power supply sources, coupled with a sharp drop in the value of those resources when offered for resale in the wholesale markets. The Company has recently begun a serious effort at cost-cutting, seeking out substantial savings opportunities in all operational areas, with a goal of lowering non-power costs by $20 million annually. This heightened attention to costs is a welcome sign. Unfortunately, even if achieved, all of these non-power cost savings would be more than offset by the $21.6 million in power cost increases that CVPS has already incurred since 1989. In addition, the Company also asserts a need to collect a further $2.55 million because of increased power costs for 1995 and foresees a total of $48.5 million (34 percent) in net power cost increases between 1994 and 1997, due primarily to substantial increases in expected payments for imported power.

The Board shares the concern expressed by CVPS's management that these circumstances call for a heightened and intensive focus on all of the Company's costs. However, we do not accept the Company's current prescription for change as an adequate response. As proposed by CVPS, restructuring costs would be borne principally by ratepayers and, to a lesser extent, by the Company's employees and suppliers. Under the Company's proposal, shareholders would bear neither any

---

1. A precise calculation of the actual increase should be made in the compliance filing required by this Order.

responsibility for the current situation nor any share of the cost of necessary remedies. This would be neither just nor reasonable. The evidence that we have heard has demonstrated significant errors by CVPS in management of its resource options in recent years. For these reasons, we conclude that CVPS's management and shareholders must share the financial consequences of decisions that have raised the Company's power costs and their customers' bills.

The Department of Public Service, on behalf of ratepayers, has advocated significant disallowances to the cost of service, associated with mismanagement of both power costs and energy efficiency programs. Substantial evidence in the record convinces us that ratepayers must not be asked to bear all of the costs associated with excessive power commitments, failure to fully explore return sales opportunities, ineffective energy efficiency programs, and the transition costs of the current restructuring program. Costs incurred in response to these problems should be borne, at least in part, by the Company's investors. For this reason, we accept the Department's recommendation to adjust the Company's allowed rate of return.

We apply an adjustment of 75 basis points (.75 percent) on the return on equity. While it is significant, this adjustment is smaller than the total effect of the separate adjustments recommended by the Department and by intervenors for mismanagement of both power supply and energy efficiency programs. It is also less than the full adjustment that the evidence on these issues would support. However, it is in accord with similar reductions ordered by other utility commissions and by this Board in regard to other utilities, and it reflects our conclusion that CVPS must maintain its essential financial viability as we work through a difficult period of transition.

This Docket, involving 20 days of technical hearings and thousands of pages of testimony and exhibits, has been the most lengthy and contentious electric case in Vermont since the nuclear-era cases of the 1980's. Unfortunately, the advocacy has at times seemed to focus inordinate attention on relatively minor aspects of the costs of service, thus diverting attention from far more important elements of CVPS's costs.[2]

---

2. The debate over fuel-switching as a technique for energy efficiency is perhaps the chief example of this tendency to focus on a tree while ignoring the forest. The difference between Central Vermont's 1993 budget for residential programs with fuel-switching measures and the DPS's proposed annual expenditures for those same programs is less than $1.0 million. CVPS 1993 DSM Annual Report at 12, 21; Docket 5270-CV-1&3, exh. JJP-15, B-1. We do not even attempt to

Those fundamental problems include the fact that CVPS increased its number of employees by one-third between 1983 and 1989, the Company's personnel costs have risen dramatically through 1993, while the number of customers per employee has dropped. Even more significant is the prospect of escalating power costs. This is a problem that must be faced squarely, as a matter of fairness to ratepayers and for the good of Vermont's economy. Its resolution should also be the highest concern of investors, because it is the single factor most threatening to the long-term financial viability of the Company.

It is likely that the electric industry is entering a period of rapid structural and regulatory change. Our Order in this proceeding is intended to set the stage for a new period of regulation and to support a transition to a more competitive position for CVPS. In past orders and hearings, this Board has invited CVPS and other electric utilities to propose new mechanisms and alternative forms of regulation that could improve their companies' competitive positions and capture the efficiency benefits of market mechanisms, while equitably sharing costs and benefits between investors and ratepayers.

The electric industry has entered a period of intensified cost consciousness and is approaching a period of restructuring and regulatory reform. We specifically invite CVPS and the Department to work with the Board to develop equitable cost-reduction and transition strategies for the Company -- strategies that recognize both the benefits of energy efficiency programs and the realities of power markets. It is time to move from confrontation to cooperation, for the ultimate benefit of the Company's ratepayers and its investors, and for the general good of the state.

II. THE "CEILING ADJUSTMENT"

---

resolve the core of that debate in this docket; however, we must observe that either of these figures is a small portion of the Company's costs of service, and pales in comparison to the almost $50 million annual increase in net power costs that CVPS anticipates by 1997. It seems likely that more money has been spent litigating fuel-switching than has been spent implementing programs. This conflict has consumed resources, regulatory attention, and mutual good will. Most importantly, it has diverted all parties' attention from the truly fundamental problems that must be faced by the Company's management.

CVPS claims that its cost of service supports a 12 percent rate increase. However, the Company has filed for an 8.9 percent increase, reducing the total increase requested by the use of a voluntary, Company-imposed, mechanism called the "Ceiling Adjustment". The Ceiling Adjustment represents an additional $4,788,000 of, as yet, unknown and unmeasurable savings that result in the 8.9 percent cap. CVPS states that the purpose of the Ceiling Adjustment is to limit the Company's rate increase to approximately 8.9 percent —— an increase that is slightly less than the inflationary increase that has occurred since the Company's last rate increase in September 1991. CVPS states that capping its total rate increase request at 8.9 percent is a response to the increased competitive pressures facing its customers and the increasing competitive market facing the Company. Refer to the Findings in Section V.R., below. Pennington pf. at 9.

The Ceiling Adjustment is designed to include possible savings, as well as the costs that the Board disallows in this proceeding. CVPS believes that this adjustment provides a balance between the interests of both customers and shareholders, while limiting the Company's actual rate increase to no more than 8.9 percent. Findings 146-151; Pennington sup. pf. at 4; tr. 8/31/94 at 93.

The DPS does not support the Company's proposed Ceiling Adjustment as filed. The DPS refers to CVPS's Ceiling Adjustment as the Company's "Management Challenge" cost of service credit, emphasizing that it was CVPS management that had decided to take on the risk of achieving the $4,788,000 in additional cost savings. These savings were not reflected in CVPS's adjusted cost of service that was filed with the Board and are not considered known and measurable. The DPS believes, however, that the Company was already aware of some future cost savings opportunities that were not already built into its test year results. The Department also notes that any opportunities for adjusted test year cost savings that have not been included in the Company's current filing do not suddenly vanish merely because CVPS's filing results contained errors or other inappropriate ratemaking components which, when corrected for, would reduce the Company's as-filed revenue requirement. In essence, the DPS argues that whatever the correct level of real savings expected for CVPS, the level will not be altered by CVPS's choice to add various other elements to its claimed cost of service. Finding 149; Henkes pf. at 125, 129; tr. 7/8/94 at 224-227.

The DPS acknowledges that there are some cost savings-related adjustments to CVPS's proposed Ceiling Adjustment that are appropriate. The DPS supports offsetting Ceiling Adjustment with ten adjustments that fall into two categories: (1) the additional cost savings resulting from the updated restructuring adjustment which were identified in

CVPS's May 1994 update; and (2) any additional future cost savings adjustments made to CVPS's as-filed adjusted cost of service results. Exh. DPS-RJH-R-1, Sch. 29; Henkes pf. at 129-130; tr. 7/8/94 at 223-224, 228-234, 239-244.

The DPS applies these offsets to reduce CVPS's originally proposed $4,788,000 Management Challenge cost of service credit to a remaining cost of service credit of $2,544,000. After considering the additional cost savings that CVPS had identified in the May 10, 1994 filing update, the remaining Management Challenge that is still unknown and unmeasurable becomes $1,947,000. The DPS regards that amount as CVPS's future cost savings opportunity, or the risk that the Company had stated that it will undertake. Id.

The DPS recommends adjusting CVPS's originally filed cost of service by a total Management Challenge cost of service credit of $2,544,000. This credit consists of: (1) the $597,000 of the now known and measurable cost savings that CVPS had identified in its May 10, 1994 filing update; and (2) the $1,947,000 cost savings that remain unknown and unmeasurable, since CVPS's management assumed the risk that it will be able to achieve these savings. Finding 152.

The DPS asserts that its proposal would not create a disincentive for CVPS to propose a similar cost-cutting measure in the future. The DPS points out that the Management Challenge is consistent with the objective of electric utilities throughout the nation, including CVPS, to become more competitive by containing their costs and minimizing any required rate increases. Tr. 8/31/94 at 64-66.

We support the Company's efforts to keep rate increases to a minimum. We find that accepting the Department's proposal would provide strong disincentives for utility companies to cap their rate increase requests. However, we must note that CVPS's simultaneous presentation of its proposal as a rate cap and as a so-called "management challenge" is disingenuous. By: (a) capping its request to increase its rates at 8.9 percent; (b) including cost of service adjustments that support a 12 percent rate increase; and (c) requiring any adjustments that come out of this ratemaking proceeding as deductions from that 12 percent, CVPS is not actually accepting the risks that it claims. Management's strong opposition to the DPS's proposal is clear evidence that CVPS's approach is, in essence, a rate cap and not a true management challenge. CVPS cannot have it both ways; we believe that customers could potentially be confused by the conflicting nature of CVPS's claims regarding its request.

The DPS's "management challenge" cannot be accepted. Thus, we have applied all adjustments to the Company's filed 12 percent cost of service increase.

III. PROCEDURAL ISSUES

A. Procedural History

On November 16, 1993, the Board opened an investigation into CVPS's rates in Docket 5701. The Board held a prehearing conference on December 17, 1993, to set a schedule for proceeding and to select an appropriate historic test year and adjusted test year. On February 3, 1994, the Board issued a prehearing conference memorandum which established the schedule for Docket 5701.

On February 15, 1994, CVPS filed with the Board a separate petition to revise its tariffs to reflect an increase in rates of $17,900,000 or 8.9 percent. The Company actually filed a cost of service that supports a 12 percent rate increase.[3]

On February 24, 1994, Harriet Ann King, Esq., on behalf of Vermont Yankee Nuclear Power Corporation ("VY"), filed a motion to intervene in this Docket, stating that VY would provide an updated operating expense projection regarding its power costs for CVPS's rate cases, pursuant to an information agreement between VY and CVPS dated June 1, 1988.

On March 17, 1994, the DPS, pursuant to 30 V.S.A. § 225, notified the Board that it had conducted a preliminary review of the Company's February 15th rate filing and recommended that it be suspended.

On March 21, 1994, the Department filed a Motion to Consolidate Docket No. 5701 with CVPS's filing for an 8.9 percent rate increase.

In an Order issued March 23, 1994, the Board suspended CVPS's rate request for an 8.9 percent increase, opened this investigation (Docket No. 5724), and set the date of March 28, 1994 for a prehearing conference to discuss a schedule, VY's motion to intervene, and other relevant issues. The Board also scheduled a status conference for the same time to consider the Department's motion to consolidate the two proceedings and to consider the Board's proposal to appoint an independent expert witness for the purpose of evaluating the Company's management of power costs.

On April 7, 1994, the Board granted the Department's motion to consolidate dockets and directed the Company to employ the 1993 calendar year as the test year and the year beginning November 1, 1994 and ending October 31, 1995 as the adjusted test year.

---

3. The Company proposes a Ceiling Adjustment to limit CVPS's rate request to 8.9 percent. See, Finding 146 below.

On May 23, 1994, the Board held a prehearing conference to discuss the schedule, to consider Lewis Milford's petition to intervene on behalf of the Conservation Law Foundation ("CLF") which was filed with the Board on April 11, 1994, and the Board's May 10, 1994 memorandum to the parties regarding the Company's power costs.[4]

On May 24, 1994, the Board issued a procedural Order implementing a protective agreement for certain information that CVPS alleges or may allege is confidential during the course of the proceeding.

On June 1, 1994, CLF sent a letter to the Board asking whether it planned to retain an expert witness on the issue of power costs and if not, why not. The Clerk of the Board responded in a letter of June 15, 1994, stating that the Board reached the conclusion that it would be appropriate to raise specific power cost questions in a memorandum to the parties and their experts, rather than to hire a parallel expert witness.

The Board issued two modified scheduling Orders on July 28, 1994, and August 22, 1994.

Technical hearings were held on July 5-8, 1994, July 18-19, 1994, August 16-19, 29, and 31, 1994, and September 1, 2, 6-9, 12, and 13, 1994. A public hearing was held on August 17, 1994 at Middlebury.

B. The Nadel Paper and Demand-Side Management ("DSM") Annual Reports

At the August 17, 1994 technical hearing, the Board informed the parties that it would like to introduce various documents as Board Exhibits in this proceeding. They included a study entitled "Achieving High Participation Rates: Lesson Taught By Successful DSM Programs" prepared by Steven Nadel, *et al*. (the "Nadel Paper") and the 1993 DSM Annual Reports of: (a) Green Mountain Power Corporation ("GMP"); (b) the City of Burlington Electric Department ("BED"); (c) Washington Electric Cooperative, Inc. ("WEC"); and (d) Citizens Utilities Company ("CUC").[5] During the hearings of August 17 and 29, 1994, Central Vermont objected to the introduction of these items. Tr. 8/17/94 at 163-169; tr. 8/29/94 at 11-34; CVPS Brief, Vol. I at 6-8.

---

4. That memorandum on power costs also was the subject of a follow-up conference call on June 7, 1994.

5. The Board added the request for CUC's DSM annual report in a memorandum to the parties in this proceeding, dated August 24, 1994.

We conclude that it is not necessary to rule on the merits of CVPS's objection substance of this issue at this time. The numerous witnesses that have testified in this proceeding have provided the Board with sufficient evidence to establish findings and reach conclusions concerning the DSM matters that now require resolution. The Nadel Paper and the annual DSM reports of other utilities need not be included as part of the record for decision in this docket.

We note, however, that CVPS, in opposing consideration of these reports, failed to address *In Re NET&T*, 1 PUR 3d 33, an apparently controlling case which held, at 51, that this Board may take judicial notice of formal legally-required reports that have been filed before us.

C. Identifying Commercial and Industrial Recipients of Incentives

1. CVPS provided a confidential list identifying customers (and associated incentive amounts) who participated in the Large and Small C&I Retrofit program, the Small Commercial Remodeling program, the Equipment Replacement program, the Energy Efficient Motors program, the Industrial New Construction program, and the Large Commercial Remodeling and Equipment Replacement program.[6] CVPS filed the information at the request of the Board and under the confidentiality agreement that had been implemented in this docket by the Board's May 24, 1994 Order. Exhs. Board-W and Board-X.

2. In response to the Board's request, CVPS contacted those customers that had received incentives in the programs listed above. CVPS asked each customer whether it would object to the release of its specific identification, linked to the amount of incentive paid by CVPS to that customer under such programs. Out of at least 126 customers, only two indicated a concern upon this point. Id.

---

6. We hereby take official notice of CVPS's response to the Board's request for a list of large customers and incentive amounts who have participated in CVPS's energy efficiency programs besides the Large C&I Retrofit program, pursuant to 3 V.S.A. §810(4). CVPS's response was filed with the Board on September 20, 1994 and is referred to as Exhibit Board-X.

Discussion re: Identifying Commercial and Industrial Recipients of Incentives

CVPS argues that the names of specific customers who have received incentive payments as participants in its energy efficiency programs should remain confidential unless the customers consent to the release of their names. However, after explicit notice, only two customers indicated an objection to such a release. Thus, public copies of Board Exhibits X and W will be redacted by deleting the names of those two customers, while still indicating the names and incentive levels of all other customers, as well as still indicating the amounts paid to the two unidentified customers. At this time, however, we are not ruling on the confidentiality of the filed information for the two customers seeking confidentiality. There is no pending objection to providing that information under a confidentiality agreement. In addition, none of the parties argued for publicly releasing this information during the technical hearings or in their briefs. Findings 1, 2. We note, however, that commercial and industrial recipients of substantial individually negotiated incentive payments are, in many ways, similar to recipients of special contracts. Similar balancings of public and private interests may be appropriate in resolving any future debates upon these issues.

While not seeking release of specific data at this time, the DPS makes a more abstract argument about future treatment of such data. The DPS asserts that, as a general principle, such names not be kept confidential. The DPS adds that it does not like to enter into protective agreements, but believes that it has no choice if it wants to get information on a timely basis. Tr. 8/17/94 at 116-117.

We are sympathetic to the Department's concerns that utilities are more frequently seeking protective agreements in response to discovery requests. In other dockets, the Department has expressed its position that, as a public agency, it prefers a policy of openness for public review as detailed in 1 V.S.A. § 315. Docket 5270-HDWK-1, Order of 6/14/94 at 4.

As to the future, we note that the party seeking confidential treatment bears both the initial obligation to make a prima facie showing of entitlement to confidentiality and the ultimate burden of demonstrating that necessity. Vt. R.Civ.P. 26, Killington vs. Lash, 153 Vt. 628 (1990). We encourage the DPS to pursue this policy of openness in future proceedings by requesting explicit rulings upon specific confidentiality requests, pursuant to Rule 26(c).

We note that it will often be most efficient for the DPS to first request, receive, and review allegedly confidential data under a standard confidentiality agreement. Following such review, the DPS may wish to exercise the standard clause in such agreements that allows a petition for a declaration that specific material received is not

entitled to confidential treatment. This should allow a more focused and informed resolution of such disputes.

D. CV's First Amendment Claims

CVPS's reply brief makes a new claim that had not previously been at issue in these proceedings. CVPS asserts that the DPS's arguments for a penalty in this rate case amount to an effort to dissuade the Company from asserting its positions before the Board and other state regulatory agencies. CVPS asserts that the DPS seeks, in effect, to abridge the Company's First Amendment right to free speech under the United States Constitution. CVPS Reply Brief at II-68.

CVPS's argument in its reply brief is its first presentation of this claim. It comes months after the DPS's original request for a penalty; after hundreds of hours devoted to prefiled testimony, hearings, and briefs; and at a time that makes it impossible for the DPS to make a meaningful response to this attack on its positions. As such, CVPS's claim offers a classic example of why courts universally refuse to consider arguments that are first raised in reply briefs and absent a compelling reason for a failure to make a more timely presentation. It must be rejected upon these grounds alone.

An independent reason for rejecting this argument also exists. The Company's arguments suggest that we should focus upon the allegedly improper motives of the Public Advocate, rather than upon the evidence supporting or critiquing the costs that CVPS seeks to collect from ratepayers. The U. S. Supreme Court has previously ruled (in a case that CVPS has not mentioned in its brief) that such a claim should not even be considered in the absence of extraordinary supporting evidence. Morgan v. United States, 304 U.S. 1 (1938) (Morgan II). CVPS, in contrast, cites no direct evidence to support its allegations about the DPS's motivations. Public Advocates in numerous American jurisdictions have often sought imprudence and mismanagement penalties, and they routinely seek rate reductions comparable to those pursued by the DPS in this case. *See* cases cited in Section VII. The DPS's efforts in this case have been focused upon the financial effects upon ratepayers of utility actions and inactions, not on the Company's preferences or public policy arguments. Upon the record in this case, we find CVPS's last-minute First Amendment claim to be without merit. See also, Central Hudson Gas v. PSC, 447 U.S. 557, at 563, 571 (1980).

Finally, lest there be any doubt about the substance of this issue, we stress that we unequivocally support the rights of regulated companies, interested persons, and the Department to petition this Board, and make any and all arguments regarding the positions they wish adopted, subject only to the usual rules of judicial tribunals, such as

relevance, repetition, compliance with underlying statutes, and applicable procedural requirements. Indeed, our ability to decide the complex matters often put before us depends upon the vigorous presentation of competing views by the parties. But we are not here persuaded by CVPS's brief, which appears to treat the DPS's attempt to protect ratepayers because of a substantive concern as being equivalent to pursuing a penalty for advocating the recovery in the first place.

IV. RATE BASE ISSUES

A. Rate Base/Cost of Service Agreement

3. The parties agreed to certain revisions to the Company's proposed rate base. Those adjustments to rate base are hereinafter referred to as the "Rate Base/Cost of Service Agreement" and summarized as follows:

Rate Base Adjustments	Filed	Corrected
RB 10 - Vernon Road	270,000	129,000
RB 28 - Accounts Correcting for Efficiency	1,174,000	1,089,000
RB 29 - Construction Work in Progress	(5,424,000)	(5,471,000)
RB 35 - Working Capital	(6,083,000)	derivative
RB 54 - Accumulated Depreciation	2,144,000	2,140,000
RB 55 - Accumulated Deferred Income Taxes	3,698,000	derivative
RB 58 - Other Post-Employment Ben. FAS 112	125,000	101,000
RB 60 - Restructuring Savings	-0-	145,000
RB 61 - Other RB Deductions in Account 242	-0-	932,000

Frankiewicz pf. at 3-14; Frankiewicz reb. pf. at 1; tr. 7/7/94 at 3-14.

4. CVPS's test year rate base, adjusted for known and measurable changes is $277,967,000. Exh. RJH-1, Sch. 18, Rev. 9/15/94.[7]

B. Uncontested Revisions

5. In order to correct for an error associated with the Vernon Road Cap Bank rate base claim, CVPS must reduce its originally claimed plant in service by $141,000, increased construction work in progress by $13,000, reduced accumulated deferred income taxes by $5,000, and reduced depreciation expenses by $4,000. Henkes pf. at 7-8, 21, 41 and 100.

---

7. We hereby take official notice of the DPS exhibit RJH-1, revised 9/15/94 ("Exh. RJH-1, rev. 9/15/94") which was filed with the Board on 9/23/94 with the Department's brief in this proceeding. Pursuant to 3 V.S.A. § 810(4), any party that objects to including that exhibit in the official record of this Docket shall notify the Board of its objections by November 9, 1994.

6. CVPS must reduce its claimed rate base investment for construction work in progress by $47,000 to correct for errors related to the Vernon Road Cap Bank and certain unregulated and growth-related CWIP. Henkes pf. at 21.

7. CVPS must reduce its rate base claim for prepayments by $656,000. This corrects for a $66,000 error, removes $359,000 of "below-the-line" prepayments, and annualizes the impact of certain prepayment offsets, a $231,000 adjustment. Henkes pf. at 26-28; CVPS Reply Brief at I-9.

8. CVPS must reduce its claimed rate base component for ACE by $85,000 and its claimed cost of service amortization expense for ACE by $351,000 to correct for certain errors. Henkes pf. at 38; Pennington reb. pf. at 42-43; Henkes surreb. pf. at 32.

9. CVPS must reduce its rate base by $763,000 to reflect rate base offsets for self-insurance and deferred compensation reserve accruals in Account 242. Henkes pf. at 42-43.

10. CVPS must reduce its rate base by a net amount of $145,000 to correct for errors associated with the rate base impact of its proposed restructuring adjustment. Henkes pf. at 120-121.

Discussion re: Uncontested Revisions

In its original filing, CVPS had proposed a pro forma plant in service addition of $270,000 for the Vernon Road Cap Bank. After discovery by the DPS, the Company conceded that it had made an error in calculating this proposed rate base addition. CVPS confirmed that the correction for this error reduced the claimed plant in service addition for Vernon Road Cap Bank from $270,000 to $129,000. Henkes pf. at 7-8; exh. DPH-H, Sch. 19 at 1; tr. 7/7/94 at 7.

This correction also resulted in an associated $13,000 increase in CVPS's originally claimed Construction Work In Progress ("CWIP") balance (Henkes pf. at 21; exh. DPH-H, Sch. 21), an associated $5,000 decrease in CVPS's originally claimed accumulated deferred income tax balance (Henkes pf. at 41; exh. DPH-H, Sch. 24), and an associated $4,000 depreciation expense decrease (Henkes pf. at 100; exh. DPH-H, Sch. 15.). CVPS reduced its originally claimed rate base investment for CWIP of $5,067,000 by $47,000. This rate base reduction amount of $47,000 represents the net impact of a $13,000 increase associated with the Vernon Road Cap Bank error correction, a $2,000 decrease to remove CWIP related to unregulated operations, and a $58,000 decrease to remove Work Order ("WO") 36 growth-related CWIP. Henkes pf. at 21; exh. DPH-H, Sch. 21.

In its original filing, CVPS proposed a rate base investment level of $2,693,000 for the prepayment component of the working capital allowance. Pursuant to discovery

by the DPS, CVPS has conceded that this rate base claim should be reduced by $66,000 to correct a mathematical error. Henkes pf. at 26; Finding 7.

CVPS also confirmed that its claimed prepayment level should be reduced by $359,000 to remove "below-the-line" prepaid insurance balances for executive officer supplemental insurance, directors and officers deferred compensation insurance, executive officers insurance-1988 plan, and deferred cont. plan insurance. In addition, the Company's claimed prepayment level should be reduced by $231,000 to reflect the appropriate annualization of offsetting payables associated with the prepayment component for "prepayments to affiliates". The total reduction to CVPS's originally claimed prepayment rate base balance is $656,000, resulting in an appropriate net prepayment balance of $2,037,000. Henkes pf. at 26-28; exh. DPH-H, Sch. 22; finding 7.

In its original filing, CVPS proposed an adjusted test year ACE amortization amount of $1,039,000 and an adjusted test year ACE rate base investment level of $1,260,000. During discovery, CVPS confirmed that it had made certain calculation errors. Henkes pf. at 38. Subsequent to this original filing, CVPS also revised its proposed ACE amortization and rate base calculations to remove the impact of wholesale allocations and to correct for errors relating to its lost revenue calculations. Pennington reb. pf. at 42-43. The total impact of the above-described corrections and revisions reduces CVPS's original ACE rate base claim by $85,000 and original ACE amortization claim by $351,000. CVPS exh. JMP-4; Henkes surreb. pf. at 32, exh. DPS-RJH-R-1, Sch. 31.

CVPS's originally claimed rate base should have been reduced by $763,000 to reflect certain self-insurance and deferred compensation reserve accruals. This would be particularly appropriate since CVPS's originally proposed rate base includes rate base additions for the prepaid deferred taxes associated with these reserve items. CVPS has agreed that a rate base deduction of $763,000 for these items would be an appropriate adjustment. Henkes pf. at 42-43; exh. DPH-H, Sch. 26; DPS Brief at 5.

As part of its originally filed restructuring adjustment, CVPS proposed a net rate base deduction associated with VRP, VSP and ISP restructuring costs.[8] However, when the Company filed its updated restructuring adjustment, it failed to reflect such a net rate base deduction. Pursuant to DPS discovery on this matter, CVPS agreed that a net rate

---

8. VRP, VSP, and ISP are CVPS's Voluntary Resignation Plan, the Voluntary Severance Plan, and the Involuntary Severance Plan, respectively.

base reduction of $145,000 should be made, representing a VRP-related rate base reduction of $814,000, offset by VSP- and ISP-related rate base increases of $542,000 and $127,000, respectively. Henkes pf. at 120-121, exh. DPH-H, Sch. 28. pg. 3.

C. Pittsford Penstock

11. CVPS proposes to add $120,000 to rate base to reflect the projected plant in service addition for the Pittsford Penstock project. Henkes pf. at 8.

12. The Pittsford project has no supporting work order and is not projected to be on line until September 1995. CVPS has not yet completed a cost/benefit analysis for this project, and the Company does not expect to spend any money on this project until the summer of 1995 when work on the project is projected to start. Henkes pf. at 8.

Discussion re: Pittsford Penstock

The Pittsford Penstock project is not expected to come on line until (at best) one month prior to the end of the adjusted test year in this case. Therefore, a slight delay in the currently expected completion date of this project would move it outside of the adjusted test year. In addition, the Company's proposed rate base claim for this project is not supported by any work order or cost/benefit analysis details. Henkes pf. at 8. We remove this project from CVPS's rate base because the projected completion date is too far removed from the date of this decision and because CVPS has not provided sufficient information to render the proposed revenue requirement impact of this project known and measurable at this time. Findings 11, 12.

D. Cavendish Breaker

13. CVPS proposes to add $189,000 to rate base to reflect the projected plant in service addition for the Cavendish Breaker project. Henkes pf. at 8.

14. The Cavendish Breaker project has no supporting work order and CVPS has not yet completed a cost/benefit analysis for this project. Id.

Discussion re: Cavendish Breaker

The Company's proposed rate base claim for this project is not supported by any work order or cost/benefit analysis details. CVPS has not secured permits or hired contractors for this project. Henkes pf. at 8. Therefore, CVPS's proposed rate base addition for this project is not known and measurable at this time. CVPS's proposed $189,000 rate base addition for the Cavendish Breaker project is denied. Findings 13, 14.

E. FERC Hydro Projects

15. CVPS proposes to add to rate base estimated capital costs of $231,000 associated with FERC hydro licensing. Henkes pf. at 9.

16. The proposed $231,000 rate base claim represents an estimate for which CVPS could not provide a detailed breakdown by specific component and on a per-site basis. Henkes pf. at 9.

17. The exact projects that make up the estimated $231,000 capital costs will depend on FERC licenses which may or may not be issued in 1994. Henkes pf. at 9.

18. CVPS has not yet prepared a work order for these projects and, to date, it has not spent any amount of the $231,000. Henkes pf. at 9.

Discussion re: FERC Hydro Projects

CVPS's proposed estimated rate base addition of $231,000 for the FERC hydro projects is dependent upon a number of factors which are not known and measurable based on the record evidence in this proceeding. First, the projected rate base claim is based on a pure estimate on the Company's part, unsupported by any work order details (no work order has as yet been prepared) and specific project component details. Second, the $231,000 capital cost estimate is based on CVPS's assumption that certain potential projects be included in this cost estimate. These potential projects, in turn, would depend on whether CVPS will receive FERC licenses for these projects. Henkes pf. at 9. Finally, the timing and outcome of any FERC licenses to be issued is not known and measurable. Accordingly, CVPS's proposed rate base claim of $231,000 for these projects is denied. Findings 15, 16, 17, 18.

F. Section 225 Objection

At the July 5, 1994 technical hearing, CVPS attempted to introduce revisions to Witness Kirn's prefiled testimony with respect to the costs and in-service dates of the North Springfield and Sunderland service centers.[9] The adjustment for the North

---

9. CVPS has plans to consolidate operating districts. The Company is transferring personnel from the Ascutney operations center to North Springfield. The Company intends to consolidate the Springfield and Ascutney service centers into a single North Springfield service center. In addition, the Manchester and Bennington District offices are being consolidated in Sunderland. Kirn pf. at 4; tr. 7/5/94 at 212-213.

Springfield center represents an increase in rate base of $1,022,000 (the difference between the new adjustment of $1,569,000 and the original amount of $547,000). The adjustment for the Sunderland center is a decrease in rate base of $506,000 (the difference between the new adjustment of (-$24,000) and the original amount of $482,000). Tr. 7/5/94 at 202-204.

CVPS argued that the adjustments, which had been provided to the DPS as part of discovery, were not amendments proscribed by 30 V.S.A. § 225. This, according to CVPS's theory, was because they would not increase the amount the Company was requesting in rates due to the proposed Ceiling Adjustment which capped CVPS's rate request at 8.9 percent. Tr. 7/5/94 at 191-192.

The Department moved to strike Kirn's attempt to make changes to his testimony. The DPS based its objection on 30 V.S.A. § 225's anti-updating rule and noted that CVPS had failed to provide the Department with the information until the Friday before the hearing. The Department stated that it was "prejudicial for us [the DPS] bringing it in at the last minute". Tr. 7/5/94 at 190-197.

The Board sustained the DPS's objection. The Board stated that CVPS's correction is in fact an amendment and a substantial revision and, therefore, is prohibited by 30 V.S.A. § 225. Id. at 192-197.

CVPS requests that the Board reconsider its oral ruling not to permit Witness Kirn's adjustments regarding the costs and in-service dates of the North Springfield and Sunderland service centers. CVPS offers three reasons for making this request. First, it states that by not accepting the revisions, the Board is "concluding that it will base its order on information it knows to be incorrect". Second, CVPS asserts that the decision was egregious because no one challenged the correctness of Mr. Kirn's revisions. Finally, CVPS states that the Board's ruling is contrary to good public policy. CVPS argues that failure to consider this testimony was a violation of the Board's obligation to consider any evidence which may illuminate the case, and cites the Vermont Supreme Court case, *Central Vermont Public Service*, 141 Vt. 282 (1982). CVPS Brief, Vol. I at 5-6.

The DPS requests that CVPS's request for reconsideration of this issue be denied. The DPS argues that the legislature was very clear on how late a company can produce evidence to support its case. The Department asserts that without a cut-off point, the Department and the Board would be forced to evaluate a constantly moving target. DPS Reply Brief, Vol. I at 3-4.

After reviewing both parties' briefs on this matter, we affirm our original ruling which found the testimony to be an impermissible update. We deny CVPS the opportunity to revise its Witness Kirn's original prefiled testimony.

It is necessary to respond to CVPS's concern that the Board would be relying upon "incorrect information" by ignoring the proferred testimony. Ratemaking is comprised of a set of principles which in Vermont include normalization, amortization, and the use of unadjusted test year revenues. Each of these ratemaking approaches is an attempt to obtain a fair and appropriate balance of available financial information, yet none use actual adjusted test year data. CVPS itself employs ratemaking approaches of this nature. The fact that these principles do not rely on actual information does not make them "incorrect" for ratemaking purposes.

CVPS also raised a concern that the Board's ruling is "contrary to good public policy". CVPS's argument is quite surprising in light of the public policy regarding updates that is explicitly contained in 30 V.S.A. § 225. That section expresses a clear public policy, based on a recognition that the utility controls the information and (usually) the timing relevant to a rate case. It also recognizes the public risk posed by forcing the Public Advocate to litigate against a moving target or to risk the kind of litigation-by-ambush that CVPS has attempted in this instance. Thus, Section 225 explicitly prohibits a company from updating either its own filing or its own evidence supporting that filing. CVPS's proposed modification is an update, and therefore, the statute forbids it. See Board's Order of 1/26/94, Docket 5656 at 6-9.

Application of 30 V.S.A. § 225(a) sets forth the "updating" standard for utilities:

> In no event may a company amend, supplement or alter an existing filing or substantially revise the proof in support of such filing in order to increase, decrease or substantiate a pending rate request, unless, upon hearing, the company demonstrates that such a change in filing or proof is necessary for the purpose of providing adequate and efficient service. However, upon application of any company subject to the provisions of this chapter, and with the consent of the department of public service, the board may for good cause shown prescribe a shorter time within which such change may be made. (Emphasis added).[10]

The Board's Order of 11/26/90 in Docket No. 5428 found this statute to be similar and consistent with 30 V.S.A. § 226, which establishes the showing necessary before

---

10. PSB Rule 2.204(G) parallels and implements the § 225(a) standard, while PSB Rule 2.402(C) provides the Board with the power to allow exhibits into rate proceedings at its discretion.

temporary rates can be granted.[11] On page five in that Order, the Board concluded that, "the Legislature's decision to use precisely the same text in two immediately adjacent sections of Title 30 must have reflected a conscious intent that they be interpreted in similar and consistent ways." Therefore, we conclude that the updating standard under § 225 (i.e., that the update is permitted only if necessary for the purpose of providing adequate and efficient service) is met only by a utility that is faced with financial need to the degree that it must either reduce service or curtail maintenance.

Since Section 225 applies to proposed changes of either the filing or evidence supporting the filing, and CVPS proposes a modification to the evidence supporting the filing, we conclude that Section 225 applies to CVPS's proposed modification. We also express our dismay both about the Company's effort to add substantial amounts to its claimed rate base immediately before the evidentiary hearings and for the Company's repeated efforts to reiterate this point without acknowledgment of clear precedents and binding statutory texts.

G. Sunderland Service Center

19. CVPS's 13-month average 1993 test year rate base includes $1,919,000 for the plant in service and $246,000 for accumulated depreciation related to its current Bennington and Manchester service centers, for a net rate base claim of $1,673,000. Henkes pf. at 11; exh. DPH-H, Sch. 19 at 2.

---

11. In the Board's Order of 11/26/90 in Docket No. 5428, the Board compared the updating standard in 30 V.S.A. § 225 (i.e., the update must be "necessary for the purpose of providing adequate and efficient service") with the criteria for granting temporary rates under 30 V.S.A. § 226. In that Order, the Board discussed two prior cases that applied the criteria for granting approval for temporary rates under Section 226. The first case was the Board's Order of 11/13/90 in Docket No. 5461, in which the Board relied on In re Green Mountain Power Corp., 142 Vt. 373 (1983). The second case was the Board's Order of 6/27/85 in Docket No. 5001. In both cases, the Board, in ruling on temporary rates for utilities, applied the standard that the utility must be faced with some financial need "to the degree that it must either reduce service or curtail maintenance." Docket No. 5428, Order of 11/26/90 at 4-5, quoting Docket No. 5001 Order of 6/27/85 at 8.

20. CVPS proposes to consolidate its current Bennington and Manchester service centers and Bennington commercial office into a single new facility in Sunderland starting July, 1995. Henkes pf. at 10.

21. CVPS proposes a pro forma rate base addition of $482,000 to reflect its projected investment for the new consolidated facility in Sunderland as of July, 1995. Henkes pf. at 10.

22. CVPS's proposed adjusted test year rate base also includes the plant investments for the current Bennington and Manchester service centers which will be consolidated into Sunderland effective July, 1995. In fact, CVPS has stated that it will sell its current Manchester and Bennington facilities once the consolidation into Sunderland is completed. Henkes pf. at 10-11.

23. It is appropriate to reduce CVPS's proposed rate base by $515,000 to remove the net plant in service associated with the current Bennington and Manchester service centers as of July, 1995. Henkes pf. at 11; exh. DPH-H, Sch. 19, at 2.

Discussion re: Sunderland Service Center

CVPS's net rate base investment of $1,673,000 will no longer be used and useful when the Bennington and Manchester service centers are consolidated into Sunderland in July of 1995, and CVPS has indicated that the Bennington and Manchester centers will be sold after the consolidation into Sunderland. This period covers four of the thirteen months in CVPS's proposed adjusted test year. Therefore, it is appropriate to remove from CVPS's proposed rate base 4/13th (7/95-10/95) of the net rate base amount of $1,673,000; this equals $515,000. While CVPS has proposed a pro forma rate base addition of $482,000 to reflect the plant addition for the new consolidated Sunderland service center as of July 1995, it has failed to reflect the previously described $515,000 rate base reduction to remove the net plant investment for the current Bennington and Manchester service centers. Failure to remove this $515,000 net plant in service investment would represent an inappropriate double count. Therefore, CVPS's rate base shall be reduced by $515,000. Findings 19, 20, 21, 22, and 23.

We also note that Board practice required the gain on the sale of no longer used service centers/office buildings be used to offset the capital cost of the new or replacement facilities. Thus, any gain on a future sale of the unused centers should receive this accounting and ratemaking treatment. *See* Docket 5428, Order of 1/4/91 at 28-29.

H. Springfield Service Center

24. CVPS's 13-month average 1993 test year rate base includes $259,000 for plant in service and $57,000 for accumulated depreciation related to its current Springfield service center, for a net rate base claim of $202,000. Henkes pf. at 11; exh. DPH-H, Sch. 19, pg. 2.

25. CVPS proposes to consolidate its current Springfield service center and a portion of its Ascutney service center into a new service center in North Springfield starting July of 1995. Henkes pf. at 10.

26. CVPS has proposed a pro forma rate base addition of $547,000 to reflect its projected investment for the new consolidated North Springfield service center as of July 1995. Henkes pf. at 10.

27. CVPS's proposed adjusted test year rate base not only includes the $547,000 rate base addition for the new consolidated North Springfield service center, but also the plant investment for the current Springfield service center which will be consolidated into North Springfield, effective July of 1995. This plant investment will no longer be used and useful upon the consolidation into North Springfield starting July 1995. CVPS may sell its current Springfield facility once the consolidation into North Springfield is completed. Henkes pf. at 11-12.

28. CVPS's proposed rate base must be reduced by $62,000 to remove the net plant in service associated with the current Springfield service center as of July 1995. Henkes pf. at 11-12; exh. DPH-H, Sch. 19 at 2.

Discussion re: Springfield Service Center

Two hundred and two thousand dollars of CVPS's net rate base investment will no longer be used and useful when the Springfield service center is consolidated into the North Springfield center and since CVPS has indicated that the current Springfield facility may be sold after its functions are moved to North Springfield. As with the Sunderland service center, we must reduce CVPS's proposed rate base by 4/13th (7/95-10/95) of the net rate base amount of $202,000, i.e., by $62,000. Henkes pf. at 11-12; exh. DPH-H, Sch. 19 at 2. CVPS proposes a pro forma rate base addition of $547,000 to reflect the plant addition for the new consolidated North Springfield service center as of July 1995. It has failed, however, to reflect the previously described $62,000 rate base reduction to remove the net plant investment for the current Springfield facility. CVPS's failure to remove this $62,000 net plant investment is an inappropriate double count. Therefore, CVPS's rate base must be reduced by $62,000. Findings 24-28.

I. Capital Expense

29. CVPS claims a pro forma rate base addition of $1,321,000 for common stock issuance expenses. Henkes pf. at 24.
These capital expenses represent expenses incurred by CVPS when it issues common stock and, as such, reduce the net common stock issuance proceeds received by CVPS from its stockholders.

Discussion re: Capital Expense

CVPS asserts that these common stock issuance expenses over the years have been incurred for the benefit of ratepayers, and although these costs do not get amortized, CVPS asserts that it would be appropriate to receive rate base treatment. Henkes pf. at 24.

Common stock issuance expenses are a permanent component of CVPS's capital stock account similar to other capital stock components such as common stock issued, premium on capital stock, other paid-in capital, and retained earnings. All of these components together represent the appropriate stockholder investment in CVPS. Henkes pf. at 24-25. CVPS has not cited and we are not aware of any Vermont electric utility that has been allowed to treat these costs in this manner in the past. Moreover, CVPS has not presented any evidence in this proceeding that would justify a change in this ratemaking policy. CVPS's claimed rate base addition of $1,321,000 for common stock issuance expenses is denied. Finding 29.

J. Working Capital Allowance

30. The working capital allowance consists of materials and supplies, net nuclear fuel, prepayments, accrued interest, ratios of various O&M expenses, and the accounts receivable sale. Based on these specific working capital allowance components, CVPS claims a total working capital allowance of $2,584,000, while the DPS recommends a total allowance of $2,684,000. Exh. RJH-1, Sch. 22 at 1, Rev. 9/15/94.

31. CVPS's claimed prepayment balance of $2,693,000 should be reduced by $656,000 to $2,037,000. Finding 7; CVPS Reply Brief at I-9.

32. CVPS's claimed accrued interest amount of $1,701,000 must be reduced to correct for a calculation error made by CVPS and must be recalculated based on the rate base and weighted cost of debt levels approved in this case. The appropriate accrued interest amount will be those calculated when the final rate base components are determined. Exh. RJH-1, Sch. 22 at 3, Rev. 9/15/94.

33. There are no real issues with regard to the remaining working capital allowance components (i.e., ratios of various O&M expenses and the $12,000,000 offset

for the accounts receivable sale). The DPS recommended amounts with respect to these remaining working capital allowance components differ from CVPS's proposed amounts because the DPS has determined different adjusted test year expense levels for purchased power, transmission, salaries/wages, and other operating expenses. This timing difference is not substantive. Henkes pf. at 29-30.

Discussion re: Working Capital Allowance

The DPS does not contest the specific working capital allowance methodology and components proposed by CVPS in this case. The DPS recommended working capital allowance amount of $2,684,000 is $100,000 higher than CVPS's originally proposed working capital allowance. This is the result of: (1) the correction for errors contained in CVPS's originally filed working capital allowance; (2) the "flow-through" effect of the Power Cost Stipulation in this case (findings58,59); and (3) the "flow-through" effect of adjustments to CVPS's originally proposed expenses for transmission by others, salaries and wages and other operating expenses. As previously discussed in Finding 7, CVPS concedes that its originally claimed prepayment working capital allowance component should be reduced by $656,000. The Company also made a calculation error in determining its originally proposed accrued interest balance of $1,701,000. Henkes pf. at 29. The correct accrued interest balance will be calculated by the results of the Board's final determination of cost in this docket. Findings 30-33.

K. Accumulated Deferred Income Taxes ("ADIT")

34. CVPS's originally filed rate base deduction for its proposed average adjusted test year ADIT is $40,486,000. Henkes pf. at 41.

35. CVPS's proposed average adjusted test year ADIT balance of $40,486,000 should be reduced by a total amount of $1,081,000 to an adjusted balance of $39,405,000. This adjustment allows for the "flow-through" effect directly associated with adjustments made by the DPS to certain of CVPS's proposed rate base and cost of service components. Henkes pf. at 41-42; exh. DPS-RJH-R-1, Sch. 24.

Discussion re: Accumulated Deferred Income Taxes

CVPS's originally proposed average adjusted test year ADIT balance of $40,486,000 should be adjusted to reflect the deferred tax impacts directly associated with ten adjustments to be made to certain CVPS's proposed rate base and cost of service

components.[12] The associated ADIT impacts of these rate base and cost of service adjustments are shown on Exh. DPS-RJH-R-1, Sch. 24. The appropriate ADIT balance to be reflected for ratemaking purposes in this case is $39,405,000. Findings 34, 35. This amount will be adjusted by the Company's compliance filing with respect to its ACE and C&LM cost of service and rate base impacts.

L. FAS 112 Unfunded Accruals

36. Similar to its treatment of accrued pension and accrued post-retirement expenses, CVPS, in its Rate Base Adjustment No. 58, incorporated a rate base reduction of $125,000 for the thirteen-month average effect of the pro forma unfunded FAS 112 liability. Pennington pf. at 19.

37. CVPS proposed a rate base deduction of $125,000 to reflect its proposed average adjusted test year unfunded accruals associated with OPEBs. This should be rejected. Henkes pf. at 73; see cost of service Findings 60-65 and related discussion on this topic.

Discussion re: FAS 112 Unfunded Accruals

We find that the DPS's recommendation to amortize the FAS 112 liability over 7.5 years is reasonable. To be consistent with our decision regarding FAS 112 expense ratemaking treatment, we reject CVPS's proposed rate base deduction of $125,000. Finding 37.

M. FAS 106 Unfunded Accruals

38. CVPS proposes that its negative 13-month average unfunded FAS 106 accrual balance of $598,460 be treated as a rate base addition. Henkes pf. at 63.

---

12. These ten rate base and cost of service adjustments include: (1) removal of 50 percent of Vernon Road Cap Bank ADIT; (2) removal of Pittsford Penstock ADIT; (3) removal of Cavendish Breaker ADIT; (4) removal of Consumer Information System ("CIS") Phase II and III negative ADIT; (5) removal of income tax rate change amortization ADIT; (6) removal of MIP-related negative ADIT; (7) adjustment for FAS 106 rate base adjustment; (8) adjustment for FAS 112 rate base adjustment; (9) adjustment for C&LM rate base adjustment; and (10) adjustment for ACE rate base adjustment. Henkes pf. at 41-42; exh. DPS RJH-R-1, Sched. 24.

39. In claiming this proposed $598,460 rate base addition, CVPS ignores the pre-adjusted test year unfunded FAS 106 accruals that have been and will continue to be accumulated on its books through October 1994. The Company takes this position because it believes, contrary to the DPS's position, that none of its per-books unfunded FAS 106 accruals accumulated through October 1994 have been collected in rates from the ratepayers. Henkes pf. at 63-64.

40. During 1992, CVPS recorded $450,000 of FAS 106 expense accruals on its books. Even with this expense deducted from stated earnings, CVPS's actual earned return on equity was 12.7 percent.[13] Henkes pf. at 66.

41. In December of 1992, CVPS made a one-time reserve booking for its Cleveland Avenue site which had the effect of reducing operating income by $4,900,000. CVPS's actual 1992 return on utility equity would have been 14.86 percent absent this reserve booking. Henkes pf. at 66.

42. On January 15, 1993, the DPS began an inquiry into the reasonableness of the retail revenues of CVPS for 1993. Central Vermont supplied and the DPS reviewed extensive cost of service data relative to 1993 and for the period 1994 through 1996. CVPS and the DPS also engaged in extensive discussions regarding this inquiry. Henkes surreb. pf. at 24-25.

43. On April 28, 1993, CVPS and the DPS jointly filed a stipulation (the "Docket 5651 Stipulation") with regard to CVPS's cost of service and retail rates. The Board approved this stipulation in Docket No. 5651. Docket No. 5651, Board's Order of 9/20/93; exh. DPS-F.

44. With respect to the Docket 5651 Stipulation, the DPS and CVPS agreed that no change in the Company's rates was then required. In addition, CVPS agreed to lower its return on equity from 12.5 percent to 12 percent, effective January 1, 1993, and to credit its DSM deferrals with any excess earnings over 12 percent. Id.; Henkes pf. at 66-67; Henkes surreb. pf. at 24-25.

45. During 1993, CVPS booked FAS 106 expense accruals of $1,085,000. CVPS, by its own calculations, earned 11.971 percent on its utility equity in 1993 and, therefore, seeks not to flow any DSM credits to the ratepayers as a result of excess returns on equity earnings. Henkes pf. at 67; Henkes surreb. pf. at 22-23.

46. CVPS's calculated 1993 utility return on equity of 11.971 percent incorporates the actual FAS 106 expense of $1,085,000 that was booked in 1993. Thus,

---

13. CVPS's Board-authorized return on equity during 1992 was 12.5 percent.

the $1,085,000 served to reduce CVPS's calculated 1993 return on equity number to 11.971 percent. Without the 1993 FAS 106 expense of $1,085,000, CVPS's actual return on utility equity, under its own calculation methodology, would have been 12.43 percent. Henkes pf. at 67; Henkes surreb. pf. at 23.

47. In accordance with the Docket 5651 Stipulation, a 1993 return on utility equity of 12.43 percent would have resulted in a ratepayer benefit through DSM credits of approximately the same amount as the 1993 FAS 106 expense of $1,085,000. CVPS has not proposed any such DSM credits; therefore, the Company's ratepayers have paid for CVPS's 1993 FAS 106 expense of $1,085,000. Henkes pf. at 67-68; Henkes surreb. pf. at 23; exh. DPS-F.

48. The Board's Order of September 20, 1993 approving the stipulation effectively "re-based" CVPS's retail rates as of January 1, 1993. In other words, even though rates did not change, CVPS's retail rates, from January 1, 1993 forward, are presumed to include a full recovery for all of CVPS's cost of service components, including CVPS's FAS 106 expense accruals. Henkes pf. at 67; tr. 7/8/94 at 178-179; Henkes surreb. pf. at 25; exh. DPS-F.

49. Because ratepayers have paid for all of CVPS's per-books unfunded FAS 106 expense accruals up until the November 1, 1994 start of the adjusted test year in this proceeding, CVPS's 13-month average adjusted test year unfunded FAS 106 accrual balance is $767,612. This balance should be treated as a rate base deduction for ratemaking purposes in this case. Henkes pf. at 64, 68; exh. DPH-H, Sch. 25.

Discussion re: FAS 106 Unfunded Accruals

The key question here is whether CVPS's actual per-books unfunded FAS 106 accruals up until the beginning of the adjusted test year represent expense accruals that have already been collected in CVPS's rates. CVPS asserts that none of those accruals accumulated through October 1994 have been collected in rates from the ratepayers. The DPS argues otherwise, recommending a rate base deduction of $767,612 which represents the adjusted test year's 13-month average positive unfunded FAS 106 accrual balance. Findings 38, 39; Henkes pf. at 64.

In 1992, CVPS booked FAS 106 expense accruals of $450,000, yet CVPS still earned 12.7 percent return on its utility equity. In December 1992, CVPS made a one-time reserve booking for its Cleveland Avenue site effectively reducing operating income by $4,900,000; CVPS's actual 1992 return on utility equity would have been 14.86 percent, absent this reserve booking.

In essence, it appears that CVPS used a FAS 106 charge against earnings in order to avoid a credit for DSM expenses that it would otherwise have provided to ratepayers. Finding 47. Having "charged" ratepayers for that decision in the past, CVPS cannot now persuade us that ratepayers should once again pay for these costs. In this regard, when a utility during a particular period does not earn a return that it believes to be reasonable, it has the option to file a rate case to correct for its under-earnings. Findings 40, 41.

With regard to CVPS's 1993 FAS 106 accruals of $1,085,000, we find, based on the evidence in the record, that CVPS's ratepayers have already paid for these FAS 106 expense accruals through October of 1994. In addition, as a result of the Board-approved Docket 5651 Stipulation, we conclude that CVPS's rates as of January 1, 1993 include recovery of FAS 106 expense accruals. CVPS's 1993 FAS 106 expense, which the Company started booking on January 1, 1993, represented a large and highly visible expense increase. The extensive cost of service information supplied by CVPS and reviewed by the DPS leading up to the Docket 5651 Stipulation included the FAS 106 expense. The Docket 5651 Stipulation and the subsequent Board Order approving that stipulation served to re-base CVPS's rates until such time that the Board conducts another rate case proceeding. Therefore, there was no reason for the Company's then current rates to change. Henkes surreb. pf. at 25; Findings 42-48.

CVPS argues that the ratepayers have not paid for the Company's 1994 FAS 106 expense accruals, noting that all 1994 earnings information available to management today indicates that the Company will not earn its authorized return on equity during the calendar year 1994. Pennington reb. pf. at 32-33. CVPS did not support this statement with any exhibits, workpapers, or calculations. In addition, there is no evidence in the record of this case to show what CVPS's appropriately calculated actual return on utility equity is for the twelve-month period ending October 31, 1994. Finally, as part of the Docket 5651 Stipulation, CVPS agreed not to file for a general rate increase that would become effective before August 1, 1994. Docket 5651, Order of 9/20/93 at 2. Thus, regardless of whether CVPS earned its authorized return on utility equity during the twelve-month period ending October 31, 1994, CVPS voluntarily agreed not to file for a rate increase with effective rates prior to August 1, 1994.

In summary, we reduce CVPS's average adjusted test year rate base by $767,612 to reflect CVPS's average unfunded FAS 106 expense accruals during the adjusted test year. Finding 49.

N. "Interim Period" Depreciation Reserve Growth

50. On April 22, 1994, the Vermont Supreme Court issued an order in Docket No. 92-353, involving certain appeals made by the DPS with regard to the various Board decisions in GMP's 1992 base rate proceeding, Docket No. 5532. That case held that GMP should have added the depreciation expense accruals on the 1990 test year embedded plant to its test year depreciation reserve. GMP had continued to book the depreciation expense accruals during the 1991 "interim year" as a "known and measurable" change, thereby resulting in an additional rate base deduction of $3,100,000. In re GMP, No. 92-353, slip op. at 2-8 (Vt. S. Ct. April 22, 1994); Motion to Reconsider denied, July 18, 1994.

51. CVPS's filing in this case did not recognize any interim period "known and measurable" depreciation reserve additions as an adjustment to its test year rate base. Henkes pf. at 14.

52. The "interim period" in this case represents the 10-month period between the end of the 1993 test year and the November 1, 1994 starting point of the adjusted test year. The DPS proposes to calculate the depreciation reserve growth as half the accumulated reserve growth during the "interim period" (i.e., 10/12ths of 1993 test year booked depreciation x 50 percent). Henkes pf. at 19.

53. The appropriate depreciation reserve growth to be reflected in the calculation determining the interim period adjustment for accumulated depreciation is $14,465,412. Pennington reb. pf. at 25; Henkes sur. pf. at 16.

54. Using the DPS approach, the "interim period" depreciation reserve should be increased by $6,027,255 to reflect the appropriate "interim period" depreciation reserve growth. Henkes pf. at 19; Pennington reb. pf. at 25; Henkes sur. pf. at 16.

Discussion re: "Interim Period" Depreciation Reserve Growth

This issue concerns growth in CVPS's depreciation during the "interim period" between the Company's proposed test year and the adjusted test year. This issue was the subject of the recent Vermont Supreme Court decision concerning the Board's decision in Board Docket 5532, a general rate case for Green Mountain Power Corporation. In that case, the Department argued for reducing a utility's rate base to account for "interim period" accumulated depreciation for the test year plant-in-service as a "known and measurable" adjustment to rate base. The positions of the parties and the facts of this case are similar to those in the GMP case in which the Vermont Supreme Court ruled in favor of the Department. In re GMP, No. 92-353, slip op. at 2-8 (Vt.S.Ct. April 22, 1994); Finding 50.

In this proceeding, the Department adjusts CVPS's rate base to include depreciation that has occurred during the "interim period" or the ten-month period between December 31, 1993 (at the end of the test year) and November 1, 1994 (the beginning the adjusted test year). The parties disagree about whether we should recognize "interim period depreciation" in this case, but there is no genuine dispute about the actual value of that amount.[14]

If we include an adjustment for accumulated depreciation during this period, both the Department and the Company conclude it should be appropriately set at $6,027,255; a value equal to 50 percent of the estimated increase in depreciation growth during the ten months between the end of the test year and the beginning of the adjusted test year. Pennington reb. pf. at 25; Henkes sur. pf. at 16; finding 54.

In its recent decision, the Court notes that "known and measurable" changes in plant investment are those changes that can be measured with a "reasonable degree of accuracy" and that "have a high probability of being in effect" in the adjusted test year. The Court accepted the Department's position that interim accumulated depreciation is that which is "'known and measurable' with absolute certainty." In re GMP, above at 3.

The Court further notes that once customers have, in effect, returned a portion of the utility's investment,

> they should not be required to pay for that portion a second time, once as depreciation expense and again as a return on plant value which had not been correspondingly reduced to reflect the "return of" the investment through depreciation expense payments.

In re GMP, above at 6.

Based on the Vermont Supreme Court ruling and based on the evidence presented by the Parties, we conclude that the Company's proposed adjusted test year depreciation reserve should be increased by $6,027,255 for ratemaking purposes in this proceeding to reflect the appropriate "interim period" depreciation reserve growth as a "known and

---

14. In its testimony and briefs, the Company objected to the addition of this $6,027,255 addition to the depreciation reserve, noting that the matter was still before the Vermont Supreme Court for reconsideration. Whatever the original merit of the CVPS argument, it cannot now carry any weight. This is because the matter is no longer before the Vermont Supreme Court. The motion to reconsider this decision was rejected by the Court. In re GMP, No. 92-353, slip op. (Vt.S.Ct. July 18, 1994).

measurable" adjustment.[15] This "interim period" depreciation reserve growth represents one-half of the appropriate depreciation expense accruals on CVPS's average 1993 test year embedded plant, which CVPS continues to book during the "interim period" January, 1994 through November 1, 1994. One half the value is appropriate in order to assure comparability between these additions and the average test year rate base to which these balances are being applied. Finding 52.

Upon deciding that we must recognize interim period depreciation, a secondary issue arises. The Company argues that if the Board accepts an "interim period" depreciation reserve growth adjustment, it should also accept, as an offset, the difference between the actual end of test year 1993 plant balances and the 1993 test year average plant balances. The Company argues that this would result in an additional plant investment of $2,509,000 for rate base additions during the test year that has not been included in the projected adjusted test year rate base. The Company also urges the Board to recognize an amount equal to one half the $10,440,000 that the Company maintains "will have been invested in non-growth related rate base by the end of the interim period." Pennington reb. pf. at 22.

In essence, the Company is requesting rate base recognition of an approximate additional $7,720,000[16] in rate base as an offset to the Department's request for an addition in accumulated depreciation during the 10-month interim period.

With respect to the inclusion of $2,509,000 for plant additions during the test year, the Company's argument is not persuasive. To include this amount would result in a mis-match of test year investment and revenues. The 1993 test year revenues reflected for ratemaking purposes in this case have been generated and supported by the Company's average plant-in-service during 1993. As the Department's witness Henkes notes, to consider the Company's year-end December 31, 1993 plant (which includes additional growth-related plant) without making a corresponding adjustment to restate and analyze the test year revenues based on test year-end load conditions is incorrect and inappropriate. Henkes sur. pf. at 13.

The Department also persuades us that CVPS's argument is inconsistent in that it fails to recognize the corresponding depreciation reserve and accumulated deferred

---

15. Increasing a depreciation reserve has the effect of reducing the rate base upon which a return is earned. Thus, an increase in the reserve results in a reduction in ultimate rates.

16. $2,509,000 for part of 1993 test year + 50 percent x $10,440,000 for 12 months in 1994.

income tax growth implicit in the difference between the end of year 1993 and average 1993 balances for these rate base deductions. The Company's increase in actual depreciation reserve balance on December 31, 1993, is even greater than the increased rate base requested by the Company and that increase is not reflected in the projected adjusted test year rate base. Henkes sur. pf. at 13.

The Company next argues for inclusion of the Company's 1994 six-month actual construction data and six-month capital forecast. CVPS values investments at an additional $10,440,000 in non-growth-related rate base by the end of the interim period, and states that this amount has not been reflected as an adjustment to the adjusted test year rate base. The Department objects to this $10,440,000 addition to plant-in-service on the grounds that it is a "late filing," entered "at the eleventh hour of this proceeding." Pennington reb. pf. at 21-22; Henkes sur. pf. at 14; DPS Brief at 30.

The Department also argues it was unable to verify the figure and that this figure cannot be relied upon because it was entered "without any supporting back-up information in the form of exhibits, workpapers, underlying work orders and associated cost/benefit analysis, and without ever before having been seen, reviewed or analyzed by the other parties." Henkes sur. pf. at 14; DPS Brief at 30.

The Company provides no support for the capital additions beyond the statements of a Company witness. More specifically, there are no exhibits, workpapers, underlying work orders and associated cost/benefit analysis that would enable either the Department or the Board to conclude that these investments are indeed interim period non-growth-related investments. As such, there is no firm basis for concluding that these investments are not already included as adjustments to test year plant in service in the Company's original rate request. Indeed, the testimony of the witness suggests that these amounts pertain to the entire twelve-month 1994 calendar year. It is therefore apparent that the figure extends well beyond the ten-month interim period and into the adjusted test year. We therefore conclude that this figure does not represent a "known and measurable" addition to plant in service during the interim ten-month period between December 31, 1993 and November 1, 1994.

We find the "late filing" argument to pose a difficult dilemma. On one hand, the text of 30 V.S.A. § 225 appears to exclude consideration of this offset, and Vermont PSB Rule 2.204 (G) expresses a similar principle. On the other hand, we note that in its recent decision, the Court was influenced by the fact that the relevant utility "had an ample opportunity to introduce evidence as to its adjusted test year additions to plant, and did not do so." In this case, the Court's decision was made on April 22, 1994, well beyond the filing of the Company's direct case on March 8, 1994, but in time to

introduce evidence during the later stages of this proceeding. Since we conclude that these interim period plant in service additions -- even if admitted into the record -- could not be accepted as a known and measurable adjustment to test year plant, it is not necessary to rule on the issue of whether the testimony on these investments constitutes a "late filing" prohibited by 30 V.S.A. § 225 and Vermont PSB Rule 2.204 (G).

In the future, we expect that the Department will continue its efforts to reflect interim period accumulated depreciation as a "known and measurable" adjustment to the rate base. Companies filing for rates may provide actual and projected plant investments as offsetting investments to match interim period accumulated depreciation balances, provided that these investments are fully supported with sufficient detail to meet the standards of "known and measurable" changes in the Company's plant investments based on the standards established by the Vermont Supreme Court.

O. Other Depreciation Reserve Adjustments

55. CVPS's proposed average adjusted test year accumulated depreciation reserve balance should be reduced by a total of $70,000 to reflect the "flow-through" effect directly associated with adjustments recommended by the DPS and approved by this Board to certain of CVPS's proposed rate base and cost of service components. Henkes pf. at 21; exh. RJH-1, Sch. 23, Rev. 9/15/94.

Discussion re: Other Depreciation Reserve Adjustments

CVPS's claimed average adjusted test year accumulated depreciation reserve balance must be reduced to reflect the depreciation reserve impacts of four adjustments to certain CVPS proposed rate base and cost of service components.[17] These adjustments are discussed under the corresponding Findings in this order. The associated depreciation reserve impacts of these four rate base and cost of service adjustments are shown on Exh. RJH-1, Sch. 23, Rev. 9/15/94. Finding 55.

V. COST OF SERVICE ISSUES

---

17. These four rate base and cost of service adjustments include: (1) removal of 50 percent of Vernon Road Cap Bank accumulated depreciation; (2) adjustment of CIS II and III accumulated depreciation; (3) removal of the Pittsford Penstock and Cavendish Breaker accumulated depreciation; and (4) Removal of FERC Hydro Projects accumulated depreciation. Exh. DPS RJH-1, Sch. 23, Rev. 9/15/94.

A. Power Cost Stipulation

56. CVPS's net power costs have increased from $96,800,000 in 1989 to $118,400,000 in 1993, an increase of $21,600,000 or 22.3 percent.[18] Over the same time period, peak demand increased from 410 MW to 418 MW, or an increase of 1.95 percent, and energy grew from 2,270,000 MWH to 2,417,000 MWH or 6.5 percent.[19] See 1989 and 1993 FERC Form I Reports. The increase in dollars per MWH from 1989 to 1993 is from $42.65/MWH to $48.99/MWH, respectively. Stein/Page pf. at 9; tr. 9/7/94 at 360; exh. CVPS RS-1 at 1; exh. Board-2.

57. CVPS's filed test year cost of service, adjusted for known and measurable changes and net of the Restructuring Savings Adjustment and Ceiling Adjustment, was $218,939,000. Frankiewicz pf. at 3.

58. The Board accepted a bottom-line stipulation ("Power Cost Stipulation") relating to the first five cost of service adjustments: (a) Purchased Power net of the various wholesale sales credits, (b) Production Fuel, (c) Millstone Net Deferral/Amortization, (d) Joint Ownership Costs, and (e) Transmission By Others, as well as certain O&M savings imputed by Department witness Henkes concerning several rate base plant-in-service additions (i.e., Glen Station Water Wheel, Milton #1 Transformer, Reconstruction St. Johnsbury/Lyndonville 34.5 Kv Line, Smith Sluice Gate and Fairfax Number Two Upgrade). Tr. 7/6/94 at 3-9, 106-113; Stein/Page pf. at 3-5.

59. Pursuant to this stipulation, the Company agreed to reduce the just described power costs by $2,550,000. CVPS's originally filed net purchased power expense amount of $101,308,000 is reduced by $2,550,000 to reflect the Power Cost Stipulation

---

18. Net power costs are power costs net of transmission by others, sales of system power to Connecticut Valley Electric Company, Inc. ("Conn Valley"), and other requirement sales. Tr. 9/7/94 at 360.

19. We hereby take official notice of the 1989 and 1993 FERC Form I Reports for the peak demand ("1989, 1993 FERC Form I Reports"), pursuant to 3 V.S.A. §810(4). CVPS and the DPS did not object during the September 13, 1994 hearing when the Board told the parties that it would be taking administrative notice of some of CVPS's FERC Form I reports. Tr. 9/13/94 at 264. Any party that wishes to comment on the Board's usage of that information as an exhibit in the official record of this Docket shall notify the Board of its objections by November 9, 1994.

approved by the Board during the hearing of July 6, 1994. Id.; exh. RJH-1, Sch. 1, Rev. 9/15/94.

Discussion re: Power Cost Stipulation

Cost of Service Adjustments One through Five increase test year cost of service by $7,483,000. These power cost issues are related to Purchased Power net of the various wholesale sales credits, Production Fuel, Millstone Net Deferral Amortization, Jointly-Owned Operations and Maintenance Expense, and Transmission by Others and Rate Base Adjustments 30 through 34 and 36 through 40. Finding 58. The Department initially proposed a reduction of approximately $3,800,000 relating to these adjustments.

The Department and CVPS jointly filed a stipulation reflecting a settlement of all such power cost issues. The two parties stipulated to a bottom-line $2,550,000 net reduction, attributable to these adjustments. The Board accepted that stipulation. Finding 59.

B. Other Post-Employment Benefit Expenses (FAS 112)

60. Prior to 1993, CVPS accounted for its other post-employment benefit ("OPEB") expenses based on the pay-as-you-go method. However, Statement of Financial Accounting Standards No. 112 (FAS 112) now requires companies to use the accrual method for the recording of their OPEB expenses. Henkes pf. at 69.

61. In compliance with FAS 112, CVPS began to book its OPEB under the accrual method effective January 1, 1994. Henkes pf. at 69.

62. The changeover to the FAS 112 accrual method for CVPS's OPEB liabilities has created a one-time Transition Benefit Obligation ("TBO") of $771,967. The Company proposes to amortize its FAS 112-related TBO over a three-year period. Henkes pf. at 70; Pennington reb. pf. at 39; Henkes surreb. pf. at 30-31.

63. CVPS's originally proposed adjusted test year expense level for OPEBs was approximately $303,000. In response to discovery by the DPS, CVPS concedes that it had erroneously overstated this expense level by $35,000. Henkes pf. at 71; Pennington reb. pf. at 39.

64. CVPS's three-year amortization period for the TBO portion of its FAS 112 liability serves to increase its FAS 112 expense by 136 percent over the FAS 112 expenses currently reflected in rates. Henkes pf. at 72; Henkes surreb. pf. at 29.

65. The DPS's recommended FAS 112 expense amount of $113,848 is equal to the FAS 112 expenses currently reflected in rates. Henkes surreb. pf. at 28-29.

Discussion re: Other Post-Employment Benefit Expenses (FAS 112)

Financial Accounting Standard 112 addresses "Other Post-Employment Benefit Expenses" ("OPEBs"). These represent long-term disability and medical benefits for former or inactive CVPS employees prior to their retirement. Since 1993, FAS 112 has required companies to use the accrual method to account for their OPEBs. The change to an accrual accounting method for the OPEBs has created a "Transition Benefit Obligation" ("TBO") for CVPS, yet there are no rules applicable to FAS 112-related TBO. The Company proposes to amortize its FAS 112-related TBO over a three-year period. Henkes pf. at 69-70; Findings 60, 61, 62.

Both CVPS and the DPS are proposing full rate recognition for the entire FAS 112 liability determined by CVPS in this case. The only difference between CVPS's and the DPS's positions is that CVPS has proposed to amortize the TBO portion of the FAS 112 liability over three years whereas the DPS has recommended a 7.5 year amortization for the TBO. Henkes surreb. pf. at 28.

In support of its recommendation, the DPS points out that CVPS stated in its rebuttal testimony that it does not profess that a three-year amortization for the FAS 112 TBO is a "magic number". CVPS added that it may be entirely appropriate to amortize the TBO over a four-or five-year period and achieve similar results. Pennington reb. pf. at 42.

More importantly, the Department states that its proposed 7.5 year amortization period would match the adjusted test year OPEB expenses under FAS 112 to the test year OPEB expenses under the previously applied pay-as-you-go method. Thus, this amortization period would remove the initial rate impact of FAS 112 on current ratepayers without being punitive to CVPS's shareholders. Henkes pf. at 72; Findings 64, 65.

We find that the DPS's recommendation is reasonable and reject CVPS's proposed rate base deduction of $125,000. Finding 37.

C. Management Incentive Program Expenses

66. Central Vermont proposes an adjusted test year Management Incentive Program expense of $201,300. This expense represents the 1993 test year per-books Management Incentive Program expense of $231,319 reduced by $30,019 for expenses related to three officers who are no longer employed at CVPS. Henkes pf. at 50.

67. The Company's Management Incentive Program allows its officers an opportunity to earn incentive payments as a reward for having contributed to successful corporate performance. The Company determines the degree of "successful corporate

performance" and subsequent award payment by comparing the actual results achieved in certain selected corporate performance areas during a particular year to the targets set for these corporate performance areas at the beginning of that year. These corporate performance areas, each of which carries a weighing factor of approximately 33 percent, consist of:

(1) O&M expenses and DSM efficiencies;
(2) the return on equity for CVPS's regulated utility operations; and
(3) customer satisfaction levels.

Henkes pf. at 50-51.

68. CVPS awards a bonus payout to employees even if 100 percent of the goal is not achieved. This is because the Company uses a payout range. A range is used rather than an absolute target in order to create the incentive for management to drive towards the goal even when there is little likelihood of fully achieving it. Chouinard reb. pf. at 6.

Discussion re: Management Incentive Program Expenses

CVPS gives an incentive component to its managers in order to further significant corporate objectives; it asserts that most businesses do so. For this purpose, CVPS proposes an adjusted test year Management Incentive Program expense of $201,300. Finding 66.

CVPS contends that it would be inappropriate to disallow its Management Incentive Program costs in their entirety. CVPS states that its Management Incentive Program focuses primarily on the best interests of customers, noting that two of the three criteria focuses on customers (including energy efficiency), with the final criterion focusing on shareholders. Finding 67; CVPS Brief, Vol. I at 32.

The Company also is against equally sharing the cost of the Management Incentive Program between shareholders and customers. CVPS points out that although the Board approved of a 50-50 sharing of costs in GMP's last fully litigated rate case, GMP uses only one criterion —— return on equity —— without any criterion addressing the concerns of customers. Id.; Chouinard reb. pf. at 6.

CVPS wants the recognition of the entire amount of its proposed adjusted test year Management Incentive Program expense. CVPS states that it serves a useful purpose, and it is in the best interest of its customers. Moreover, CVPS notes that there is no evidence that its incentive criteria are inappropriate, nor any evidence that the Company did not set standards of performance high enough. However, as an alternative, CVPS

would support an allocation of the expense on the basis of its criteria —— two-thirds to customers and one-third to shareholders. CVPS Brief, Vol. I at 32.

The DPS argues for the disallowance of the entire amount of CVPS's proposed Management Incentive Program award expenses based on four primary arguments. First, the DPS notes that CVPS is simply assuming that the adjusted test year's performance targets and measured success in meeting those targets will be exactly the same as in 1993. The DPS contends that the corporate performance targets for the adjusted test year and the actual corporate achievement based on CVPS's specific performance criteria are not known and measurable at this time. Henkes pf. at 51-53; Henkes surreb. pf. at 41.

Second, a properly designed Management Incentive Program should have as its objective to improve management's performance over previous performance levels. This, in turn, would lead to improved corporate performance with a direct benefit to ratepayers and shareholders. Simply assuming the same level of Management Incentive Program award expenses for the adjusted test year as it experienced during the 1993 test year does not contain that incentive. DPS Brief at 43-44.

Third, the Department acknowledges that the record does not prove that CVPS's Management Incentive Program performance standards are easily achievable; however, it argues that there is also no evidence indicating that CVPS's Management Incentive Program performance standards are truly challenging. The Company has presented no evidence with regard to any details of its Management Incentive Program performance targets, the degree of difficulty and challenge inherent in these targets, and whether its established year-to-year performance standards were designed in such a way that meeting these standards would result in year-to-year management and corporate performance improvements. Given the Company's ultimate burden of proof, the DPS asserts that the lack of evidence on either side suggests that disallowance is proper. Henkes surreb. pf. at 40-41.

Finally, the DPS states that CVPS's Management Incentive Program payout ratios have varied significantly from year-to-year during the last nine years. This is another indication that CVPS's Management Incentive Program award expenses during the adjusted test year could be significantly different than its 1993 test year expense level. Henkes surreb. pf. at 41; exh. CVPS JAC-R4.

We have previously observed that cost-sharing of a "plan that encourages better management should be borne by all those who share its benefits". Docket 5428, Board's Order of 1/4/91, at 60. CVPS has not demonstrated a persuasive basis for changing this policy. Both shareholders and ratepayers benefit equally from a well managed utility; thus, they are to share equally the costs of CVPS's management program. This means a

continuation of the Board's policy of a 50-50 split of appropriate Management Incentive Program expenses.

The DPS points out that the Management Incentive Program payout ratios have varied greatly over the past nine years. Because of this, the DPS argues that the Management Incentive Program expense for the adjusted test year is unlikely to equal that of the test year. We agree and conclude that because of this variability, the preferred measure of Management Incentive Program ratios would be an average derived from several prior years. However, in this case, the record does not contain the past nine years of Management Incentive Program expense data which could have allowed for an averaging of the Management Incentive Program expense over a period of time. Thus, in this case, we will start with the filed management incentive plan test year expense level of $206,300. For cost of service purposes, this must be adjusted by assigning one half of the costs to shareholders, leaving $100,650 assigned to ratepayers.

D. Distribution Contract Tree Trimming

69. CVPS projects its annual distribution contract tree trimming expenses using a "formula-generated" approach. CVPS first determined a baseline using the year 1986. Applying a "distribution line mile" formula, CVPS calculated a tree trimming budget for 1986 at $2,600,000. CVPS then calculates succeeding years' budgets by adjusting the 1986 tree trimming budget for assumed 5 percent inflation and 1 percent system growth factors. Henkes pf. at 74.

70. CVPS's actual tree trimming expenses for each year of the past five years were lower than the projected tree trimming expenses resulted from CVPS's "formula-generated" budget approach. On average, the Company's actual annual tree trimming expenses during the most recent 5-year period have been $333,000 below CVPS's claimed "formula-generated" budgeted levels. Henkes pf. at 74-75.

71. Due to the discretionary nature of tree trimming expenses, CVPS's management makes the actual budget decisions for tree trimming on a year-by-year basis. Henkes pf. at 75.

72. CVPS's "formula-generated" tree trimming budget for 1994 is $4,031,000 and for 1995 is $4,275,000. Henkes pf. at 74, 76.

73. CVPS management has decided upon a tree trimming budget for 1994 of $3,521,000 which is $510,000 lower than the "formula-generated" budget for that year. Henkes pf. at 76.

74. CVPS's proposed adjusted test year tree trimming budget is $4,048,250, representing 2 months (2/12th) of the actual 1994 budget of $3,521,000 and 10 months

(10/12th) of the "formula-generated" 1995 budget of $4,275,000. Dickinson pf. at 2; Henkes pf. at 76.

Discussion re: Distribution Contract Tree Trimming

CVPS claims a tree trimming expense of $4,048,250 for the adjusted test year. The Company notes that the principle item driving the cost of the program is that contractor rates have increased 15 to 20 percent since 1991. Findings 69, 71, 72, 74; Dickinson pf. at 2-3.

The DPS opposes CVPS's use of its formula to generate the tree-trimming budget for the adjusted test year. The DPS asserts that CVPS has failed to establish that its initial "formula-generated" budgeting approach to project its annual tree trimming expenses is a reliable method to accurately measure the level of expenditures to be expected in the future. The DPS refers to CVPS's actual tree trimming expenses for the years 1989 to 1993, which have been significantly lower than the "formula-generated" budgeted levels for those years. The DPS also notes that CVPS management reduced the 1994 "formula-generated" budget by $510,000 or 13 percent. Findings 70, 73.

The DPS recommends an adjusted test year tree trimming expense level of $3,639,000. The Department derived this expense level by: (a) combining 2 months (2/12th) of the final "management-decided" 1994 budget of $3,521,000 with 10 months (10/12th) of the final "management-decided" 1994 budget of $3,521,000, and (b) adjusting this amount using a 4 percent inflation factor. Henkes pf. at 77; exh. DPH-H, Sch. 7.

We are persuaded by the DPS that CVPS's "formula-generated" annual tree trimming budgets have not matched the Company's ultimate "management-decided" budgets or actual expenditure levels. We find CVPS's "formula-based" method of estimating annual tree trimming budgets an unreliable determinant of actual tree trimming expenses. Instead, for ratemaking purposes, CVPS's adjusted test year tree trimming budget must be based on the approach recommended by the DPS. The appropriate adjusted test year tree trimming expense for ratemaking purposes in this case is $3,639,000. By including that amount in cost of service, we expect the Company to spend these funds on line clearing and to do so in a regular and cost-effective manner. Docket 5372, Order of 5/31/90 at 28.

E. Expense Savings - Sunderland and Springfield Service Centers

75. CVPS's adjusted test year cost of service includes incremental O&M expenses, depreciation expenses, property taxes, and insurance expenses directly

associated with its proposed pro-forma plant in service additions for the new consolidated service centers at Sunderland and North Springfield. Henkes pf. at 84-85.

76. CVPS failed to remove from its adjusted test year cost of service $31,279 worth of depreciation expenses, rent expenses, property taxes, and insurance expenses directly associated with the current Manchester, Bennington, and Springfield service centers. These service centers will be consolidated into the new Sunderland and North Springfield service centers and will no longer be used and useful at that time. Henkes pf. at 85-86; exh. DPS-H, Sch. 9 at 2.

Discussion re: Expense Savings - Sunderland and Springfield Service Centers

CVPS's proposed adjusted test year cost of service includes expenses not only for the two new consolidated service centers at Sunderland and North Springfield, but also for the current three service centers that will be replaced by the new consolidated ones. At the time of such replacements, CVPS will no longer incur the total expense of $31,279, which is included in CVPS's proposed adjusted test year cost of service. Finding 75, 76.

Therefore, CVPS's claimed adjusted test year cost of service must be reduced by $31,279.

F. O&M Expense Savings Associated with Basic Records and Work Order Management

77. CVPS proposes pro forma adjusted test year plant in service additions for the Basic Records and Work Order Management Phases One through Four projects. Yet, CVPS has not recognized associated cost savings generated by these rate base additions. Henkes pf. at 82-84.

78. As part of the work orders for the Basic Records and Work Order Management Phases One through Four projects, CVPS performed cost/benefit analyses indicating that these rate base additions would generate substantial cost savings. Henkes pf. at 82, 84.

79. CVPS's performed cost/benefit analysis for the Basic Records rate base addition indicates annual cost savings from this project ranging from a low amount of $103,000, to a medium amount of $155,000, and to a high amount of $206,000. Henkes pf. at 82.

80. CVPS's performed cost/benefit analysis for the Work Order Management Phases One through Four projects identifies $600,000 as annual cost savings that could be expected from the implementation of those projects. Henkes pf. at 84.

81. The DPS's recommended cost savings adjustments to CVPS's proposed cost of service is a "compromise" position, consisting of removing $103,000 (half of $206,000 or the low estimate) for Basic Records and $300,000 (half of $600,000) for the Work Order Management Phases One through Four projects for a total adjustment of $401,000. Henkes pf. at 83-84.

82. The savings associated with Basic Records and Work Order Management as reflected in those work order cost/benefit analyses were estimated labor or payroll savings that were projected to result from the implementation of those systems. These savings were projected at the time CVPS prepared the analyses which had not been updated or required updating since that time. Tr. 7/8/94 at 205.

83. Those savings, particularly with respect to Work Order Management, relate to employees that are not leaving CVPS because of the restructuring plan. Tr. 7/8/94 at 205-208.

Discussion re: O&M Expense Savings Associated with Basic Records and Work Order Management

The DPS recommends that the Board reduce CVPS's proposed cost of service by $403,000 in order to reflect the cost savings generated by the rate base additions of Basic Records and Work Order Management. Finding 81.

The DPS states that CVPS's cost/benefit analyses associated with its proposed rate base additions for the Basic Records and Work Order Management Phase One through Four projects show that these rate base additions will result in substantial cost savings. The Department notes that CVPS makes its resource acquisition decisions based on these cost/benefit analyses. If the results of such cost/benefit analyses cause CVPS's management to make important and expensive resource acquisitions, the DPS contends that these same cost/benefit results can and should be used to set rates for the resource acquisitions. Findings 78, 79, 80.

CVPS disagrees with the Department's recommendation. The Company asserts that the level of payroll and benefit costs incorporated in the adjusted test year cost of service has already reflected all known and measurable payroll and benefit savings associated with staffing level changes that may result from these projects. The Company states that during the past year, the Company has undergone an extensive review of its man-power requirements across the entire organization as part of its restructuring plan, including the functional areas from which both Basic Records and Work Order Management savings would originate. CVPS contends that to the extent any man-power savings would materialize in these functional areas during the adjusted test year, they

have already been reflected in the Company's restructuring savings adjustment. Thus, the Company argues that to adopt the DPS's recommendation would be confiscatory, in that the same savings, payroll, and benefits would be imputed twice. Pennington reb. pf. at 9-12; CVPS Brief, Vol. I at 63.

CVPS makes reference to a recent GMP rate case, where the DPS challenged computer and equipment additions to rate base because the Company did not offer a cost-benefit analysis to demonstrate why such additions are needed to serve test year needs. CVPS notes that, in that case, the Board rejected the DPS's arguments:

> In conjunction with many of its resource acquisition decisions, a utility will conduct thorough assessments, including cost-benefit analyses of the various alternatives it faces. A cost-benefit analyses will, given certain assumptions, identify the most cost-effective resource to acquire. However, not all resource decisions are susceptible to easy quantification, and we rely on management's judgment in many cases. In addition, we cannot conclude that the savings resulting from increased worker productivity are not reflected in the *pro formed* cost of service. Such savings are generally reflected in the absence of additional workers, less efficient computers, etc.

Tariff filing of Green Mountain Power Corporation requesting a 15.69% increase in rates, to take effect June 4, 1990, Docket 5428, Order of 01/04/91 at 31; CVPS Brief, Vol. I at 64.

We find circumstances in this case substantially different from those in the GMP case. CVPS had conducted benefit-cost analyses. CVPS had informed the Department that there are cost savings associated with these computer additions that are not reflected in the Company's rate year estimates.[20] However, CVPS had stated that it had not prepared any additional information to update that analysis. Finding 82.

---

20. In response to a Department interrogatory in Docket No. 5701, CVPS stated with respect to the Basic Records project and associated annual cost savings:

> The software system is in service, however manual data conversion, training, and interim data backlog are being conducted centrally in the Plant Accounting Department. System responsibilities are being transferred to the districts one at a time, as these activities are completed. *The anticipated first year savings associated with this project are not reflected in the rate year* [a rate year ending October 31, 1994].

Henkes pf. at 82-83 (emphasis added).

Although CVPS asserts that the cost savings are already reflected in its restructuring cost of service adjustment, the savings, particularly with respect to Work Order Management, relate to employees that are not leaving CVPS. Finding 83.

We conclude that CVPS has not accounted for the cost savings from these rate base additions. We, therefore, adopt the expectation included in the Company's own justification for this equipment; this reduces CVPS's proposed cost of service of the Basic Records rate base addition and Work Order Management Phases One through Four by the projected cost savings of $206,000 and $600,000, respectively, for a total reduction of $806,000. Findings 79, 80.

G. Account 931 Rent Expenses

84. CVPS's account 931 rent expenses were $665,253 for 1991, $642,427 for 1992 and increased to $939,870 for the 1993 test year. Henkes pf. at 87.

85. CVPS claims its adjusted test year account 931 rent expense level will be at the same level of $939,870 as during the 1993 test year; yet the Company's own budget indicates that its account 931 rent expenses for the adjusted test year will be $781,891. Henkes pf. at 87.

86. CVPS has identified savings associated with certain computer systems projects. The following computer systems provide a total savings of $173,113:

Client/Server Implementation:	$50,235	(software)
Network Infrastructure:	94,878	(hardware & software)
AS/400 replacement:	28,000	(lease & property tax)
TOTAL:	$173,113	

Exh. DPS-EFR-1; tr. 8/19/94 at 105-106.

87. CVPS anticipates converting to a client/server computer platform by the end of 1997.[21] As a result of this project, CVPS has eliminated $47,535 of software costs from the test year Cost of Service Adjustment No. 27 —— Operations and Maintenance ("O&M") Expense/Savings.[22] Pennington pf. at 14.

---

21. The Client/Server project is to replace the Company's mainframe computer systems and the AS/400 computer system. The project includes all the hardware and software necessary to implement corporate critical systems on a client/server platform. Pennington pf. at 14.

22. CVPS states that the anticipated savings from the conversion to the client/server platform are associated with "reduction in batch processing, movement to on-line, real-time applications, reduction

88. The Network Infrastructure is scheduled to be placed in service in March 1995.[23] As a result of this project, CVPS has eliminated $89,779 of hardware and software costs from the test year in the Cost of Service Adjustment No. 27.[24] Pennington pf. at 16.

89. The conversion to the client/server environment will result in replacement of the current C&LM Monitoring and Evaluation application for the AS/400. Replacing the AS/400 results in the elimination of $25,301 in lease and property tax costs from the test year in Cost of Service Adjustment No. 27. Pennington pf. at 16.

Discussion re: Account 931 Rent Expenses

CVPS supports an Account 931 rent expense of $939,870. CVPS states that its budgeted rent expense of $781,891 reflects the $173,113 in capital lease savings associated with the Client/Server Implementation, Network Infrastructure, and AS/400 replacement, and that these cost savings are already reflected in CVPS's Cost of Service Adjustment No. 27 —- O&M Expense/Savings. The Company states that if the Board accepts the DPS's proposed adjustment, the rent savings would be reflected twice in the cost of service. Findings 84, 86; Ryan reb. pf at 3-4; exh. DPS-EFR-2.

The DPS recommends an adjusted test year Account 931 rent expense of $784,891. The DPS notes that the Company's budget shows this rent expense level for the adjusted test year. Finding 85.

---

in hardware and software maintenance and licensing fees, faster and more flexible development through package purchases and modification or in-house development, reduced hardware upgrade costs, and relative vendor independence". Pennington pf. at 14.

23. This project includes all the network hardware, network software, server hardware, server software, and support services required to build the network. Pennington pf. at 15.

24. The primary benefits of this network include "more effective utilization of existing software and hardware, prospectively lower ISD (CVPS's Information Systems Department) and software costs, faster application development, more responsive applications, improved timeliness and quality of information, better integration of applications, reduced data redundancy, and easier to use, more intuitive applications." Pennington pf. at 16.

The DPS also showed that CVPS has not presented any documentation to support its position that the capital lease savings attributable to computer replacement are already reflected in its filed cost of service. Although CVPS has specified cost savings after converting to the client/server platform, the Company does not offer any clear evidence to demonstrate that the client/server will result in Account 931 rent expenses. Similarly, CVPS does not offer evidence that the Network Infrastructure or the AS/400 replacement will result in Account 931 rent expenses. Findings 87, 88, 89; tr. 8/19/94 at 106-107, 109-112; exh. DPS-EFR-2.

We find that the evidence on the record does not demonstrate that CVPS's filed cost savings for the Client Server, Network Infrastructure, and AS/400 replacement specifically consist of Account 931 rent expense savings. Therefore, CVPS's proposed adjusted test year Account 931 expense level of $939,870 is to be reduced by $157,979 to $781,891.

H. Advertising Expenses

1. Vermont Educational Television ("ETV")/Vermont Public Radio ("VPR")

90. CVPS proposes an adjusted test year advertising expense of $17,468 for its Vermont ETV/VPR advertising campaign —— a campaign that places advertising messages on the public television station, ETV, and the public radio station, VPR. Exhs. CVPS-JSG-1, DPS-H, Sch. 11.

91. The Vermont ETV/VPR advertisement campaign consists of advertising messages surrounding two programs on ETV and a public affairs commentary series on VPR. Griffin pf. at 4.

92. The credit which ran on Vermont ETV shows a billboard of the Company's Efficiency Plus logo with the following voice-over/tag-on: "broadcast of (program name) on Vermont ETV is funded in part by Central Vermont Public Service Corporation, offering Efficiency Plus programs and services to customers throughout Vermont." The tag-line for the VPR commentary series was very similar. Giffin pf. at 3.

93. The Board's Order in Docket 5372 established criteria for utility advertising expenses recoverable through rates. The criteria include: promoting safety, informing customers about utility services, lowering costs through demand-side management, or satisfying administrative or legal needs. Advertising intended simply to boost the utility's sales or to enhance its corporate image is not properly chargeable to ratepayers. Docket 5372, Order of 5/31/90 at 25-26; tr. 7/8/94 at 98 (Henkes).

2. Water Heating

94. CVPS proposes a cost of service inclusion of $2,777 for water heating advertising. Exh. DPS-H, Sch. 11.

3. "It Was Cold" Campaign

95. CVPS proposes to share equally the $4,282 cost of its "it was cold" campaign between its stockholders and ratepayers. The amount proposed for the cost of service is $2,141. Exhs. CVPS-JSG-1, DPS-H, Sch. 11.

96. "It was cold" was a newspaper campaign in which the Company thanked its customers for reducing their electrical use when a main power transformer failed at the Vernon Road substation in Brattleboro during the cold weather in February, 1993. The transformer had failed because a transmission line failed and fell onto another transmission line, causing a short circuit. Exh. CVPS-JSG-13.

4. Economic Development

97. CVPS's economic development advertising campaign features the theme "Vermont, We're Open For Business". CVPS spent $129,067 on this campaign during the 1993 test year. Although much of the $129,067 was for the preparation of advertising, which was a one-time expenditure that would not recur for the adjusted test year, CVPS proposes to include the same amount in its adjusted test year cost of service. CVPS notes that in 1993, the advertisements ran for only three months. The Company plans for additional months of placement for the adjusted test year. Henkes pf. at 90-91; tr. 8/19/94, Vol. I at 77.

98. The $129,067 spent on economic development advertising during the 1993 test year is comprised of $86,866 in television advertising, $26,546 in print advertising, and $15,655 in administrative expenses. Exh. CVPS-JSG-1.

99. CVPS airs its economic development television advertising during the seasons of high tourist activity. Tr. 8/19/94, Vol. I at 74-75.

100. CVPS tracks and responds to inquiries resulting from all of its economic development advertising activities. Exh. CVPS-JSG-R2; Giffin reb. at 5-6.

101. As to those respondents listed in its recruiting analysis that indicated the television medium as their source of information, CVPS could not present any evidence that any had actually relocated to Vermont or expanded an in-State facility. Tr. 8/19/94, Vol. I at 75-76.

5. Efficiency Plus/Conservation and Load Management ("C&LM"), District Efficiency, and "It's Happening" Advertising

102. CVPS originally reported the following breakdown of expenses in support of its Efficiency Plus/C&LM, District Efficiency, and "It's Happening" advertising during 1993[25]:

Program Expense	Amount	Of that Amt. Using TV
Efficiency Plus:	$187,139	$167,085
It's Happening:	5,951	0
District Efficiency:	2,391	0

Exh. CVPS-JSG-1.

103. CVPS uses a "multi-faceted" approach (that is, integrated to extend beyond just television) to encourage customer participation in its energy efficiency programs. CVPS's approach contains both program-specific and general educational components. The campaign is designed to promote "Efficiency Plus" and establish CVPS as a "knowledgeable, professional source of expertise and customer assistance when it comes to efficiency." Exh. CVPS JSG-R-8 at 1; tr. 8/19/94, Vol. II at 9-10.

104. CVPS is proposing to reduce its expenditures on energy efficiency programs in the adjusted test year by approximately forty percent and reduce participation by five percent, but is seeking to include in rates the same amount of expense for advertising its energy efficiency programs. Tr. 7/8/94 at 340-342; 9/6/94 at 196-200.

105. CVPS reports that $167,085 or 89 percent of its Efficiency Plus/C&LM program advertising budget was spent on television advertising. CVPS also reports that $5,951 was spent for the non-television costs of the "It's Happening" campaign. Giffin pf. exh. JSG-1 at 1.

---

25. The DPS reports that CVPS is seeking rate recovery of $184,774 spent in support of the following advertising campaigns:

Efficiency Plus:		$176,762
It's Happening:		5,621
District Efficiency		2,391
TOTAL	$184,774	

Owen pf. at 2; exh. DPS-H, Sch. 11; tr. 7/8/94 at 320. The Company did not challenge the slightly different estimates presented by the DPS at the hearings and cited in finding 102, above. Our discussion assumes that, for overall ratemaking purposes, CVPS's reported Efficiency Plus advertising campaign of $187,139 would not be materially different from the amount of $176,762 provided by the DPS. Exh. CVPS-JSG-1.

106. CVPS's television advertising on energy conservation could, at best, be characterized as "educational" in nature, featuring energy quizzes that were not clearly linked to the Company's energy efficiency programs that offer products and services to customers. Owen pf. at 6-7; tr. 7/8/94 at 328.

107. Other Vermont utilities have conducted successful DSM programs with low-cost marketing, relying primarily on newsletters and other economical advertising techniques. GMP and BED have experienced higher penetration rates than CVPS with respect to residential programs that market energy efficiency products such as compact fluorescent lightbulbs and showerheads, yet those utilities do not use television advertising. Tr. 7/8/94 at 357; 8/19/94, Vol. II at 33-34; 8/31/94 at 194-196.

108. Print and radio advertisements omitted the Company's telephone number, creating a barrier for customers wanting to respond. Tr. 7/8/94 at 337-338.

109. District Efficiency advertisements are ads placed by the Company's district managers in local publications and are typically of a sponsorship nature, such as the Knights of Columbus or a program for a local sporting event. Owen pf. at 8.

Discussion re: Advertising Expenses

Vermont ETV ("ETV")/Vermont Public Radio ("VPR")

CVPS asserts that it is reasonable and prudent for the Company to advertise on Vermont ETV and VPR, citing, as one reason, that ETV is the second most watched television station in the State. The Company also notes that advertising on these stations allows the Company to reach an audience with demographics which other media may not reach. Findings 90, 91; Giffin pf. at 5; Giffin reb. pf. at 30.

CVPS further asserts that the Efficiency Plus advertising conducted by the Company through the ETV and VPR programs does not constitute "image advertising", as it is different from the previous Company advertising on these stations. CVPS points out that it now includes a tag-line with a specific message promoting Efficiency Plus programs (a series of programs designed to save the customer and the Company money) and is part of an integrated campaign to get that message out to customers. Finding 92; tr. 07/05/94 at 281-282.

The DPS contends that the advertising expense for Vermont ETV/VPR should be removed from cost of service. The DPS asserts that this represents corporate image advertising, and should not be charged to the ratepayers under the ratemaking advertising policy that was established by the Board in Docket 5372. Henkes pf. at 88-90; findings 93, 109.

The DPS also notes that in GMP ratemaking proceedings, Dockets 5372 and 5428, the Board specifically ruled that ETV/VPR advertising did not meet the established criteria for rate inclusion. Pursuant to these prior Board rulings, GMP did not include its ETV/VPR advertising expenses in cost of service in its two subsequent rate proceedings, Dockets 5532 and 5695. Henkes pf. at 89-90.

The DPS's arguments are persuasive; we conclude that the $17,468 in advertising expense for Vermont ETV/VPR must be removed from cost of service.

Water Heating

The DPS does not support the CVPS's $2,777 water heating advertising expense. The Department asserts that the primary purpose of CVPS's water heating advertising is to promote electric water heating options. The Department notes that the advertising has direct benefits for the Company's non-regulated subsidiary, SmartEnergy, whose main product is the leasing, selling, installing, and servicing of water heaters. It also serves to increase CVPS's sales of energy. Finding 94; Henkes pf. at 90. Henkes surreb. pf. at 44-45.

We agree with the DPS that there are some obvious benefits for CVPS's non-regulated subsidiary, SmartEnergy, from promoting water heating options. We find that these are benefits that the ratepayers should not pay for. We find it appropriate to disallow half of the $2,777 water heating advertising expenses or $1,389 due to the water heating advertisement's direct benefit to SmartEnergy.

The record, however, contains some evidence that identifies potential benefits associated with *well-managed* water heating load control efforts for the Company's ratepayers, such as lower rates from a greater efficiency in the use of the utility's system and from a greater contribution to fixed costs. Tr. 9/2/94 at 142-143, 151-152, 254; tr. 9/13/94 at 115-116. Because of pending dockets addressing the benefits and costs associated with fuel-switching and water heating alternatives —— Docket 5270-CV1&3 and Docket 5686 —— we will avoid prejudging this issue and not base a total disallowance upon this issue at this time.

"It Was Cold" Campaign

The DPS argues that the $2,141 cost of the "it was cold" campaign should be disallowed because this advertising fails to meet the Board's criteria for rate inclusion. Findings 95, 96; Henkes pf. at 90-91.

We find that this advertisement campaign to a certain extent promotes the Company's corporate image. Nevertheless, we recognize that there is also a benefit to educating ratepayers of the value that some customers provided to CVPS's system by conserving energy during the critical time when the transformer had failed. We find it

appropriate to remove only half the amount of $2,141, or $1,071 from CVPS's proposed cost of service.

Economic Development

CVPS states that its economic development incentive program ("EDIP") advertising satisfies two criteria the Board has identified as being appropriate for inclusion in cost of service. First, it is using advertising to inform its customers about its EDIP program, a utility service. Second, the EDIP program serves to encourage energy efficiency, since eligibility for the EDIP program requires participation in the Company's energy efficiency programs. Giffin reb. pf. at 11-12; finding 97.

The DPS contends that CVPS's economic development campaign essentially promotes business expansion and load growth in CVPS's service territory and enhances CVPS's image as a good corporate citizen of Vermont, thereby failing to meet the Board's previously established advertising criteria for rate inclusion. In addition, the DPS believes that it is unreasonable for CVPS to place the entire cost burden associated with its desire to be a leader in the economic development of Vermont on its captive ratepayers. Henkes pf. at 92; Henkes surreb. pf. at 43.

The DPS supports the disallowance of the $129,067. However, if the Board decides to give some recognition of CVPS's economic development advertising expenses, the DPS argues that it should incorporate an appropriate allocation and sharing mechanism. DPS Brief at 53-54.

There is no evidence in the record to persuade us that the television medium is an effective way to target businesses that may be interested in relocating to the State or expanding their in-State operations. This is particularly so in light of Central Vermont's striking inability to cite a single company that had actually expanded or relocated in response to CVPS's television ads. In addition, we find that usage of the television medium for the Company's economic development activities is principally corporate image advertising. The $86,866 in television expense must be disallowed. Findings 98, 99, 100, 101; tr. 8/19/94, Vol. I at 70-83.

We find that the remaining EDIP advertising indirectly satisfies the criteria the Board has identified as being appropriate for inclusion in cost of service. However, we agree with the DPS that it is inappropriate to place the entire expense of the advertising on the Company's captive ratepayers. We conclude that CVPS's shareholders and ratepayers shall share this expense equally. Therefore, of the remaining $42,201 for economic development advertising, $21,100 is to be included in the adjusted test year expense.

Efficiency Plus/C&LM, District Efficiency, and "It's Happening" Advertising

CVPS seeks to recover approximately $185,000 to cover the cost of print, radio, and television advertising under three categories: "Efficiency Plus/C&LM Program", "District Efficiency", and "It's Happening". CVPS states that it is reasonable and prudent for the Company to concentrate its Efficiency Plus advertising on television given that research demonstrates that roughly 245 minutes per day are spent by the average adult watching television as opposed to 34 minutes as an example for newspapers, 15 minutes per day for magazines. Giffin reb. pf. at 14-15; tr. 8/19/94, Vol. II at 57.

The DPS recommends removing the Company's media budget for C&LM from cost of service. The DPS believes that CVPS's marketing campaign focuses on energy information while overlooking the opportunity to pointedly market the Company's energy-saving programs available to customers, thus, making it unreasonable and imprudent. The DPS makes a particular compelling demonstration that other Vermont utilities have achieved greater success in those markets without using expensive television campaigns. DPS Brief at 135; finding 107.

The DPS states that CVPS's educational approach in advertising its Efficiency Plus/C&LM campaign, which relied predominantly on expensive television advertising, was to raise awareness among viewers about the benefits of residential energy efficiency. The Department argues, however, that this approach, by itself, does not satisfy the Board's criterion that the advertising should lead directly to lowering costs through DSM. The DPS argues that the advertisements themselves have only obscure links to the Company's DSM programs. Owen pf. at 5-9; Findings 93, 109, 105, 106.

The DPS further notes that it is possible to both educate and prompt a consumer to act simultaneously, referring to CVPS's profit-minded subsidiary, SmartEnergy Services, which uses this "hard-sell" technique of advertising to promote the GreenPlug product. The DPS also argues that CVPS is using television, an expensive medium, when more economical options were available. Tr. 7/8/94 at 339-340; Owen surrebut. pf. at 7; finding 107.

We are not convinced that CVPS's television advertising of its Efficiency Plus/energy efficiency programs has satisfied the criterion established in Docket 5372. We particularly take note that other Vermont utilities have marketed their DSM programs based on the Board's criteria with greater success than CVPS, without CVPS's pattern of expensive television advertising. CVPS's own subsidiary, Smart Energy, does not use television advertising, implying that the Company is also convinced that advertising with bill inserts is a more cost-effective mechanism.

We are not persuaded by CVPS's argument that its extensive use of television for advertising its Efficiency Plus campaign is prudent simply because the average adult watches over four hours of television per day. The evidence in the record persuades us that CVPS's argument here is not a credible one. Tr. 8/19/94, Vol. I at 81-83.

We note that CVPS relied on a 1992 Advertising Recall Survey to support its claims that energy savings were produced by the media campaign.[26] The DPS uses the Survey to demonstrate that bill inserts are twice as effective for reaching CVPS customers than television advertising. Owen pf. at 5. We are not convinced that a recall survey is a reliable means for determining whether television is an effective way to advertise energy efficiency programs. Tr. 8/31/94 at 190-193. For all these reasons, we find that the amounts spent for television costs in it's Efficiency Plus/C&LM Program advertising ($167,085) must be removed from the Company's cost of service. Since we are disallowing the television advertising, which represents 89.3 percent of the total advertising expenditures for the Efficiency Plus/C&LM Program, we are disallowing 89.3 percent ($15,273) of the $17,106 in administrative costs associated with this program. Exh. CVPS-JSG-1.

We find that the ads for District Efficiency are designed with a primary emphasis upon promoting CVPS's corporate image, and thus, we disallow its associated $2,391 expense.

The Company's "It's Happening" campaign is targeted for commercial and industrial customers. This campaign is very informative, effectively describing the kinds of services CVPS has offered to some customers, and therefore could provide to non-participants. We permit the inclusion of the $5,951 for Central Vermont's "It's Happening" campaign in the Company's cost of service.

We conclude, therefore, that the $184,749 spent in support of its Efficiency Plus/C&LM and district efficiency advertising during 1993 ($167,085 in television advertising, $15,273 in administrative costs, and $2,391 in District Efficiency advertising) must be removed from the cost of service. Finding 102.

I. Trade Show Expenses

---

26. The Recall Survey probed respondents in general terms about its corporate image, media recall, water heating, and opinions about saving energy. The survey indicated that viewers made more effort to save energy. Tr. 7/8/94 at 325-326, 348.

110. CVPS proposes to include in its cost of service $5,676 for the airfares, meals and lodging expenses incurred by a number of State representatives and senators on various trade show trips to cities across the United States and Canada.[27] For this ratemaking proceeding, CVPS has classified these expenses as economic development expenses. However, CVPS reports the same costs to the Vermont Secretary of State as lobbying expenses. Henkes pf. at 94; exh. DPS-H, Sch. 12.

111. The Company's proposed cost of service also includes $19,691 for other expenses incurred by CVPS on these same trade show trips. Henkes pf. at 95-96; exh. DPS-H, Sch. 13.

Discussion re: Trade Show Expenses

The DPS seeks a reduction in CVPS's proposed cost of service of $25,367 to remove trade show-related expenses. Those expenses include $5,676 for the travel expenses of a number of State legislators and $19,691 for similar expenses of CVPS's employees. The DPS asserts that the Board, when it had approved CVPS's economic development program in Docket No. 5569, had no intention to allow rate recovery for such trade show expenses. The DPS also notes that CVPS had failed to demonstrate that these expenses are truly necessary for the provision of safe, adequate and reliable electric service. Findings 110, 111.

We conclude that CVPS's expenses for legislators to travel to trade shows are lobbying expenses and are to be removed from the cost of service as required by Board policy and practice. Finding 112; see Docket 4634, Order of 9/16/82 at 60; Docket 5001, Order of 12/27/85 at 75.

We also find that the expenses of CVPS's employees to travel to the same trade shows must be treated as "below the line" items, to be removed from the Company's cost of service. A utility may have a valid claim that some of the costs of traveling to economic development trade shows should be borne by the ratepayers, since they, in turn, could benefit from such development.[28] However, CVPS has funded the

---

27. The trade show trips were to Toronto, San Francisco, Chicago, and Atlanta. Henkes pf. at 94.

28. There are other equally valid viewpoints regarding the expenses associated with traveling to trade shows, as well. Such expenses could be considered a charitable contribution to the State's economic development efforts. Another alternative is to view the utility's involvement as a joint-venture with the State's economic development agency; if so,

participation of State legislators at some trade shows but has not separated out the trade show expenses of its own employees where no State legislators were in attendance. We therefore cannot disentangle the economic development aspects of those trips from the intermingled opportunities to lobby those legislators. We remove $25,367 —— the total amount of trade-show expenses —— from the Company's cost of service.

J. Community Relations Expenses

112. CVPS proposes to include in cost of service $50,888 for community relations expenses, including such activities as the President's Community Breakfasts, poster contests, the "Growlab" program, community grants, other donations to help non-profit organizations, and expenses associated with its Speaker's Bureau. Henkes pf. at 96-97.

Discussion re: Community Relations Expenses

The DPS asserts that the expenses related to CVPS's community relations programs have little to do with the provision of electric service and primarily serve to enhance the Company's corporate image. The Department supports the removal of these expenses from CVPS's cost of service. Henkes pf. at 97.

We concur with the DPS and find these expenses charitable contributions.[29] We disallow the $50,888 in community relations expenses from the cost of service.

K. Edison Electric Institute ("EEI") Dues

113. CVPS seeks to recover from ratepayers an amount of $69,920 in order to reflect its expenses for affiliation with EEI.[30] Henkes pf. at 98.

114. In GMP's rate proceeding, Docket No. 5428, the Board established the ratemaking policy that 31.88 percent of GMP's EEI expenses be excluded from cost of service. The Board continued this ratemaking policy in all of GMP's subsequent rate proceedings. Henkes pf. at 97.

---

funding should come partly from general revenues.

29. See e.g., Docket 5614, Order of 1/29/93 at 17; Docket 5532, Order of 4/2/92 at 81.

30. EEI is a multi-purpose trade show association with significant expenses for activities such as legislative advocacy, institutional advertising, contributions. Docket 5428, Order of 1/4/91 at 63.

Discussion re: EEI Dues

The DPS notes that in GMP's Docket No. 5428 rate proceeding, the Board found, based on evidence presented in a NARUC prepared "Audit Report on the Expenditures of the Edison Electric Institute", that 31.88 percent of GMP's EEI dues are allocated by EEI to activities such as legislative advocacy, institutional advertising, contributions, and other activities which have no direct benefit to ratepayers. In this regard, the Board stated in its Docket 5428 Order:

> We conclude that a significant portion of EEI activity serves interest of utilities and their shareholders, not those of their ratepayers. Accordingly, EEI expense shall be reduced by 31.88 percent. . . .

Public Utilities Reports, 119 PUR 4th, at 87 and 88 § 151; Henkes pf. at 97; Finding 114.

The DPS asserts that the ratemaking treatment for CVPS's EEI dues should not be different than the ratemaking treatment for GMP's EEI dues. The DPS recommends a reduction of CVPS's proposed cost of service by $20,002. Henkes pf. at 97-98; exh. RJH-1, Sch. 13, Rev. 9/15/94.

We agree with the DPS and apply this same cost disallowance standard to CVPS's EEI dues. CVPS's cost of service is to be reduced by $20,002.

L. Expenses Related to the Docket No. 5546 Executive Compensation Proceeding

115. CVPS's cost of service includes $46,054 for consultant expenses incurred by CVPS for the Docket No. 5546 executive compensation proceeding. Henkes pf. at 98.

116. Since this type of expense is not experienced on a recurring basis, it should have been included in CVPS's "PSB five-year averaging" cost of service adjustment for regulatory expenses. CVPS failed to do so. Therefore, its cost of service should be adjusted to reflect one-fifth of these costs ($9,211), and the remaining $36,843 should be amortized over the next four years. Henkes pf. at 98-99.

Discussion re: Expenses Related to the Docket No. 5546 Executive Compensation Proceeding

CVPS made an error in calculating the proper cost of service impact of this regulatory expense. We reduce the claimed cost of service by $36,843 to correct for this error. Findings 115, 116.

M. Gain on Sale of Utility Property

117. During the 1993 test year, CVPS realized a profit of $77,000 on the sale of various utility properties that had always been included in CVPS's rate base for ratemaking purposes. CVPS has not proposed to treat this gain as a cost of service credit. Henkes pf. at 109.

118. Such property sales are made by the Company on a recurring basis. CVPS's gains on property sales have been increasing during recent years, and CVPS faces the possibility of large utility property sales in the near-term future. Thus, the $77,000 gain incurred during the 1993 test year is representative of what, at a minimum, can be expected during the adjusted test year. Henkes pf. at 10-11, 110.

Discussion re: Gain on Sale of Utility Property

The DPS supports a $77,000 reduction to CVPS's cost of service in order to realize the Company's gains from the sales of utility properties for ratemaking purposes. The DPS argues that the ratepayers have always paid for the return requirements and operating expenses (such as the return on rate base, property taxes, maintenance expenses, security expenses, insurance, etc.) associated with these properties and, therefore, should receive the benefits of any gains realized upon the sales of such properties. Furthermore, the DPS asserts that ratemaking recognition of the 1993 test year gain of $77,000 is appropriate and representative of what can reasonably be expected during the adjusted test year. The Department points out that CVPS is planning the sales of its current Manchester, Bennington, and Springfield service center properties after it replaces these centers with the new consolidated service centers in Sunderland and North Springfield during the adjusted test year. Findings 22, 27; Henkes pf. at 109; Kirn pf. at 4-5.

In similar past cases, we have relied upon the difference between book value and appraisal value. See, Docket 5428, Order of 1/4/91 at 28-31. However, in this case, the Company (which has the burden of proof and the better access to such data) has failed to provide the appraisal data necessary for that calculation. Therefore, we will accept the DPS's valuation of $77,000 in this instance. *See also* the discussion in Section IV, Rate Base. We direct the Company to notify the DPS and Board, at the time it sells its service center properties, of the date of sale and sales prices. This information will inform us of the market values of these properties, a fact that is likely to be helpful in any future rate proceedings.

N. Depreciation Expenses

119. CVPS's proposed adjusted test year depreciation expenses shall be reduced by $25,000 to reflect the "flow-through" effect directly associated with DPS-recommended adjustments to CVPS's proposed rate base additions for the Vernon Road Cap Bank ($4,008, Finding 5), Pittsford Penstock ($4,332, Findings 11, 12), Cavendish Breaker ($4,332, Finding 13) and the FERC Hydro projects ($8,556, Findings 15, 16). Henkes pf. at 100; exh. DPS-H, Sch. 15.

120. As revised by the Rate Base/Cost of Service Agreement, the Company's Cost of Service Adjustment No. 13 —— Depreciation Expense —— increases test year cost of service by $1,364,000 to reflect increased depreciation expense related to rate base additions reflected on CVPS Exhibit CJF-4. Pennington pf. at 5.

121. The depreciation expense adjustment of $1,364,000 was revised from the originally filed amount of $1,368,000 to reflect an agreed upon reduction to the Vernon Road rate base adjustment. Tr. 7/7/94 at 12-13.

122. The economic life assigned to the "limited term electric plant" investments is difficult to assess and is based on judgment rather than specific and detailed engineering studies. To recognize this fact, utilities typically use a consistent, across-the-board economic life assumption for all of their limited term electric plant. This approach averages out any excesses and shortfalls. Henkes surreb. pf. at 26-27.

123. CVPS employs an across-the-board economic life assumption of five years for all of its limited term electric plant, including the Consumer Information System ("CIS") I project (the original system). For its proposed enhancements to that system (the CIS II and III rate base additions), CVPS has assumed economic lives of approximately three years.[31] The result is an overall composite amortization rate of 30 percent rather than the 20 percent amortization rate used by CVPS for all of its other limited term electric plant. Henkes surreb. pf. at 27.

124. CVPS proposes using a three-year amortization period for the CIS enhancements because this period coincides with the remaining amortization period left on the original CIS project. Pennington reb. pf. at 38.

125. In its work papers for this adjustment, CVPS also claims test year payments by Central Vermont for its share of the Millstone 3 Decommissioning Fund in the amount of $154,512. Because current Internal Revenue Code § 468A does not allow current tax deductions for decommissioning costs not expressly approved in regulatory commission

---

31. The economic life of CIS II and III is 41 months and 38 months, respectively. Henkes sur. pf. at 27.

orders, CVPS can take tax deductions for these costs only if the Board expressly approves the $154,512 associated with these decommissioning costs. Pennington pf. at 5.

126. In previous Orders in Docket Nos. 5372 and 5491, the Board approved similar decommissioning expenses for which recovery was sought in rates, and approval of the Company's share of the Millstone 3 Decommissioning Fund in the amount of $154,512 will substantiate and protect the Company's tax deduction in future IRS audits and is consistent with the decommissioning cost tax benefit being passed on to ratepayers in the adjusted test year Cost of Service. Id.

Discussion re: Depreciation Expenses

CVPS proposes to use very specific economic lives for the proposed CIS II and III rate base additions. The Company supports its proposal by asserting that the economic benefits of CIS II and III will not extend as far into the future. CVPS is planning to retire the entire CIS project within the remaining three-year amortization when it moves to a client server environment for all of its main frame applications. Pennington reb. pf. at 38; Findings 122, 123, 124.

The DPS does not support CVPS's proposal and recommends a reduction of the cost of service by $38,000 to reflect a 20 percent amortization rate for CIS II and III. The Department argues that it is inconsistent and inappropriate to use the same across-the-board economic life estimate for all limited term electric plant (in recognition of the difficultly in evaluating the economic lives of each individual limited term electric plant component) but then to make exceptions for certain specific proposed limited term electric plant additions. With respect to CVPS's claim that it is planning to retire the CIS system in three years, the DPS notes that although CVPS's current assumption and plan is to retire the CIS system in three years, the fact remains that this assumption is not known and measurable at this time. Findings 122, 123.

We are persuaded by the Department's arguments and reduce CVPS's cost of service by $38,000. We note that this is a specific example of a general issue: if an estimate is developed from an overall average, there will always be an incentive to "game" the system by leaving unfavorable items in the general pool and seeking special recognition of favorable ones. Allowing this would be both inequitable and inefficient, since it would destroy the validity of the original average.

With respect to the decommissioning expenses for Millstone 3, the Board has approved similar decommissioning expenses for which recovery was sought in rates. We affirm the approval of the Company's share of the Millstone 3 Decommissioning Fund,

in the amount $154,512. This explicit approval should lead to recognition of the Company's tax deduction in future IRS audits and is consistent with the decommissioning cost tax benefit being passed on to ratepayers in the adjusted test year Cost of Service. Findings 125, 126, 133.

O. Income Taxes

127. As a result of an IRS audit that was completed in 1991 and involved tax activities during the years 1983-1988, CVPS incurred certain additional tax liabilities. Up to this time, CVPS has not recorded any amortization for these tax labilities. Henkes pf. at 104.

128. In 1991, CVPS made all required tax payments to the IRS associated with these audit-related tax liabilities and adjusted its books and records by establishing a deferred asset for these tax liabilities. Upon the adoption of FAS 109 in 1993, CVPS reclassified the deferred asset for these tax liabilities to a regulatory asset. Wakefield reb. pf. at 5-10.

129. CVPS proposes to amortize this regulatory asset totalling $1,640,000 over four years, resulting in a proposed adjusted test year income tax increase of $410,000. Henkes pf. at 102-103.

130. These tax liabilities became known and measurable when the IRS field audit was completed during 1991. Henkes pf. at 105 and 106; Henkes surreb. pf. at 45-46.

131. The final agreement on those tax years did not occur until after review by the Joint Committee on Taxation, which occurred on October 15, 1993. Wakefield reb. pf. at 4-5.

132. Prospective rate recognition for such past tax liabilities would represent retroactive ratemaking. Henkes pf. at 105 and 106; Henkes surreb. pf. at 45-46.

133. To treat these "out-of-period" tax liabilities would be inconsistent with CVPS's proposals in this proceeding to remove $345,805 of "out-of-period" test year revenues. CVPS treats these test year revenues in this manner because these revenues, most of which came about as a result of a prior FERC audit, were related to activities in periods prior to the test year. Henkes pf. at 105-106.

Discussion re: Income Taxes

CVPS proposes to amortize this regulatory asset totalling $1,640,000 over four years, resulting in a proposed adjusted test year income tax increase of $410,000. The DPS disagrees with this proposal. The Department states that these tax liabilities became known and measurable when the IRS field audit was completed during 1991 and asserts

that CVPS's proposal for prospective rate recognition for past tax liabilities would represent retroactive ratemaking. Findings 127, 129, 130, 132.

CVPS states that it would have been inappropriate for the Company to commence in 1991 amortization of the deficiency discovered during the IRS audit associated with the income tax rate change because: (1) the IRS audit did not become final until 1993; and (2) the excess deferred tax asset was identified during a transition from Opinion No. 11 to statement 109 in 1993. Under Opinion No. 11, an adjustment for the excess deferred taxes was not required, indeed prohibited, until actions of the regulator permitted recovery in rates for future ratepayers or their related differences were fully reversed. Upon adoption of Statement 109 in 1993, the excess deferred taxes were required to be adjusted and Central Vermont is seeking regulatory approval in this case to recover such cost from its customers. Wakefield reb. pf. at 11-12; Findings 128, 131.

CVPS states that the DPS's opposition to this adjustment on the grounds that it is "out-of-period" is also inaccurate and taken-out-of-context. The Company notes that income taxes are not like most other expenses -- they are self-assessed, based upon complete extremely complex laws, and subject to review and change by an outside authority many years after the fact. The Company also notes that the adjustment is completely consistent with the normalization of accounting for income taxes, previously approved by the Board, and a policy of not permitting the adjustment of deferred taxes after the year that the temporary differences arise would penalize Central Vermont and its ratepayers. In periods of declining tax rates, the utility would be penalized for over-estimating its deductible expenses and underestimating its taxable income. In periods of increasing tax rates, customers would be penalized for the utility's over-estimating its deductible expenses and under-estimating its tax income. Wakefield reb. pf. at 12.

CVPS also states that under FAS 109 accounting, if the Board disallows the Company's recovery in rates of the $410,000, it would be forced to recognize the entire $1,600,000 in expense, absorbed solely by shareholders in 1994. Tr. 8/18/94 at 308 (Wakefield).

CVPS's request in this proceeding to receive prospective rate recognition for these past tax liabilities is denied. We find that the tax liabilities at issue became known and measurable in 1991, by which time CVPS had made all related payments to the IRS. CVPS argues that the then-current accounting conventions allowed the Company to defer these tax liabilities on its books in 1991 because a Board decision had not been made at that time regarding the ratemaking treatment of these tax liabilities. However, the reason why such a Board decision was not available is because CVPS never requested a

Board ruling on these tax liabilities at that time. Instead, CVPS simply deferred these tax liabilities on its books. Finding 130.

The Company, more than three years after these tax liabilities were incurred, is requesting prospective rate recognition for these past tax liabilities. We find that granting such a request would be retroactive ratemaking. Ratemaking is prospective in nature and should not allow for the recognition of past rate excesses and/or deficiencies in future rates. Otherwise, the parties would be forced to review and analyze all of the cost of service changes that have occurred as a result of IRS audits, FERC audits, or other events subsequent to prior rate proceedings in order to evaluate and reflect the extent of past rate excesses or deficiencies. Finding 132. Moreover, approval of CVPS's current request would destroy all incentives for the Company to seek a prompt resolution of these uncertainties at a time when the record is fresh.

We also note that CVPS's proposal to reflect these "out-of-period" tax liabilities is inconsistent with its proposal to remove $345,805 of "out-of-period" test year revenues. Finding 133. Thus, the principle of minimizing inter-period inequities offer another reason to reject CVPS's proposed treatment of these costs.

We therefore reduce CVPS's adjusted test year income taxes by $410,000.

P. Uncollectibles

134. CVPS calculates its proposed adjusted test year uncollectible expenses by applying an uncollectibles/total revenue ratio of 0.4292 percent to its projected adjusted test year cost of service. This uncollectible ratio represents the average uncollectible ratio experienced during the five-year period, 1989-1993. Henkes pf. at 110-111.

135. The actual uncollectible ratios experienced by CVPS during the most recent eight years are as follows:

Year	Ratio (%)
1986	0.2019
1987	0.2880
1988	0.2307
1989	0.1427
1990	0.4936
1991	0.6538
1992	0.4696
1993	0.3862

Henkes pf. at 111.

136. CVPS's uncollectible ratios during the three-year period 1990-1992 and to a certain extent during the 1993 test year, were very much influenced by the effects of the worst recession since World War II during those years. Henkes pf. at 111-112; Henkes surreb. pf. at 35.

137. General economic conditions are expected to improve. CVPS also acknowledged this expectation in its 1993 Annual Report to its stockholders. Henkes pf. at 112.

138. A "five-year averaging" methodology to approximate expected near-term expense levels may be appropriate for expense items experiencing significant upward and/or downward fluctuations from year-to-year without any discernable trend. However, there is a clear and discernable trend present in CVPS's year-to-year uncollectible ratio experience which can be explained. Henkes surreb. pf. at 37.

Discussion re: Uncollectibles

CVPS proposes a 0.43 percent adjusted test year uncollectible ratio, reflecting a five-year average of the ratios of uncollectible accounts expenses to total revenue. The Company uses this methodology to smooth out the recovery of this fluctuating expense. CVPS supports this methodology by noting that the Board has treated other uncertain yet recurring expenses in this way, such as overhead service restoration, hydro maintenance, and regulatory commission expense. Frankiewicz pf. at 15; CVPS Brief, Vol. I at 67-68; Finding 134.

The DPS recommends an adjusted test year uncollectible ratio of 0.36 percent, based on the average uncollectible ratio actually experienced during the eight-year period, 1986-1993. This average incorporates the uncollectible ratio experience for both pre-recession and recession years and would be representative of what can reasonably be expected during the adjusted test year. Finding 135.

The DPS makes the argument that the Board's objective in setting rates is to use cost of service expense levels that can be considered most representative of conditions expected during the adjusted test year. The DPS agrees that for certain expense items that fluctuate without any discernable trend, it may be appropriate to approximate their representative adjusted test year levels based on a five-year historic averaging approach. For other expense items, however, that show a discernable trend that can be explained, a five-year averaging approach may not be appropriate. That approach may render unrealistic adjusted test year projections that are not representative of expected conditions during that time period. Finding 138.

The DPS believes that the 0.36 percent ratio has a higher probability of occurring during the adjusted test year than CVPS's projected ratio of 0.43 percent. The recent and very severe recession had a negative impact on the Company's uncollectible ratios for the last five-year period; however, that level is not typical of uncollectibles over a longer time period. Subsequent to the height of this recession, CVPS has experienced

declining uncollectible ratios, from 0.6538 percent in 1991 to 0.3862 percent in 1993. A projection from this "most recent trend" data would actually lead to a lower bad-debt allowance than that recommended by the DPS. Overall, given that the economy is continuing on its path of recovery, albeit slowly, the DPS recommends that the Board find a projected adjusted test year ratio of 0.36 percent (the average of the last eight years) to be reasonable. Henkes pf. at 111; Henkes surreb. pf at 35; Findings 136, 137.

We are persuaded by the DPS's arguments and find the Department's recommendation of a 0.36 percent uncollectible ratio reasonable and most representative of conditions to be expected during the adjusted test year.

Q. Restructuring

139. Between 1984 and 1994, the Company's employee base has grown by more than one-third and far faster than the Company's number of customers. Almost all of this growth took place from 1984 to 1989. The Company now has 11 percent fewer customers-per-employee than in 1984. Salaries as a percent of retail revenue have grown from 12.7 percent to 14.9 percent since 1984. Chouinard pf. at 4.

140. Including employees of the Company's unregulated subsidiaries and some employees serving Connecticut Valley, CVPS employee numbers are as follows:

Year	Number of Employees
1983	585
1984	588
1985	628
1986	654
1987	702
1988	727
1989	746
1990	752
1991	755
1992	758
1993	775

Chouinard reb. pf. at 1.

141. The objective of the CVPS restructuring programs is to reduce the number of employees by ten to fifteen percent and to reduce the Company's payroll by approximately $4.5 to $5 million annually by 1995. Chouinard pf. at 4.

142. The following are the results of the early retirement program, the voluntary resignation program, and layoffs are:

	Total Number of Employees Before Plan	Reduction in Number of Full Time Employees	Total Number of Employees After Plan
Early Retirement		39.0	
Voluntary Resignation		27.5	
Layoffs		20.0	
Cutback in hours		0.5	
Subtotal		87.0	
Attrition		18.5	
Total	769[32]	105.5	663.5

An additional 18.5 jobs, including three officers, were reduced since the fall of 1993, or a net reduction of 105.5 jobs. CVPS reduced its total work force from 769 to 663. All except one retirement covered by this plan will be completed by the end of 1994.

Chouinard pf. sup. at 2-4.

143. CVPS modeled their voluntary severance program on that of National Life of Vermont's severance program. Tr. 7/5/94 at 178-179 (Chouinard).

144. The Company estimates that the costs to CVPS for each departed employee was about $50,000. Tr. 8/19/94 at 61-62 (Chouinard).

145. Restructuring savings decrease adjusted test year cost of service by $2,170,000. These restructuring savings are the result of adjusted test years' gross savings of $3,193,000, net of the adjusted test year costs of $1,023,000. Pennington supp. pf. at 2.

Discussion re: Restructuring

CVPS has engaged in a plan to reposition its organization to produce a more efficient operation. This plan follows a decade of significant increases in the number of persons employed by the Company. Including subsidiary operations, the Company reported an increase of 190 employees during the period from 1983 to 1993. Of this increase, the bulk of the increases were prior to 1990. Between 1983 and 1989, the employment base of the Company increased by 161 employees or roughly 26 percent. Finding 140.

CVPS states that its plan to reposition should lead to a substantial reduction in its employee and salary base. In combination with attrition, CVPS's plan leads to a reduction of 105.5 positions out of a total of 769 employees (roughly a 13.7 percent

32. We note that there is a discrepancy between CVPS's number of employees for 1993 in Finding 140 and in Finding 142. We presume that the differences are attributed to timing and/or subsidiary employment.

reduction in their workforce).[33] The Company estimates savings from the program to be approximately $3,193,000 during the adjusted test year. Pennington pf. sup. at 2; Findings 142, 145.

Two issues arise in considering restructuring costs when setting rates. The first is whether the restructuring costs (including employee incentives for departure) are indeed appropriate. This encompasses whether: (1) restructuring is in the best interests of the utility and its customers as a whole; (2) the nature and scope of the costs incurred in restructuring are appropriate. The second issue is to what extent the costs of such initiatives should be shared between ratepayers and shareholders.

It would be premature to draw conclusions concerning the overall impact of this initiative. Certainly there are nominal savings associated with a leaner employee base. Those savings are significant and we encourage such savings wherever they can be accomplished without diminishing the quality of customer service.

Nonetheless, the ultimate impact of this initiative on the Company and its customers is far from apparent. The Company offered no defined goals with the restructuring beyond expense reduction, so that it is difficult to gauge success. We can only look to the future to determine the effect of the restructuring on Company efficiency, customer service, and service quality.

We also note that while the savings projected by CVPS are potentially quite significant, the immediate costs claimed by the Company are extremely high. In fact, the Company estimates that the reductions in the employee base will cost about $50,000 per employee. Tr. 8/19/94 at 61-62 (Chouinard); Finding 144.

Management should be accorded some latitude in its discretion as to the scope, design and costs of a restructuring program. However, we are not convinced that requiring ratepayers to carry the full burden of financing the proposed repositioning program provides the Company with the proper incentive to be as efficient as possible in its efforts to downsize. While this program appears to offer substantial savings to ratepayers, over time, this repositioning should also improve the value of the Company to its shareholders. We therefore conclude that recovery of the amortized costs of this program should be recovered in rates, but without carrying costs. As such, the costs of the plan should not be accorded rate base treatment and should be recovered over a five-year amortization period.

---

33. A reduction of 18.5 percent was the result of attrition.

We anticipate similar initiatives from other companies in Vermont, as competitive pressures continue to encourage the regulated utilities to cut costs. On a going-forward basis, in order to preserve the incentives for management to be as efficient in its efforts to restructure as possible and as a matter of basic fairness to shareholders and ratepayers, we will consider whether companies should recover restructuring program costs in a similar manner.

R. The Ceiling Adjustment (also known as the "Management Challenge")

146. CVPS claims that its cost of service supports a 12 percent rate increase. Pennington reb. pf. at 2, 4.

147. The Ceiling Adjustment is a voluntary, Company-imposed, mechanism to limit CVPS's rate request to 8.9 percent. The Ceiling Adjustment represents an additional $4,788,000 of as yet unknown and unmeasurable savings that result in the 8.9 percent cap. Pennington pf. at 9-10.

148. CVPS wishes to have the Ceiling Adjustment absorb any disallowances by the Board of any costs included in the Company's as-filed Cost of Service or Rate Base and any Board-approved, non-cost savings-related adjustments that are required to correct for errors in the Company's filing results or for other appropriate reasons. Pennington pf. at 9; Henkes pf. at 126, 128.

149. CVPS states that it is assuming the risk that it will be able to achieve cost reductions equal to the amount of the Ceiling Adjustment. Pennington pf. at 10.

150. CVPS also desires to have the Ceiling Adjustment absorb the net restructuring savings the Company proposed after it had revised the restructuring savings in May. The Supplemental Testimony of Mr. Pennington indicated that the original estimate of net savings of costs associated with the Restructuring Adjustment of $1,782,000 should be increased to $2,170,000. As a result, the difference of $388,000 should be imputed to the Ceiling Adjustment. Pennington pf. at 9; Pennington sup. pf. at 1-2.

151. CVPS asserts that the balance of the Ceiling Adjustment should include whatever cost savings (that are currently unknown and unmeasurable and therefore not reflected in the Company's adjusted test year results) the Company can achieve. The Ceiling Adjustment does not include the savings that would result from any of the Company's current Restructuring Program. These savings are contained in CVPS's Restructuring Adjustment No. 34. Pennington pf. at 9.

152. The Company also adjusted the Ceiling Adjustment by another $597,000 to reflect the impact of additional known and measurable savings. Pennington sup. pf. at 2; exh. CVPS-JMP-2.

Discussion re: The Ceiling Adjustment

Refer to the discussion in Section II, above.

S. Cost of Service Adjustment for Services Provided to SmartEnergy Services, Inc. ("SES")

153. SES was formed on January 1, 1993, and is one of four wholly-owned subsidiaries of CVPS. At the time of its formation, it acquired what had previously been the below-the-line electric hot-water heater rental operations of CVPS. Pennington/Ryan pf. at 1-2.

154. SES's primary business is to rent and sell energy-related services and appliances. For example, SES sells electric lawnmowers and electric outdoor barbecue grills at retail. SES also rents hot water heaters to approximately 22,000 of CVPS's 135,000 retail electric customers. Lackey pf. at 5; Giffin pf. at 35.

155. SES utilizes CVPS's retail monthly billing system to promote and bill for its hot water heater rentals and to market its other products. During 1993, SES included at least six different messages promoting electric hot water heating in CVPS's monthly billings to its 135,000 customers. Owen pf. at 15.

156. The issue of CVPS's cost allocation method arose on July 7, 1994, when the Board asked CVPS to describe the method and formula it uses to bill SES for these mailing services. The Board also made clear that CVPS's methods of cost allocation would be examined closely in this docket. Tr. 7/7/94 at 158-159.

157. SES receives tangible and intangible benefits from its affiliation with CVPS that are not reflected in the cost assignment procedures used by CVPS. One particularly valuable intangible benefit that SES receives is CVPS's implicit endorsement. This is significant because of CVPS's long-standing relationship with its customers, many of whom perceive that CVPS has expertise in matters relating to energy, and perceive that CVPS acts in the public interest. Lackey pf. at 11; tr. 8/31/94 at 145-146; tr. 9/1/94 at 65.

158. DPS Witness Owen concludes that SES has received $175,500 worth of free services from CVPS. Mr. Owen's calculation only addresses the costs of advertising and publicity services provided by CVPS; it does not address the costs of being part of CVPS's billing process. Mr. Owen recommends that the value of these services be

credited to CVPS ratepayers through a $175,500 reduction to the cost of service. Owen pf. at 3; tr. 7/8/94 at 346.

159. At the July 8, 1994 technical hearing, DPS Witness Henkes recommended the use of a "higher of cost or market" standard when a regulated parent company billed an unregulated affiliate, and a "lower of cost or market" standard when an unregulated affiliate company billed a regulated parent. Tr. 7/8/94 at 288.

160. On August 9, 1994, DPS Witness Lackey filed testimony in support of Mr. Owen's proposed cost of service adjustment, and in support of a "greater of fair market value ("FMV") or allocated cost" standard when billing an affiliate company. Lackey surreb. pf. at 4, 16-17.

161. Mr. Lackey also proposes other policies for the Board to consider with respect to non-utility activities and affiliate transactions, but suggests that they might be beyond the scope of this rate case. Lackey surreb. at 21.

162. Mr. Owen derived the $175,500 proposed adjustment using two separate categories of disallowance. The first applied to four billings in which electric water heating was prominently promoted. In this case, the DPS computed a disallowance using $0.25 per billed customer. The $0.25 is comprised of $0.10 for the use of each customer name and $0.15 as a "partial payment for postage, printing and handling." This methodology produced a disallowance of $135,000 (4 mailings x $0.25/billed customer x 135,000 billed customers). Owen pf. at 15-16.

163. Mr. Owen's second category of disallowance applied to two mailings in which the topic of electric hot water heating was treated with brevity. Here the DPS used a disallowance of $0.15 per billed customer, which is comprised of $0.10 for each customer name and $0.05 as a "partial payment for postage, printing and handling." This methodology produced a disallowance of $40,500 (2 mailings x $0.15/billed customer x 135,000 billed customers). Owen pf. at 16.

164. SES pays nothing for the use of CVPS's electricity customer list, although the mailing list industry typically values a list at $0.05 to $0.15 per name. Owen pf. at 15.

165. A list of electric customers should have a significant value to a company like SES, which is marketing products that consume electricity. CVPS's ratepayers have paid for the development of CVPS's mailing list through their utility bills, and have a right to expect the company to maximize its value when it lets another entity utilize the list. Owen surreb. at 6.

166. Under CVPS's "fully-allocated costing methodology," CVPS charges SES for direct incremental costs which CVPS incurs, plus additional allocations for overhead,

depreciation or amortization, and payroll. In 1993, the total cost charged by CVPS to SES for the use of CVPS's centralized billing system was $162,000, broken down as follows: (a) direct costs, $8,400; (b) common overhead, $81,400; (c) software amortization, $61,900; and (d) payroll, $10,300. Ryan/Pennington pf. at 12-13.

167. CVPS estimates that the market cost of billing services that are "comparable" to the services provided by CVPS is $137,300 annually, which is roughly $25,000 less than the $162,000 charged to SES in 1993. SES maintains that if it were to bill quarterly, this margin would grow to $86,400. Ryan/ Pennington pf. at 14.

168. Higher of cost or market compensation for services provided to the unregulated subsidiaries would not be a violation of generally accepted accounting principles. Tr. 8/18/94 at 312-313 (Wakefield).

169. CVPS's cost of service is to be reduced by $81,000 to properly impute fees that it should have received from its non-regulated subsidiary, SES. This amount is for SES's use of CVPS's mailing list, endorsement, and on the advantage that for having its promotional material contained in an envelope which the recipient will almost certainly open in order to retrieve the enclosed bill. Findings 158, 162; Owen pf. at 14; exh. RJH-1, Sch. 2, Rev. 9/15/94.

Discussion re: Cost of Service Adjustment for Services Provided to SES

On August 15, 1994, CVPS filed with the Board a Motion in Limine seeking to exclude Mr. Lackey's proposed affiliate transaction rules and the related portions of Mr. Lackey's surrebuttal testimony that discusses these proposed rules. The basis of CVPS's motion was that: (1) this material was irrelevant; (2) the DPS offered its testimony too late to afford CVPS an opportunity to present evidence; and (3) because of their general applicability to other Vermont utilities, the proper forum to consider such issues would be in a generic rulemaking proceeding. CVPS Motion, 8/15/94 at 1-3.

At the technical hearing on August 18, 1994, the Board denied CVPS's Motion in Limine, but noted that some of Mr. Lackey's proposals were quite comprehensive, and that after concluding the rate portion of the docket, the Board would examine "prospective issues for inter-company transactions and diversification of activities" as a separate area of inquiry. Tr. 8/18/94 at 178-179. On September 1, 1994, the Board again clarified the aspects of Mr. Lackey's testimony that would be relevant to the ratemaking phase of the proceeding: testimony relating to the allocation of costs and the $175,500 proposed adjustment would be considered at this stage, while prospective guidelines related to the management of affiliate transactions would be dealt with in a later phase. Tr. 9/1/94 at 7.

CVPS takes issue with the DPS's proposed adjustment of $175,500 on both procedural and substantive grounds. Procedurally, CVPS asserts that the concerns it raised in its Motion for Limine (regarding the timing and appropriateness of the affiliate cost allocation principles) still apply to the adjustment, despite the fact that the Board has deferred consideration of the broader issues until a later phase of the docket. It maintains that the underlying concept supporting the $175,500 adjustment is based on one of the deferred issues; hence, an item that was supposed to be postponed is being considered in this case. CVPS Brief, Vol. I at 11; Finding 161.

CVPS outlines three reasons why the entirety of testimony regarding the adjustment should be stricken from the record: (1) CVPS did not have an opportunity to fully discover and present evidence and argument on the issues; (2) the adjustment is dependent upon basic principles which are rules of general applicability and therefore, under the Vermont Administrative Procedures Act, can only be considered in the context of rulemaking; and (3) "singling out" CVPS to unilaterally confront an issue of general applicability is discriminatory and in contravention of the Equal Protection Clause. CVPS Brief, Vol. I at 11-14.

In Docket 5470, *Petition of Department of Public Service requesting an investigation into subsidiaries of Vermont Investor-Owned Electric Utilities*, the Board initiated an investigation into the allocation of common costs between regulated utilities and their unregulated affiliates. Docket 5470, Order of 11/20/90 at 1. At that time, the Department and CVPS held extensive, albeit unfruitful, negotiations on utility diversification and affiliated transactions. After it became clear that the parties would be unable to reach a negotiated settlement, the Board closed the docket and stated that "it appears that the substantive issues raised . . . can best be resolved upon a case by case basis in future dockets." Docket 5470, Order of 9/27/93 at 1. This statement served to put utilities on notice that such topics could come under consideration in future rate proceedings.

Notwithstanding Docket 5470, CVPS was again put on notice that cost allocation would be an issue in this docket when DPS witness Owen entered his prefiled testimony on May 27, 1994. Almost a fourth of that testimony dealt with inter-affiliate transactions with SES. It was at that time that he initially proposed the $175,500 adjustment and explained the conceptual basis for it, including the valuation of certain advertising and promotional costs at fair market value. If there were any questions about the extent to which these issues would be examined, the Board dispelled them in early July when it expressly called attention to cost allocation methods and indicated to the parties that

these methods would be examined closely. See generally, tr. 7/7/94 at 158-58; tr. 7/8/94 at 294; Findings 156, 158.

CVPS has petitioned the Board for an increase in rates. By doing so, it has assumed the burden of demonstrating that the rates that it seeks are just and reasonable. In turn, we are obligated to employ all the relevant criteria at our disposal to judge the representations put forth by CVPS in this rate proceeding. Since CVPS is seeking specific dollar amounts from its captive ratepayers, it cannot avoid a determination of the validity of the principles it uses in connection with those monies.[34]

CVPS has characterized Mr. Lackey's testimony as being based on general principles that can only be considered in the context of a generic rulemaking. CVPS neglects to cite the fundamental case law on this point, however, and its argument is inconsistent with well-settled doctrine. The accepted principle is that when formulating policy, an agency has significant leeway in deciding between using rulemaking or a contested case procedure. In the seminal case on this topic, the U.S. Supreme Court has stated:

> [T]he choice made between proceeding by general rule or by individual, ad hoc litigation is one that lies primarily in the informed discretion of the administrative agency.

Securities & Exchange Commission v. Chenery Corp. (II), 332 U.S. 194, 203 (1947); see also National Labor Relations Board v. Bell Aerospace Co., 416 U.S. 267, 294 (1974).

The Vermont Supreme Court has also spoken on this issue. The Court quoted extensively from Chenery in In re Vicon Recovery Systems, 153 Vt. 539 (1990), and in specific reference to the Public Service Board, stated the following:

> Not every principle essential to the effective administration of a statute can or should be cast immediately into the mold of a general rule. Some principals must await their own development, while others must be adjusted to meet particular, unforeseeable situations. In performing its important functions in these respects, therefore, an administrative agency must be equipped to act either by general rule or order. To insist upon one form of action to the exclusion of the other is to exalt form over necessity.

In re Vicon Recovery Systems, 153 Vt. 539, 549-50 (1990) (quoting SEC v. Chenery (II), 332 U.S. 194, 202-03 (1942)).

---

34. CVPS might have chosen not to seek these monies pending the outcome of the deferred proceeding in this docket. However, since CVPS has put these issues before us, we are exercising our duty to scrutinize them closely.

Furthermore, with respect to the Vermont Public Service Board, this principle of agency choice has been codified into a statute, which states in relevant part:

> The public service board, with respect to any matter within its jurisdiction, may issue orders on its own motion and may initiate rule-making procedures.

30 V.S.A. § 2(c).

In light of the broad latitude accorded the Board by this statute, any given question will turn on whether or not the matter under consideration is within the Board's jurisdiction. Since it is beyond dispute that ratemaking investigations are within the jurisdiction of the Board, § 2(c) operates to empower the Board to proceed by either rule or order.

There are also practical reasons for proceeding by order in this instance. First, as noted earlier, CVPS has put its request for these monies before us in the context of a rate case, thereby triggering our duty to investigate it. Second, the corporate structure of each utility is different, leading to different factual issues and different priorities. This diversity, and the differing priorities that arise from it, cause certain issues to require considerable attention in one utility's rate case, but not necessarily in another's.[35] A contested case provides the flexibility needed to accommodate this diversity. And

---

35. CVPS has asserted that it is being "singled out" in contravention of the Equal Protection Clause. We find that this suggestion lacks merit. There are no suspect classifications at issue, nor are there impacts on fundamental rights. Consequently, only the rational basis standard of review would apply, which is easily met, as the foregoing discussion illustrates. <u>See</u> <u>Tariff filing of Central Vermont Public Service Corporation requesting a 12% increase in rates, to become effective June 2, 1986 (re: Seabrook Issues)</u>, Docket No. 5132, Order of 7/31/87 at 39-41.

On a somewhat different Constitutional note, it is also worth pointing out that the U.S. Supreme Court has found that it is the total impact of a rate order which determines Constitutionality; "[i]f the total effect of the rate order cannot be said to be unreasonable, judicial inquiry . . . is at an end. The fact that the method employed to reach that result may contain infirmities is not then important." <u>Duquesne Light Company v. Barasch</u>, 488 U.S. 299, 310 (1989) (<u>quoting</u> <u>FPC v. Hope Natural Gas</u>, 320 U.S. 591, 602 (1944)).

finally, although broad rules concerning affiliate transactions could conceivably be determined in a generic setting, it is probable that the application of those rules can best be examined within the confines of a contested case, based on the specific facts relevant to that utility.[36]

CVPS also attacks the proposed adjustment based upon substance. It asserts that its "fully allocated costing methodology" actually results in higher charges to affiliates than generally accepted "economic" costing principles, because CVPS's method includes imputed overhead charges. CVPS Brief, Vol. I at 94. We need not reach this issue in this proceeding. The controversy over Mr. Owen's proposed $175,500 adjustment is less about whether cost or fair market value is the more appropriate methodology, and more about the "intangible" benefits that SES receives by piggybacking its promotional literature into CVPS's monthly billing envelope. Findings 155-160, 164-166.

CVPS asserts that with respect to billing services, SES pays roughly $25,000 more than the market cost of comparable services. The Company points out that in response to a question from Chairman Cowart, DPS Witness Lackey advised against any additional imputation of charges for postage, citing the apparent $25,000 excess.[37] Mr. Lackey's response again highlights our concern. Our focus is not on whether CVPS has adequately charged SES for postage; it is whether CVPS is being compensated for its

---

36. The failure of the parties to reach a negotiated settlement in the last generic attempt at dealing with these issues (in Docket 5470) has caused the Board to conclude that they are best dealt with on a case-by-case basis. Docket 5470, Order of 9/27/93 at 1. It is also worth noting that the contested case environment has afforded CVPS considerably greater protection that it would have in a generic rulemaking, most significantly the opportunity to cross-examine sworn testimony.

37. Mr. Lackey's advice represents a shift in the Department's position with respect to postage. Mr. Owen had originally argued that the "the cost of postage, supplies and other expenses are borne by the regulated business as part of its monthly billing process." Owen pf. at 15. Subsequently, CVPS asserted that "it is unequivocally not true to say that the cost of postage, supplies and other expenses are borne solely by the regulated businesses as part of its monthly billing process." CVPS maintains that in 1993 SES was charged $24,528 for "postage, supplies and other expenses as their allocated share of billing expenses." Ryan/Pennington pf. at 14.

endorsement of SES, which is one of SES's most significant competitive strengths. CVPS's endorsement (i.e., goodwill) has imbued SES with CVPS's imprimatur and allowed SES to draw upon CVPS's name recognition and reputation for both expertise in energy matters and concern with the public interest. Findings 162, 163, 167; CVPS Brief, Vol. I at 87-88.

In addition, SES's use of CVPS's mailing list goes far beyond CVPS simply making its customers' addresses available to SES. When it includes its promotional materials in CVPS's mailing envelopes, SES acquires advantages that an average mailing list renter does not get. First, it acquires CVPS's endorsement. Second, it also obtains the additional, significant benefit of being guaranteed that its promotional material will be viewed when the CVPS customer opens the envelope to retrieve his or her CVPS bill. These are advantages that are certainly not enjoyed by the majority of direct mail advertisers who purchase potential customer names for $0.05 to $0.15 per name from commercial mailing list vendors. SES is unquestionably doing more than merely renting a potential customer's name; it is also renting CVPS's name, its implied nod of assent and countenance, and the attentiveness of CVPS's customers. Findings 157, 158, 162-165.

CVPS has put forth evidence to demonstrate that its charges to SES adequately cover its costs associated with billing SES's customers for their monthly hot water heater rental. However, the evidence presented regarding CVPS's mailing list and its goodwill indicates that SES has been charged little or nothing for these benefits. Since CVPS's ratepayers have paid for CVPS's development of its mailing list, billing system and goodwill through their utility bills, they have a right to expect that CVPS will use its best efforts to maximize the value of these intangible assets.[38] Findings 165-167.

---

38. To bolster its contention that any benefits which accrue as a result of the utilization of intangible utility benefits by an affiliate must be shared between customers and owners, CVPS cites Petition of Village of Hardwick Elec. Dept., 143 Vt. 437, 443 (1983) for its holding that the Board must balance the interests of the consumers and shareholders of the utility. CVPS brief at 95. We find this is an excessively narrow reading of that case. Hardwick refers to rates, and it holds that they should not be set so high as to be excessive to consumers nor so low as to be confiscatory for the utility. In between these two extremes lies a "'zone of reasonableness' within which a regulatory commission is free to set rates without judicial

We find that CVPS has not maximized the return possible on its mailing list and goodwill, or on the considerable advantage that inures to SES from having its promotional material presented in an envelope which the recipient will almost certainly open in order to retrieve the enclosed bill. As a result, we conclude that an adjustment is appropriate. Valuation of goodwill is, of course, quite difficult. However, in this case, the record offers a fair proxy —— the market value of a premium mailing list. This is a fair approximation of what CVPS could have expected to receive if it had sought to maximize the value of this asset.

While we are persuaded by certain aspects of Mr. Owen's methodology, we do not accept Mr. Owen's specific calculation of $175,500. Mr. Owen isolated six billings in which he determined electric water heating was promoted. We agree that these six billings should form the basis for the adjustment. We disagree, however, with the amount he imputes for the use of each customer name, and with his inclusion of a "partial payment for postage, printing and handling," in the per customer charge. For the purposes of this proceeding, we conclude that an appropriate charge for the use of each customer name is $0.15. This represents the upper range cited by Mr. Owen as typical of the fair market value for the rental of a specific name in the mailing list industry. We find it is reasonable that a premium list rental charge be imputed, given the unique advantages that this list confers upon SES.[39] We decline to include any

---

intervention." Id. We find that the impact upon rates caused by the disallowance we consider here clearly falls within this zone.

39. This premium is not unlike a "royalty" payable by the subsidiary to the parent company. In Re Southwestern Bell Telephone Company, 137 PUR 4th 63 (1992), the Oklahoma Public Utilities Commission imputed a 5% "royalty," based upon certain gross operating expenses of affiliates, to be recognized as revenues to a parent utility company (South Western Bell Telephone of Oklahoma) for similar advantages conferred upon the subsidiaries by the parent. The Oklahoma Commission imposed the royalty to compensate the parent for intangibles which inure to benefit of the affiliates, including, but not limited to: "use of the [parent company's] trademarks and logos; use of the [parent company's] name, reputation and public image; access to and use of the [parent company's] proven methods of operation and technical knowledge; awareness of . . . industry issues and opportunities; and, reduced business risk, access to capital and

adjustments for postage, printing or handling, since it appears these items have been included in CVPS's cost allocation methodology. Consequently, at this juncture we hereby reduce CVPS's cost of service by a total of $81,000.[40] As noted above, we will examine potential further refinements to specific cost assignment methodologies in subsequent phases of this docket. Findings 162-168.

T. Salary and Wages

170. CVPS agreed to correct for a calculation error made in the determination of its originally claimed pro forma salary and wage increase adjustment. Henkes pf. at 46; exh. DPS-H, Sch. 3; tr. 7/7/94 at 5; Frankiewicz pf. at 7.

Discussion re: Salary and Wages

In calculating its originally proposed salary and wage expense increase for the adjusted test year, CVPS erroneously applied its salary/wage increase multiplier factor of 0.07411 to test year wages and salaries of $503,000 that was deferred to its C&LM deferral account rather than expensed to O&M. Thus, CVPS had overstated its proposed adjusted test year salary and wage expense increase. Finding 170.

After correcting for the error, the Department and the Company's revised salaries and wages adjustment differed by $1,000. The Company rounded the individual operating components of salary and wages (e.g., production, transmission, etc.), as shown in Cost of Service Adjustment No. 6, while the Department rounded the total salary and wage amount. We find that the DPS's adjustment is more accurate and therefore accept the Department's reduction of $38,000.

---

credit worthiness." Id. In South Western Bell, as in the case of SES and CVPS, the extra charge was designed to act "as a surrogate for reasonable compensation to [the parent company] when intangible benefits are enjoyed by affiliates with no explicit accounting for such intangible transactions on the books of [the parent] or the affiliates." Id.

40. The total of $81,000 was computed by multiplying the $0.15 per customer name charge, times CVPS's 135,000 customers, times the six mailings identified by Mr. Owen ($0.15 x 135,000 x 6 = $81,000).

U. ACE-Cost of Service and Rate Base Impacts

171. CVPS reduced its claimed rate base component for ACE by $85,000 and its claimed cost of service amortization expense for ACE by $351,000 to correct for certain errors. Henkes pf. at 38; tr. 7/7/94; Pennington reb. pf. at 42-43; Henkes surreb. pf. at 32.

172. CVPS originally proposed to include in its adjusted test year cost of service an amount of $1,039,000 for ACE amortization expenses. CVPS originally proposed to include in its adjusted test year rate base an amount of $1,260,000 for unamortized ACE deferrals. Henkes pf. at 38.

173. In the Docket 5651 Stipulation, CVPS agreed to reduce its authorized return on equity from 12.5 percent to 12.0 percent effective January 1, 1993. This stipulated return on equity rate of 12 percent did not expire on December 31, 1993. It stays in effect until such time that the Board establishes and approves a new rate through a specific order in the context of a rate proceeding. Henkes pf. at 39-40.

174. CVPS's corrected adjusted test year ACE amortization expense should be reduced to reflect a return on equity rate of 12 percent, rather than CVPS's proposed ratea of 12.5 percent, in the caluclations of the ACE amounts for the period January 1, 1994 through December 31, 1994. Henkes pf. at 39-40; ;exh. RJH-R-1, Sch. 31.

175. CVPS and the DPS have agreed to recalculate the amount and value of ACE recovery for the purposes of this rate case once the Board resolves contested issues in this Docket. CVPS will make the calculation and make a compliance filing prior to implementing any changes to its rates. Tr. 7/19/94 at 252-255.

Discussion re: ACE - Cost of Service and Rate Base Impacts

In its original filing, CVPS proposed an adjusted test year ACE amortization amount of $1,039,000 and an adjusted test year ACE rate base investment level of $1,260,000. During discovery, CVPS confirmed that it had made certain calculation errors. Henkes pf. at 38. Subsequent to this original filing, CVPS also revised its proposed ACE amortization and rate base calculations to remove the impact of wholesale allocations and to correct for errors relating to its lost revenue calculations. Pennington reb. pf. at 42-43. The total impact of the above-described error corrections and revisions reduced CVPS's original ACE rate base claim by $85,000 and original ACE amortization claim by $351,000. Exh. CVPS JMP-4; Henkes surreb. pf. at 32; exh. RJH-R-1, Sch. 31.

CVPS and the DPS disagree as to what the appropriate return on equity is for CVPS during the period January 1, 1994-October 31, 1994. CVPS asserts that the

Docket 5651 Stipulation, which was approved by the Board on September 20, 1993, was to be in effect for the calendar year 1993 only. The Company states that the stipulation does not state or imply that the cap at 12 percent would remain in effect beyond 1993. Finding 173; see findings 42-48 and related discussion.

The DPS argues that the stipulation makes no specific reference and includes no specific provisions stating that the agreed upon return on equity rate of 12 percent would expire on December 31, 1993 and revert to 12.5 percent on January 1, 1994. The Department thus asserts that the stipulated return on equity rate of 12 percent is currently still in effect and will stay in effect until a different return on equity rate is ordered as a result of this rate proceeding. The DPS's recommendation would reduce CVPS's cost of service $13,000. Finding 173.

We agree with the Department's position. The Board approved the Docket 5651 Stipulation with the understanding that it was in lieu of a fully litigated investigation into CVPS's rates. The return on equity of 12 percent would remain until the Board establishes and approves a new rate. We conclude, therefore, that CVPS must reduce its ACE accordingly.

V. C&LM-Cost of Service and Rate Base Impacts

176. CVPS proposes projected adjusted test year C&LM deferral amortization expenses and recurring C&LM expenses totaling $5,433,000. CVPS proposes adjusted test year unamortized C&LM deferrals in rate base amounting to $11,036,000. Exh. DPS-RJH-1, Sch. 14 at 1, Rev. 9/15/94.

177. According to the Board-approved Docket 5651 Stipulation, CVPS agreed to write down its DSM deferrals for any earnings in excess of a return on equity of 12 percent, to be measured effective January 1, 1993. Henkes pf. at 31; Finding 44.

178. CVPS has calculated that its actual achieved return on utility equity during 1993 was 11.971 percent. Pursuant to this calculation, CVPS has not proposed to credit its DSM deferral balance with any earnings in excess of a return on equity of 12 percent. Henkes pf. at 32-33.

Discussion re: C&LM - Cost of Service and Rate Base Impacts

In calculating its achieved return on utility equity for 1993, the DPS asserts that CVPS did not remove the financial results for such non-regulated items as CV Realty and other non-utility properties such as non-utility housing investments, the VT Venture Capital Fund or other non-utility investments. Henkes pf. at 34-35. The DPS also claims that CVPS did not exclude from its achieved return on utility equity calculations many "below-the-line" income and expense items which are typically excluded for

ratemaking purposes by the Board. The Department states that such items include revenues and expenses related to non-utility operations; non-operating rental income; interest and dividend income; non-operating taxes; lobbying expenses; donation expenses; supplemental life insurance expenses; penalties; and income and losses related to CVPS's wholesale operations. Henkes pf. at 36; Henkes surreb. pf. at 18-21.

The DPS states that because all of these items were excluded for ratemaking purposes, CVPS did not receive rates to cover these items, and thus it would therefore not be appropriate to then consider the actual per-books recordings for these same items in the calculation of the achieved return on utility equity number. Henkes surreb. pf. at 19. The DPS calculated the 1993 achieved return on equity number to be 12.55 percent which it believes is a basis consistent with the ratemaking principles applied by the Board in setting rates for CVPS. Henkes pf. at 37; Henkes surreb. pf. at 19.

The DPS failed to fully demonstrate two facts: (1) which of these items were "below the line" income and expense items that are typically excluded for ratemaking purposes; and (2) that accelerating the write-off of these assets had any net detrimental impact upon ratepayers, after taking into account the expected savings for ratepayers in the future as the result of the accelerated depreciation. No adjustment is to be made at this time.

VI. COST OF CAPITAL

A. Capital Structure

179. CVPS projects the capital structure of October 31, 1994, to determine levels of investor-supplied capital for ratemaking purposes. Booraem pf. at 6; exh. CVPS-JWB-R-2.

180. The Company develops its preferred equity cost using balances as of December 31, 1993, adjusted for redemption of nine percent preferred stock issue with a like amount of new preferred stock. However, the Company's capital structure does not include a proforma preferred stock issue and instead includes the same amount of debt. Booraem pf. at 6; Booraem reb. pf. at 3.

181. The DPS and the Company disagree on one aspect of capital structure relating to the non-regulated equity that is to be deducted from the overall common equity amount to arrive at the so-called "utility equity" base for ratemaking purposes. Exh. CVPS-JWB-R-2.

182. The Company excludes equity invested by CVPS in its subsidiaries from its proposed ratemaking capital structure. Booraem reb. pf. at 3; exh. CVPS-JWB-R-2.

183. CVPS excludes $2,532,000 equity investment in Connecticut Valley Electric Company ("CVEC" or "Connecticut Valley") from the equity portion of the Company's requested ratemaking capital structure. Booraem reb. pf. at 3; exh. CVPS-JWB-R-2; Hill sur. pf. at 6.

184. The Company excludes $28,707,000 in non-jurisdictional equity to account for the Company's equity investments in subsidiaries. Booraem reb. pf. at 3; exh. CVPS-JWB-R-2.

185. CVPS does not exclude a $2,500,000 investment in a CVEC debt issue (which appears on CVPS's balance sheet as equity capital) on the expectation that the $2,500,000 CVEC note which CVPS holds would be refinanced with another investor prior to the close of the record in this proceeding. DPS Brief, Vol. I at 106, 109.

186. The Company recommends a capital structure projected at October 31, 1994, consisting of $146,253,000 common equity, $28,054,000 preferred stock, and $128,555,000 long-term debt. Exh. CVPS-JWB-R-2.

Discussion re: Capital Structure

Both parties recommend the use of $128,555,000 of long-term debt at an embedded cost rate of 7.49 percent, and $28,054,000 of preferred stock at an embedded cost rate of 7.23 percent for ratemaking purposes. DPS Brief at 105; Finding 186.

The DPS recommends a capital structure projected at October 31, 1994, consisting of 47.60 percent common equity, 9.39 percent preferred stock, and 43.02 percent long-term debt. Hill pf., Sch. 3 at 5.

The Company recommends a capital structure projected at October 31, 1994, consisting of 48.29 percent common equity, 9.26 percent preferred stock, and 42.45 percent long-term debt. Exh. CVPS-JWB-R-2.

The fundamental difference between the Company's and the DPS's positions concerns the amount of equity to be used in CVPS's ratemaking capital structure. Both CVPS and the DPS agree that unregulated equity capital should be removed from the Company's consolidated equity balances in order to base CVPS's utility rates on utility equity only. They also provide different estimates of the Company's non-utility equity investment. Finding 181.

We conclude that the Company's proposed capital structure is acceptable with modification to incorporate the equity by an amount of the Company debt holding of its

CVEC subsidiary.[41] We reject the Department's proposal because it is unclear whether the Department's subsidiary equity figure also includes subsidiary debt. To further adjust for investments made by CVPS subsidiaries would risk overstating the equity investments in unregulated subsidiaries of the Company.[42] We invite the Department to clarify this issue in future proceedings.

The arithmetic result of applying this adjustment to the Company's proposed capital structure is 47.86 percent common equity, 9.34 percent preferred stock and 42.80 percent long-term debt.

B. Cost of Equity

187. The appropriate ratemaking dollar amount and cost rate for long-term debt are $128,555,000 and 7.49 percent, respectively. Exh. CVPS-JWB-R-2; Hill pf. at 15.

188. The appropriate ratemaking dollar amount and cost rate for preferred stock are $28,054,000 and 7.23 percent, respectively. Exh. CVPS-JWB-R-2; Hill pf. at 15.

189. CVPS's purchased power expenses over the past 20 years have averaged 48.6 percent of annual revenues, and have shown little variation during that time. Hill pf. at 12-13, Sch. 3 at 3.

190. The evidence suggests that CVPS's capital structure imparts less financial risk to the Company than that of the electric utility industry, on average. Hill pf. at 11; Hill sur. pf. at 7.

191. CVPS's fixed obligations, arising from purchased power as well as all other off-balance sheet debt, do not endanger the Company's financial viability. Hill pf. at 14, Sch. 3 at 4.

---

41. Both the Company and the DPS have acknowledged that it is necessary to deduct an amount of $2,500,000 from the equity balance of the Company in establishing an appropriate capital structure. CVPS Brief 9/26/94 at 108-109; DPS Brief 9/23/94 at 111-112.

42. The DPS's brief, filed on September 23, 1994, calls attention to this very problem, noting that unregulated operations contain debt amounts that should be removed in establishing an appropriate capital structure for rate-making purposes. DPS Brief, 9/23/94 at 112.

192. The DPS witness' analysis of cost of common equity capital for the Company and an electric utility sample group of similarly situated utilities is summarized below:[43]

Method	Sample Group	CVPS
DCF	10.71%	10.83%
EPR	10.39%	10.30%
MTB	10.45%-10.05%	10.59%-9.78%
CAPM	9.89%-11.07%	10.39%-11.72%
CAPM (ex ante)	9.22%-10.18%	9.67%-10.44%

Hill pf. at 33.

193. The DPS's "best estimate" of the cost of equity capital for an electric utility company similar in risk to CVPS falls in the range of 10.50 percent to 11.00 percent. Hill pf. at 33.

194. A point estimate of the Company's cost of equity capital is 10.75. Hill pf. at 33.

Discussion re: Cost of Equity

There are three steps in establishing the cost of capital. First, we determine an appropriate capital structure. Second, we determine the rates for each component of the capital structure. Finally, we calculate an overall cost of capital from the total of the component costs, each adjusted for its proportional contribution.

While there were some differences between the parties on the separation of subsidiary equity capital in determining the capital structure, the only significant issue in determining the cost of capital relates to the determination of the appropriate value for equity capital. The determination of this value has a significant effect on the overall cost of capital because it represents a large share of the overall capital structure (i.e., 47.86 percent).

There is no objective measure of the return required for common equity. Therefore, the Board must exercise its judgement in making the appropriate determination. The Board, however, is not without guidance in exercising its judgement here. The principle factors that should be used in establishing a rate were set out over seventy years ago:

---

43. "DCF" pertains to "discounted cash flow" analysis; "EPR" pertains to "earnings price ratio" analysis; "MTB" pertains to "market-to-book" analysis; "CAPM" pertains to the "capital asset pricing model and "CAPM ex ante" pertains to forward-looking CAPM model.

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.

Bluefield Water Works & Improvement Co. v. Public Service Commission, 262 U.S. 679, 692-93 (1923). See also Duquesne Light Company v. Barasch, 488 U.S. 299, 310 (1989)

These standards are reflected in the statutes governing the Board's decisions, and have been endorsed repeatedly by the Vermont Supreme Court. See, e.g., Petition of Village of Hardwick Electric Department, 143 Vt. 437 (1983); In re Green Mountain Power Corp., 131 Vt. 284 (1973); Letourneau v. Citizens Utilities Co., 128 Vt. 129 (1969).

There is no one model or approach accepted as being definitive in determining rate of return. Both the Company and the DPS have presented the results of several models used in determining the appropriate rate.

CVPS concluded from its analyses that its required return on equity is 11.5 percent. The Department indicated that their best estimate of the cost of equity capital fell in the range of 10.5 percent to 11.00 percent. The Department's witness recommended 10.75 percent as an appropriate point-estimate of the equity capital cost of CVPS. Hill pf. at 33; Finding 193.

The Department's witness relied on five different models or model variants. These models include models such as the discounted cash flow ("DCF") model that is now almost universally accepted in the United States and Canada. The Department used four other models or model variants to corroborate the results of the DCF model. These models included the Market to Book Ratio Analysis ("MTB"), the Earnings Price Ratio Analysis ("EPR"), the Capital Asset Pricing Model ("CAPM"), and the CAPM (ex ante).

The Company's witness also used the DCF model and the CAPM with a different set of underlying assumptions. In addition to these models, the Company's witness used the Risk Premium model.

As we have previously ruled in literally dozens of rate proceedings, rate of return must be guided by consideration of several technical formulas, but cannot be dictated by a rigid application of any specific algorithm. In general, we found the analysis of the

Department's witness more persuasive in their use of the models. The Company's risk premium model suffers both as a matter of general practice and, in particular, in its current application by the Company. The assumptions underlying the Company's application of the DCF model were similarly unpersuasive. We conclude from the Department's testimony that the CAPM model, while potentially useful in corroborating the results of other models is not effective as a sole means of determining an appropriate value or range. Indeed, any one model is less useful as a sole means of determining an appropriate return.

We found the Department's analysis both highly credible and well supported by a wide variety of measures. The models and assumptions used by the Department were well documented and detailed. The wide variety of models used ensures that their results are robust. These measures included both an industry sample group of similarly situated utilities and CVPS specific measures.

In addition to the quantitative results of the models, other considerations may play into an appropriate determination of the rate. The Company maintains that the Department's proposal is simply too low in an increasingly competitive market. Additionally, the Company maintains that its so-called off balance sheets liabilities increase the Company's financial exposure. CVPS Brief at 113.

The DPS maintains that CVPS's equity rich capital structure reduces the financial exposure of the Company and should therefore be a significant factor in determining an appropriate return for the Company. DPS Brief at 120; Finding 190.

The Company raises valid concerns regarding the impact of risk and the possibility of increased competition. Nevertheless, the market for electricity is far from competitive currently. As such we conclude that competition is not a threat to the stability of Company revenues. While the off-balance sheet liabilities of the Company present some concerns for the financial exposure of the Company, the evidence suggests that the strong equity position of the Company provides abundant coverage for such concerns. Finding 191.

No precise predictions of the cost of common equity is possible, but we have relied upon the evidence and our experience and judgment to select the best estimate possible. Taking all of these factors into account, we choose a value of 10.75 percent as

an appropriate value for CVPS's rate of return on equity before assessing reductions to reflect management performance and fairness to ratepayers.[44] Finding 193.

In doing so, we note that the evidence supports a value as low as 10.5 percent, and selecting that value as a starting point would be consistent with sound regulatory practice. It is not uncommon for state commissions to select the lower end of an appropriate range in recognizing instances of poor overall management performance.[45] Nevertheless, we favor establishing a clear separation of our starting point (*i.e.*, what might the cost of capital be, aside from considerations of management performance and ratepayer equity) from the overall rate of return question -- which results from a fair and appropriate choice of adjustments. Alternatively, we could have specified 10.5 percent as the starting point and specified a smaller equitable adjustment. In either case, the result would be the same. The discussion of those adjustments and the resulting rate of return, is discussed below in Section VII.

The overall weighted average cost of capital, before the adjustments discussed above, for the Company would be as follows:

	Adjusted	% Struct	%Cost	%ROR
LTD	128,555	42.80%	7.49	3.21
Preferred	28,054	9.34%	7.23	0.68
Common Eq.	143,753	47.86%	10.75	5.14
Total	300,362	100.00%	9.03	

For reasons outlined below, however, the return on equity allowed for the purposes of this case is 10.0 percent. See Section VII.

VII. RESOURCES AND COST MANAGEMENT

A. Power Supply Management

---

44. We note that this value and indeed, the overall result in this case, are consistent with or above those of recent Board Orders of January 26, 1994 in Docket 5656 involving Citizens Utilities and the May 13, 1994 Order in Docket 5695 involving GMP in which the Board approved target rates of 9.89 percent and 10.50 percent, respectively.

45. Re: Commonwealth Electric Company, Mass. D.P.U. Nos. 89-114/90-331/91-80 (1991) and Re: Boston Edison, Mass. D.P.U. Nos. 85-266-A/85-271-A (1986).

The Company's Management of its Power Portfolio

195. CVPS's power supply portfolio will be excessively costly to its ratepayers over much of the lives of its entitlements to the resources in that portfolio. Relative to current market prices for replacement power and long-run avoided costs, CVPS's power costs are likely to significantly exceed market costs over the next two decades.[46] Rosen pf. at 9; Rosen supp. reb. at 4.

196. In the main, CVPS's excess power costs are caused by the HQ Contract, Millstone III, Vermont Yankee, Connecticut Yankee, and Yankee Rowe. The decisions to acquire these supply resources were under the control of CVPS's management. Rosen pf. at 9-10.

197. CVPS's power costs are significantly above those of a comparably situated electric utility in Vermont. Green Mountain Power Corporation's ("GMP") net power supply costs have averaged 20-27 percent below those of CVPS over the past five years. Rosen pf. at 9.

Chronology: The Hydro-Quebec/VJO Contract and the Return Sales Agreements

198. On October 12, 1990, the Board approved a thirty-year contract ("Contract") for the purchase by the Vermont Joint Owners ("VJO") of 340 megawatts of electric power and associated energy from Hydro-Quebec ("HQ"), the provincial utility of Quebec. Under the Participation Agreement ("Agreement"), the VJO agreed to sell at cost all power and energy under the Contract to all Vermont electric utilities, in amounts as set out in the Agreement. Docket 5330, Order of 10/12/90 at 58-59.

199. In its Order approving the Contract, the Board found that the overall value of the Contract was impaired by large purchases of power and energy in the early years, in particular by CVPS. Therefore, as a condition of approving the Contract, the Board ordered the affected Vermont utilities to make all good faith efforts to negotiate return sales that would reduce or offset the early-year purchases. *Id*. at 34, 223-225.

200. Fifteen days prior to the Board's decision, the Canadian National Energy Board ("NEB") had released licenses for Hydro-Quebec's export of power under the Contract, subject to specified terms and conditions. *Id*. at 55-56.

---

46. DPS witness Rosen estimates this excess to be approximately $113 million, present value (1994 $). While we do not necessarily adopt his assumptions and methodology in calculating these excess costs, the evidence clearly demonstrates that the excess is on this order of magnitude. Rosen supp. reb. at 4.

201. Under the Contract and Agreement, CVPS acquired entitlements to HQ power according to the following non-cancellable schedules:

Sch. A (11/01/90 to 9/30/95)	22.725 MW
Sch. B (10/01/95 to 10/31/15)	90.900 MW
Sch. C-1 (05/01/90 to 10/31/12)	29.810 MW
Sch. C-2 (05/01/92 to 10/31/12)	20.031 MW

Id. at 223-225.

202. These purchases, in combination with Vermont Yankee, amount to the largest single financial commitment made by CVPS. The Schedule C-2 purchases are the most significant factor underlying the Company's current request for a rate increase. Exh. CVPS-RS-3.

203. In April 1991, the Company negotiated and the Board approved a return sale at full cost of 22.725 MW of power at Schedule A prices for the period May 1, 1991, to September 30, 1995, and at Schedule C-1 prices thereafter until April 30, 2012. Also according to the terms of this first return sale agreement, for the period November 1, 1996 to October 31, 2016, CVPS will purchase 22.725 MW of power under Schedule C-4a. While executed through legally separate contracts, the substantive effect of the first return sale agreement was an *at-par*, five-year deferral of purchases until late 1996. The Board's approval Order noted that the first return sale only somewhat reduced the Company's early-year purchases. Therefore, the Board ordered additional efforts to reduce the Company's early-year exposure to excessive costs under the Contract. *Id.*; Docket 5330-C, Order of 4/30/91 at 2-3 and Order of 9/18/91 at 4-5.

204. The first return sale agreement was expected to improve the net present value of Contract power to CVPS by approximately $2.7 million. Docket 5330-C, Order of 9/18/91 at 5.

205. In April 1991, at the time of the approval of the first return sale agreement, the Company had already begun negotiating a second such agreement. EMA pf. at 56-57; exh. CVPS-EMA-A (EMA-32).

206. On October 3, 1991, CVPS notified the Board that it had executed a second return sale agreement with HQ, effective October 1, 1991. That letter contained the first formal notice to the Board (and, apparently, the first public statement) that some return sales would occur at less than full cost. Dockets 5330-C and 5491, CVPS Letter, 10/3/91.[47]

---

47. On September 9, 1994, the Board renewed its previous efforts to have CVPS identify the first time at which it had informed regulators that the second return sales agreement would be for less than its

207. On February 11, 1992, the Board approved the second return sale agreement between CVPS and HQ. This second agreement called for the return sale of 30 MW of Schedule C-1, beginning October 1, 1991, and 20 MW of C-2 power, beginning May 1, 1992. Both return sales will terminate on October 31, 1996. Docket 5330-C, Order of 2/11/92 at 15.

208. The effect of the second return sale agreement is that CVPS is currently selling power to Hydro-Quebec at 78 percent of its full cost.[48] The second return sale

---

original purchase price. CVPS's witness stated that he was still unable to provide that information, but noted that compliance proceedings and a rate case had been pending at the time. Tr. 9/9/94 at 86-87. The Board then informed the parties that it intended to take judicial notice of records and orders related to the contact and timing of CVPS notice to the Board regarding the lock-in of the Contract and the terms of the second return sales agreement. Counsel for the Company waived any objection to review of those records for the purpose of determining whether such information had actually been presented in the hearings. He did, however, ask the Board not to conclude that failure to find such a notice meant that no notice had been given. *Id.* at 91. Counsel for the Department noted that the burden was upon the Company to demonstrate that such a notice had been given. The Board noted a continuing "open question for [CVPS] to see if there are records of documents being transmitted." *Id.* at 89. CVPS has yet to demonstrate that it notified regulators of the terms of the second return sales agreement prior to October 3, 1991. As announced on September 9, 1994, we will take notice of the relevant transcripts for the purpose of determining that the Company was explicitly informed of regulatory interst in this question and that it failed to answer explicit questions when they were raised. As to the lack of timely notice in other ways, we rely upon the fact that the Company (which controls the relevant records) has failed to respond to the reiterated "open question" upon this point.

48. Specifically, during CVPS's four winter months, HQ will pay full energy and capacity prices for the return sales. During the eight summer months, HQ will pay full energy prices and 46 percent of the capacity prices for the return sales. Two other provisions of the second return sale agreement include an energy banking arrangement, whereby CVPS can defer

agreement improves the position of the Company when compared to its overall Contract commitment, but impairs it when compared to an at-par avoidance of scheduled purchases from HQ in those years. Tr. 9/9/94 at 50.

209. The second return sale agreement was expected to increase the net present value of Contract power to CVPS by about $19 million, assuming a *prior* commitment to the overall Contract. Docket 5330-C, Order of 2/11/92 at 18.

210. In 1992, the difference between the amount paid by CVPS to HQ for Contract power and the amount paid to CVPS by HQ for the return sales equalled $2.71 million; this constituted a net cost borne by CVPS's ratepayers for electric power that they never received. In 1993, the net cost was $3.83 million. The net costs estimated for 1994 and 1995, respectively, are $3.56 million and $3.96 million. Exh. CVPS-RS-6.

211. CVPS is currently negotiating a third sell-back agreement. The terms of that agreement are unlikely to produce any benefits for the Company's ratepayers before, at least, the end of 1995. EMA pf. at 56, n. 13; Stein/Page pf. at 40; tr. 9/7/94 at 347.

Chronology: The Decision to "Lock-In" the HQ Contract

212. On April 30, 1991, the Board approved a Waiver and Release ("Waiver") entered into by the VJO and HQ. The effect of the Waiver was to defer from April 1 to November 30, 1991, the date by which the parties could cancel the Contract without liability (*i.e.*, the "lock-in" date).[49] Docket 5330-E, Order of 4/30/91 at 1; *see also* exh. CVPS-EMA-A (EMA 33).

213. The VJO executed the Waiver because CVPS and two other participants were then negotiating return sale agreements. In addition, CVPS planned to evaluate alternatives to the Contract. Stein/Page pf. at 61-62.

---

return sales for limited periods, and an option for HQ to buy 50 MW of power and energy for the four-year period beginning on November 1, 1996. If HQ exercises that option, it will pay full prices under the relevant schedules. Docket 5330-C, Order of 2/11/92 at 16-17.

49. Originally, the VJO had filed Amendment No. 3, which, among other things, extended the lock-in date until April 30, 1992, and required the terminating party to pay stipulated damages. The Board found this to be a material change to the Contract, requiring prior review. Docket 5330-E, Order of 4/19/91. The VJO then withdrew the amendment and filed the Waiver. *Id.*, Order of 4/30/91 at 2.

214. Hydro-Quebec executed the Waiver in order to consider the potential effects of the NEB's conditional release of the export licenses. At that time, HQ had not yet appealed the NEB decision to the Canadian Federal Court of Appeals. *Id*. at 62.

215. CVPS used its discretion to not lock in the Contract as a bargaining point in its negotiations for the second return sale agreement. Put another way, an affirmative decision to lock in was the *quid pro quo* for HQ's agreement to buy back some amount of Contract power.[50] Stein/Page pf. at 36; tr. 9/8/94 at 44-46.

216. HQ informed the VJO that modifying the Contract itself (specifically, changing the size or duration of the schedules) would require approval from the NEB. HQ stated that it was unwilling to return to the NEB for further Contract review. Tr. 9/8/94 at 57-58; tr. 9/9/94 at 53-54; *see* Docket 5330-C, Order of 4/30/91 at 2.

217. CVPS's original proposal for the second agreement was a return sale of an unspecified amount of Contract power and energy at full cost. HQ rejected it and informed the Company that it would not pay full cost for a second return sale.[51] CVPS did not identify the precise time when HQ responded to the Company's proposal, but it clearly was several months before CVPS informed the Board or public of this fact. Tr. 9/8/94 at 49-50; tr. 9/7/94, Vol. II at 405.

218. On June 17, 1991, CVPS witness Stein made an extensive presentation to the Company's Board of Directors, describing the HQ Contract, its value to the Company and ratepayers, and the intent and status of negotiations for the second return sale. Mr. Stein, along with Donald Rushford, CVPS's General Counsel, was the

---

50. Under the terms of the Participation Agreement, CVPS did not have unilateral power to either cancel or lock in the HQ Contract. However, testimony by CVPS witness Stein in this docket and in Docket 5330-C shows that the Company believed that it had effective control over this decision. *See, generally*, tr. 9/8/94; Docket 5330-C, tr. 10/21/91 at 138*ff*.

51. Specifically, Mr. Stein testified that: "When we first started talking to Hydro Quebec [about a second return sale], they made it very clear that they wanted to do something, that they were not going to pay full price for this. And we made inquiries as to what price we thought we could get other places for this capacity and found that we were going to get the best deal from Hydro Quebec." Tr. 9/7/94, Vol. II at 405-406. These discussions had begun before the end of April 1991. Finding 205.

Company's principal negotiator for this transaction. It was clear at that time that the return sale would not be made at full price, although no specific return-sale price was known. CVPS's Directors then authorized management to execute the second return sale agreement and lock in the Contract at their discretion.[52] Tr. 9/9/94 at 28, 49-50; Stein/Page pf. at 39.

219. On July 12, 1991, the Canadian Federal Court of Appeals struck down the two conditions that had been placed by the NEB upon HQ's export licenses. Stein/Page pf. at 63.

220. On February 15, 1991, CVPS filed a request for a 14.9 percent increase in rates. In that case, intervenors opposed to the HQ Contract sought to demonstrate that changing economic conditions had eroded the economic value of the Contract. Docket 5491, Procedural Order of 7/31/91 at 4-5 and Notice of Suspension, 3/25/91, at 1.

221. On August 7, 1991, in response to those assertions, CVPS witness Bentley testified that the Company was then engaged in negotiations with Hydro-Quebec to effect a second return sale agreement but testified that such an agreement had not yet been

---

52. Board Member Wilson and Mr. Stein engaged in the following colloquy:

> MR. WILSON: You recall that I asked you earlier whether there was already a target that if you reach that target, you would lock in. Is it fair to assume that in fact you told the [Company's] board here's what I think we need to get? If we can get this, we should lock in, that that would be a normal assumption, what you might --
>
> MR. STEIN: Yes, but the number, the 78% was literally not agreed to until whatever the last negotiation session that we had with Quebec was, which was sometime in August, I believe. So I'm not sure that I was not able to say with precision we're trying to do this. *I know that at that point in time it was clear that we were not going to get full price*, but it was not known at that time what price we would get and, you know, the board gives management wide latitude to -- you're doing the right thing, this looks like the way to go.

Tr. 9/9/94 at 50 (emphasis added).

reached. Mr. Bentley was (and is) the Company official responsible for CVPS's Integrated Resource Plan. Docket 5491, tr. 8/7/91 at 87, 126.

222. At that time, Mr. Bentley testified that he believed that the Company would be able to resell (to HQ or another utility) some portion of Contract power at full cost. Mr. Bentley also testified that he believed that the price of Contract power exceeded somewhat the market price for power at that time.[53] *Id.* at 100, 122-126, 131.

223. Mr. Bentley also testified at that time that the Company was planning to evaluate its current entitlements to HQ power in a "contingency" study to be filed in New Hampshire on September 15, 1991. There is no evidence in the record of this case to demonstrate that such a study was actually performed between that time, August 7, 1991, and the day that the VJO locked in the Contract, fewer than twenty-one days later. Docket 5491, tr. 8/7/91 at 97-99 and tr. 8/7/91 (sealed) at 21-22[54]; exh. EMA-B.

224. In its negotiations for the second return sale agreement, CVPS told HQ that, in the absence of such an agreement, the Contract would be cancelled. Tr. 9/8/94 at 29.

---

53. The August 7, 1991 hearing included the following dialogue between Mr. Bentley and the Chairman:

> MR. COWART: . . . . CV is now negotiating to sell something to Hydro Quebec. You don't know how much; is that right?
> THE WITNESS: That's right.
> MR. COWART: Suppose Hydro Quebec doesn't want to buy it?
> THE WITNESS: Okay.
> MR. COWART: Is it your judgment that CV would be able to sell that something to somebody else at full cost?
> THE WITNESS: Yes, it is.

Docket 5491, tr. 8/7/91 at 122. A few moments later, in response to a question from counsel for one of the parties, Mr. Bentley said: "And I did state previously that offers that we have put out on the table have not been warmly received, but it's not my testimony that we cannot sell the power at full cost. I just don't know that yet." *Id.* at 131.

54. Part of the hearing on August 7, 1991, was held *in camera* and the transcript was sealed. On October 3, 1991, the transcript and sealed documents in the record were made public without objection by any party. *See* CVPS Letter of 10/3/91.

225. CVPS and HQ had reached a tentative agreement on the terms and conditions of the second sell-back by August 21, 1991. EMA pf. at 63.

226. Hydro-Quebec did not require NEB approval to enter into the return sales agreements. *Id*. at 54.

227. On August 28, 1991, the VJO notified the Board that they and Hydro-Quebec had agreed that the extension to November 30, 1991, was no longer required and that both parties viewed the Contract as binding, with full liability accruing for default. Docket 5330-F, Order of 11/26/91 at 3.

228. CVPS agreed to lock in the Contract after it had completed its negotiations for the second return sale agreement. Stein/Page pf. at 36; *see* Finding 215.

229. There had been opposition to the Waiver from other Vermont utilities; that is, there had been, and remained throughout the spring and summer of 1991, significant

pressure on CVPS from other Vermont utilities to lock in the Contract.[55] Tr. 9/7/94,

---

55. In response to questions from Board Member Rude, CVPS witness Stein testified as follows:

> MS. RUDE: [I]t always struck me that Central Vermont's deal originally was much more front-end loaded in your take than many other utilities'. . . . So, I'm wondering if the other utilities at the time were saying to you: . . . we think this is a really good deal for us. We want to lock in. And you are saying: we are not happy with it yet. We want to wait. So that --
>
> MR. STEIN: I don't remember the specific conversations about how that was negotiated. I certainly remember that it was not easy to convince everyone that we should delay the lock in. There were many, many forces, including the government of Vermont, that wanted this contract locked in in April.
>
> Now, to your point about the early take and the late take. Again, I don't know. We had a forecast of need earlier than the other utilities did and we acted on that and we also reserved a big, cancellable piece out in the out years instead of taking more in the out years. It was a different strategy. We can all debate whether -- who had the right strategy and it's not all played out yet.
>
> MS. RUDE: So, there was never any discussion on the part of Central Vermont with the other utilities to say: you want us to lock in fast, you [other Vermont utilities] take a little bit more of ours, or something?
>
> MR. STEIN: No.
>
> MS. RUDE: There were no swaps you at all considered with other VJO at that time saying basically: we are taking on a little bit more of the risk here and you folks want us to move forward faster, so you take on little bit more of the risk?
>
> MR. STEIN: I don't think you could have renegotiated the shares of that contract among the Vermont utilities. We

Vol. II at 426-429; tr. 9/8/94 at 25-27.

230. In August 1991, the New York Power Authority ("NYPA") and Hydro-Quebec agreed to a one-year extension of the cancellation date of their long-term contract for the sale to NYPA of 1,000 MW of power and associated energy. Docket 5330-C, tr. 10/21/91 at 119, 122.

231. On September 5, 1991, CVPS filed its first integrated resource plan ("IRP") pursuant to the Board's April 16, 1990 Order in Docket 5270. That IRP treated the Company's entitlements to HQ Contract power as committed, *i.e.*, non-avoidable, and made no mention of the planned contingency study.[56] Rosen pf. at 35-36; Docket 5270-CV-4, Order of 3/24/94 at 10-11 (IRP at §IIIC).

232. CVPS notified the Board of the terms of the second return sale on October 3, 1991. Docket 5330-C, Order of 2/11/92 at 2, 14.

The Changing Economic and Power Market Conditions and CVPS's Analyses of its Share of the Contract

233. During 1989 and the several years following, the real prices of fuels for electric generating facilities were falling. In addition, the overall economy of Vermont and the region was deteriorating during this period. Rosen pf. at 42-44; tr. 9/8/94 at 133.

234. In preparation for the June 17, 1991 meeting of CVPS's board, the Company did not perform a re-optimization analysis of its entitlements under the HQ Contract or a new contract. It did not do so at any other time during 1991. Nor did it attempt to determine the optimal level of return sales in preparation for its negotiations with HQ. Tr. 9/9/94 at 51; tr. 9/8/94 at 59; Docket 5491, tr. 8/7/91 at 98-99; tr. 9/7/94, Vol. I at 164.

235. CVPS conducted a series of analyses in February, April, June, July, and October 1991. In each case, the analysis was merely dedicated to determining the value of CVPS's HQ Contract entitlements as a whole (*i.e.*, "HQ in" compared to "HQ out", to be replaced by generic units or other purchases) or the value of various sell-back alternatives. None of these analyses was produced as a coherent study or document,

---

never discussed that. Tr. 9/7/94, Vol. II at 426-429.

56. On August 7, 1991, in Docket 5491, CVPS witness Bentley testified that, despite the fact that the Company was not legally committed to the HQ Contract, the Company was then treating the Contract as a committed resource. Docket 5491, tr. 8/7/91 at 91.

weighing the implications or establishing the reasonableness of the Company's decision to retain the as-yet uncommitted HQ Contract in its supply mix. CVPS was unable to provide any coherent "pros and cons" decision package prepared for or presented to the Company's Board of Directors in connection with the June 17, 1991 meeting. Exh. EMA-B; tr. 9/9/94 at 52; Rosen pf. at 6; Docket 5491, tr. 8/7/91 at 98-99; tr. 9/7/94, Vol. I at 164; Stein/Page pf. at 39; tr. 9/8/94 at 102-103.

236. In February 1991, CVPS estimated that its share of the HQ Contract would provide net present value benefits (1991 $) of approximately $65.0 million. In April, the Company's estimates of its share of the Contract's benefits ranged between $45.0 million and $16.2 million. In July, the Company's estimate of the benefits was approximately $16.0 million. This analysis also showed that the point at which the early years' cumulative present value losses (totalling $70 million) began to fall had shifted farther into the future, that is, to 2005. In sum, each successive analysis before the decision to lock in the Contract was made showed a strong trend of declining value and increasing risk for the Company's share of the Contract. Exh. EMA-B at 79, 101-143, 172, 184*ff.*, and 281; Rosen pf. at 8.

237. As the projections of the likely long-run economic benefits of CVPS's share of the Contract declined, the economic risks of the Contract were increasing with each new analysis. The mid-term cumulative losses were growing, and the year in which the cumulative losses were projected to start declining was moving farther into the future.[57] These trends all indicated that the risk was increasing that the Contract might never be cost effective. Rosen pf. at 8 (summarizing CVPS's internal analyses).

238. The changing projections demonstrate that CVPS's share of the Contract was becoming even more highly front-end loaded relative to the market costs of power during the early years of the Contract. The above-market costs of HQ power were expected to extend well beyond the first five years of the Contract. *Id.*; tr. 9/8/94 at 30; *see* Footnote 55, below.

239. By April 1991, NEPOOL's forecasts predicted that the entire New England region would have excess capacity for a longer period than had been previously expected. In fact, NEPOOL's 1991 forecast, released in the spring, showed a significant

---

57. In the June and July 1991 analyses, the maximum cumulative economic losses in the mid-term had become twice as great as the likely long-term benefits. Furthermore, the year in which the cumulative losses were expected to decrease was pushed out to 2005. Rosen pf. at 8.

drop in expected demand. Tr. 9/9/94 at 10; tr. 9/7/94, Vol. II at 397-404; exh. EMA-A (EMA-5).

240. In each year from 1987 through 1991, NEPOOL forecast progressively greater amounts of energy efficiency and load management savings to be captured by New England utilities. Actual DSM savings contributed to the region's growing capacity surplus. Tr. 9/13/94 at 64-74; exh. Board-J; exh. Board-K.

241. Between the late 1980s and August 1991, significant new supply resources came on line in New England. These included Seabrook, Millstone III, the NEPOOL/Hydro-Quebec Phase II interconnection, and a large number of qualifying facilities. These contributed to the region's capacity surplus and, in certain cases, required larger than average reserve margins.[58] Tr. 9/7/94, Vol. II at 397-404; tr. 9/13/94 at 61-63.

242. Economic conditions in Vermont and New England had begun to deteriorate by late 1990 and continued to worsen during 1991. The economic decline contributed to significantly lower than expected demand for power and energy in CVPS's service territory. Tr. 9/13/94 at 63-69.

243. The Company failed to adequately document its assessments of the risks associated with the declining economics of its entitlements under the Contract. Apparently, in August 1991, the Company was willing to bear the significantly increased risks that its share of Contract power might prove non-cost-effective, but CVPS failed to properly document its decision to do so at the time. Rosen pf. at 43.

244. In the absence of any detailed economic analysis of and consideration of the alternatives to the HQ Contract during the six-month period prior to the lock in (August 28, 1991), the prudence of the Company's decision to lock in cannot be established. However, the failure to perform the requisite analyses during this period was imprudent. Rosen pf. at 7; tr. 9/9/94 at 25.

---

58. The effect that a particular resource has on a utility's (and NEPOOL's) reserve margin is a function of, among other things, its size and the probability that it will suffer an unplanned outage. Large resources with high probabilities of going off-line, such as Millstone III and Seabrook, require large reserve margins.

Regulatory Actions

245. The Company, through the VJO, agreed to lock in the Contract without seeking any prior regulatory review or approval of their decision to do so.[59] Docket 5330-F, Order of 11/26/91 at 3-4.

246. Despite the fact that the 1991 analyses of its share of Contract power showed that the amount and duration of the early years' losses had significantly increased -- *i.e.*, a "ten-year problem" -- the Company did not consider negotiating a return sale to HQ for a term of greater than five years. The Company apparently believed that a longer term would have triggered Vermont Public Service Board review pursuant to 30 V.S.A. § 248. In CVPS's view, such a review posed significant risks. Tr. 9/9/94 at 55-60, 83-84; Finding 236.

247. Section 248 of Title 30 requires Board authority of utility power purchases of greater than a specified magnitude for more than five years.[60] 30 V.S.A. § 248.

248. The Board's Order in Docket 5330 required that the Vermont utilities:

---

59. The VJO argued that prior regulatory review of their decision to lock in the Contract was not necessary because:

> (i) the new "lock-in" had the same effect as the April 30, 1991 lock-in date that had originally been approved by the Board; (ii) because the decision to treat the Contract as "locked-in" fell within the range of managerial discretion allowed by the traditional law of utility regulation; (iii) because the decision fell within the range of managerial discretion expressly contemplated by the Board in its previous approval of the Contract; and (iv) because the prudence of the utilities' decision to advance the lock-in date could be tested in any future rate cases.

Docket 5330-F, Order of 11/26/91 at 3-4.

60. 30 V.S.A. § 248 reads in pertinent part:

> (a)(1) No company, as defined in section 201 of this title, may:
>
> (a) in any way purchase electric capacity or energy from outside the state, for a period exceeding five years, that represents more than one percent of its historic peak demand. . . .

> shall evaluate their needs under the Contract and shall make a determination of any amounts of the power and energy purchased under the Firm Power and Energy Contract that may no longer be requried. They shall, within thirty days, file with this Board and with all parties a statement of their efforts to negotiate in good faith the return sale to Hydro-Quebec of such amounts.

Docket 5330, Order of 10/12/90 at 41 (¶ 11).

249. In Docket 5330-E, in reliance on the VJO's expectation that a revised Amendment 3 (relating to cancellation and liability provisions) was to be negotiated, the Board ordered that:

> 2. If the Vermont Joint Owners intend to propose further amendments or waivers to the Contract, the VJO shall exercise all diligent efforts to obtain by September 15, 1991 any required remands from the Supreme Court of Vermont, as necessary to allow a reasoned consideration of the Amendments that they intend to propose.
>
> 3. The Vermont Joint Owners shall file any such proposal with the Board and all parties on or before September 15, 1991.

Docket 5330-E, Order of 4/30/91 at 18-19 (*see also* p. 17).

250. On August 28, 1991, the VJO agreed to lock in the Contract. The essential terms of CVPS's second return sale were set by August 21, 1991. Both actions were taken by CVPS without prior Board review. In fact, the Board was not informed of the terms of the second return sale until October 3, 1991. Docket 5330-F, Order of 11/26/91 at 1; Docket 5330-C, Order of 2/11/92 at 2, 14.

Discussion re: Power Supply Management

During 1990 and 1991, the economic bases that supported CVPS's commitment to the Hydro-Quebec Contract were steadily eroding. Because the growing negative effects were strongest in the early years, and because the Company had the largest contractual commitments in those years, this erosion was much greater for CVPS than for any other Vermont utility. And, critically, both the Board and the Company recognized these facts.

As the evidence in this case demonstrates, the Company's decision to lock in its commitment to the HQ Contract is directly linked to the second return sale agreement. The record on this issue reveals significant failures and errors of judgment on the part of the Company in its power cost management between April and October 1991. Management's errors include:

- The decision to prematurely lock in the HQ Contract before considering all possible alternative strategies for managing the Contract and potential return sales;

- The failure to treat the Contract as an uncommitted resource and to fully analyze all possible alternative strategies for managing the Contract, including reoptimization of CVPS's entitlements to Contract power, either with Hydro-Quebec or other Vermont utilities;

- The failure to have developed an assessment of the appropriate level of return sales prior to beginning serious negotiations with Hydro-Quebec;

- The failure to have sought a second return sale for a term of greater than five years; and

- A pattern of misleading and incomplete information provided to the public and the Board, including the failure to fully inform the Board during the August 7, 1991 hearing of the internally expected and likely outcome and price terms of its negotiations for the second return sale.

The record in this case reveals that CVPS was repeatedly put on notice that its actions with respect to the Contract, return sales, and their effects on energy efficiency programs would be subject to regulatory review in future rate cases. Despite these clear warnings, the record demonstrates that the Company did not analyze or document several key decisions; that the Company deliberately sought to avoid prior regulatory review of its commitments; and that this policy of avoiding review included providing the Board with incomplete and misleading information, and led to self-imposed restraints on the Company's resource options.

The Company asserts that its decisions to lock in the Contract some three months before the expiration of the Waiver and to effect the second return sale agreement were sensible and prudent. CVPS Brief, Vol. III at 77*ff*.

DPS witness Rosen stated that he "cannot determine whether or not CVPS was or was not imprudent in locking into the HQ contract in August, 1991." Rosen pf. at 43. However, Dr. Rosen did testify that CVPS failed to perform the appropriate analyses to evaluate its various options in 1991, including the reoptimization of its entitlements under the Contract. This, contends Dr. Rosen, was imprudent. Tr. 9/9/94 at 25-26.

In April 1991, the VJO and Hydro-Quebec negotiated a six-month extension of the lock-in date of the Contract; the extension was referred to as a "waiver" of the previous commitment to an earlier lock-in date. One purpose of the Waiver was to enable CVPS to negotiate a second return sale agreement. At the same time, HQ also had its own reason for deferring a commitment to the Contract. This was because HQ was, at that time, dissatisfied with the conditions imposed on its export licenses by the NEB. By the end of April, when the Board approved both the Waiver and the first return sale agreement, CVPS was already negotiating the second agreement. Findings 205, 212, 215, 229.

In approving the Waiver, the Board stated:

> The VJO [Vermont Joint Owners] also agree that utility management has a legal obligation to prudently manage the contract so as to procure reliable power at the lowest long-term cost to ratepayers. They acknowledged that, in future rate cases, the Board could review the prudence of their decision to waive potential damage claims; however they note that such a prudence review must focus on the information that now is (or should be) available to them, rather than upon knowledge gained from the actual playing out of future events.

Docket 5330-E, Order of 4/30/91 at 3-4. Furthermore, we stated that:

> Finally, we agree with all witnesses' testimony that Vermont utilities should seriously explore alternatives to the HQ Contract, for use in the event that Hydro-Quebec does ultimately withdraw from the Contract. Indeed, even the most optimistic descriptions of Hydro-Quebec's potential actions make clear that there is a substantial chance of contractual termination by Hydro-Quebec, even if the Waiver is approved. Under these circumstances prudent utility managers must actively seek out other options and consider negotiations with potential alternative sources of efficiency or supply within the next few months.[61]

Id. at 18.

The Company's initial proposal (presumably in April, but certainly well before July of 1991) was for a second return sale of power and associated energy at full cost; this proposal was, in essence, similar to the at-par, or full-cost, terms of the first return sales agreement. Hydro-Quebec rejected that offer and informed the Company that it would not make a full-cost purchase of Contract power. Finding 217.

Throughout the spring and summer, CVPS analyzed several supply alternatives to its share of the HQ Contract, including purchases from Northeast Utilities, generic units, and the proposed Bonneville facility. In each case, CVPS's share of Contract power was projected to provide positive net present value benefits to the Company's ratepayers. However, the value of those comparative benefits declined significantly and consistently over time as economic and market conditions in the region deteriorated. Findings 236-237; exh. EMA-B at 79, 85, 101-143, and 172.

On June 17, 1991, CVPS witness Stein gave a crucial presentation to the Company's Board of Directors, detailing the HQ Contract, its value to the Company and ratepayers, and the intent and status of negotiations for the second return sale. If it had

---

61. Although we did not expressly state at that time that the utilities must also reevaluate the economics of the Contract, the analyses required in this instance would plainly reveal whether the Contract's cost-effectiveness had changed. *See also* Docket 5491, tr. 8/7/91 (originally confidential) at 22.

not been clear before that time, it was certainly understood then *within the Company* that the return sale would not be made at full Contract prices. It was also the point at which CVPS's Board of Directors gave management the discretion to decide when to lock in the largest financial commitment made by the Company since the Seabrook contract almost twenty years earlier. Findings 202, 218.

In July 1991, the Company evaluated a number of return sale scenarios, each of which improved the benefits of CVPS's share of the Contract. However, for framing its position in the negotiations with HQ, CVPS performed no analysis to determine the optimal level of return sales. Findings 234-235.

Evidentiary hearings in a CVPS general rate case were held in early August 1991, after the Board of Directors' meeting but before CVPS and the VJO locked in the Contract. In those hearings, the Company presented extensive testimony on the Contract, its place in the supply portfolio, the status of return sale negotiations with Hydro-Quebec, and the expected price of power under a second return sale. To address those issues, CVPS presented the testimony of Mr. Bruce Bentley, who managed the Company's integrated resource planning process, *In re CVPS's request for a 14.9% rate increase*. Finding 221.

In that case, CVPS witness Bentley testified that the Company was then negotiating a second return sale agreement with HQ, and that he had no reason to believe that a return sale would not occur at full Contract prices. He also testified that regional market prices for short- to medium-term power were falling. Findings 221-222.

Mr. Bentley also testified at that time that the Company was planning to evaluate its current entitlements to HQ power in a "contingency" study to be filed in New Hampshire on September 15, 1991. There is no evidence in the record of this case to demonstrate that such a study was actually performed between that time, August 7, 1991, and the day that the VJO locked in the Contract, fewer than twenty-one days later. Finding 223.

By August 21, 1991, CVPS and HQ reached a tentative agreement as to the terms of the second set of return sales; however, the Company did not inform the Board of this fact until October. On August 28th, the VJO notified the Board that they and Hydro-Quebec had agreed to lock in the Contract, three months before CVPS's discretion would have expired under the terms of the Waiver. Findings 206, 225, 227.

On September 27, 1991, this Board issued a final Order in Docket 5491, CVPS's general rate case. In that Order, we found that:

> Central Vermont plans to study the Hydro-Quebec contract, including an examination of whether the net present value of Hydro-Quebec is still positive. Such a study is timely. There is reasonable evidence to suggest

> that CVPS may still be committed to marginally uneconomic purchases from Hydro-Quebec in the early years of the HQ/VJO Contract, and that additional return sales could increase the present value of the purchase for CVPS and its customers.

Docket 5491, Order of 9/27/91 at 6; *see also* Finding 223.

On October 3, 1991, CVPS notified the Board that it had executed a second return sale agreement with HQ, effective October 1, 1991. The letter contained terms showing that not all of these return sales would occur at full cost. This was the first notice to the Board or public that the second return sale would not be on a full-cost basis. A hearing to review this second agreement was held on October 21, 1991. Finding 206; Docket 5330-C, Order of 2/11/92 at 1.

In November 1991, the Board issued an Order which addressed the August 28th notice to lock in the Contract and a complaint in response to that notice. Because the underlying case was on appeal before the Vermont Supreme Court, we concluded that we did not have jurisdiction at that time to act upon the notice or the complaint. Docket 5330-F, Order of 11/26/91 at 1. We pointed out, however, that:

> The Vermont utilities contended that prior regulatory review [of their decision to accelerate the "lock-in"] was not required because . . . the prudence of the utilities' decision to advance the lock-in date could be tested in any future rate cases.
>
> • • •
>
> Our previous Order noted (as the utilities now remind us) that significant managerial discretion is essential to the "efficient management of commercial contracts in general and of utility contracts in particular." However, that Order also noted that such decisions -- like all exercises of managerial discretion -- can be reviewed when the utility seeks to recover the resulting costs in future rate cases. At that time, the decision to accept an early lock-in date will be subject to the same test as other fundamental managerial decisions -- whether the decision was reasonable and prudent given the knowledge that the utilities had, or should have had, at the time that they agreed to acceleration of the lock-in date. That protection is as important now in regard to the accelerated lock-in date as it was in April in regard to the deferral of the lock-in date.

Id. at 3-5 (emphasis in original).

In February 1992, we approved the second return sale agreement. As we stated at that time:

> In April 1991, we approved an extension of the parties' "lock-in" date for the Hydro-Quebec Contract until November 1991, and we directed the Vermont utilities to explore other options carefully during 1991. However, in August of that year, the VJO and Hydro-Quebec mutually agreed to waive their rights to cancel the Contract.
>
> Vermont's utilities did not seek or require prior regulatory approval for that waiver. And the Vermont Supreme Court did not grant intervenors' request that the Contract be remanded to us for reconsideration of the original judgment. We therefore have neither heard evidence nor

> addressed the effects, if any, of recent market changes on the findings in Docket 5330.

Docket 5330-C, Order of 2/11/92 at 14. In a footnote to this section of text, we reminded the utilities that "Of course the prudence of the early lock-in decision will be subject to review in future cases." *Id.*, n. 13.

The Company argues that, because of declining prices in the short- to medium-term power market, Hydro-Quebec could effectively refuse to purchase Contract power at less than full cost. Tr. 9/8/94 at 32-34. We do not find this argument persuasive.

Because the VJO had not yet committed to the Contract, CVPS's effective power to cancel it in the absence of a satisfactory reduction to the early years' deliveries was a powerful negotiating tool. Fundamentally, Hydro-Quebec was a *seller* of long-term power, not a buyer of short-term power. CVPS has not demonstrated that it fully exploited HQ's strong incentive to preserve the overall Contract. This was especially true as regional, long-term power markets softened and as the possibility grew that New York would re-evaluate and could withdraw from its own contract with Hydro-Quebec.[62] CVPS has asserted that HQ's probable response to the New York situation would be to cancel the Vermont contract as well. We find this theory to be unconvincing and, furthermore, it raises doubts about managerial judgment if the Company actually relied upon it at that time. Reductions in competing buyers could only increase HQ's financial incentive to take all necessary steps to preserve its overall contract with Vermont.

The Company now seeks to persuade us that it committed early to the HQ Contract because of pressure from other Vermont utilities and state leaders to agree to lock in the Contract. Of all the utilities, CVPS had the largest overall share of power from the early schedules. Docket 5330, Order of 10/16/90 at 223-225. It was this large early purchase that had the greatest negative impact on the cost-effectiveness of the

---

62. At the time of CVPS's decision to lock in, New York had negotiated a one-year extension of its right to unilaterally withdraw from its contract with Hydro-Quebec. Finding 230. In February 1992, the Board elaborated on the distinctions between the Vermont and the New York relationships with Hydro-Quebec, observing that Vermont had a greater historic reliance on HQ than New York. Docket 5330, Order of 2/11/92 at 7-8. This observation is not inconsistent with our conclusion here that New York's insistence on an extension would naturally increase, rather than decrease, Hydro-Quebec's interest in maintaining a sales agreement with Vermont.

Company's entitlements to Contract power. Yet, CVPS's testimony in this case explicitly recognized that the Company failed to explore ways of reallocating that power among the Vermont utilities in return for its consent to lock in the Contract. Finding 229 (footnote 55).

CVPS also failed to conduct comprehensive analyses of the wider range of alternatives that were available. Although on several occasions the Company tested the Contract against other supply options, such as generic units and other purchased power contracts, it appears never to have seriously considered Contract power as anything but committed -- that is, unavoidable. Yet, the regional economy and wholesale market conditions had significantly changed since the Contract negotiations and subsequent hearings in Docket 5330 (1988-1990). The declining cost-effectiveness of the Contract and its consequent increasing risk were not adequately evaluated by the Company.

Perhaps the most serious of these deficiencies was a failure to respond to declining regional power costs, which stretched out -- to well over five years -- the period of time during which the early purchases were expected to be measurably above market costs. However, the Company did not even consider negotiating a return sale for greater than five years. The Company's witness testified that the reason for this self-imposed limitation was a desire to avoid a public regulatory review of the sale under 30 V.S.A. § 248, which is triggered in part by a contractual purchase of more that five years' duration. Upon this record, we can only conclude that this decision by CVPS's management was seriously in error.

First, as Exhibit EMA-B shows, CVPS's own analysis demonstrated that the losses associated with its early-year Contract entitlements were growing in magnitude and duration, rising steadily until the year 2005. Finding 236. In this context, a decision to negotiate return sales for only the first five years makes little sense. This is especially true since the Company's main bargaining leverage was the effective ability to cancel the Contract. Finding 215. Once CVPS agreed to lock in the Contract in return for the second return sale agreement, that powerful negotiating tool was lost. Therefore, we conclude that CVPS management failed to consider contract terms that might have greatly benefited its ratepayers.

Furthermore, we find no justification to the argument that the term of the second return sale needed to be limited to five years in order to preclude regulatory review under the applicable law: § 248 reviews are precipitated by specified proposals to

purchase power, not to sell it.[63] Finding 246. The length of an off-system sale to a non-Vermont utility has no bearing on the statutory authority under which the Board reviews such sale.[64] A return sale period of more than five years would not have exposed either the second return sale or the original Contract to the risk of a lengthy regulatory review. It is not clear how the Company's management came to this legal conclusion. However, we can only conclude that management as a whole, rather than ratepayers, must bear the responsibility for this strategic error.

Review of this decision against the backdrop of the other events can only lead us to the conclusion that it was consistent with a general CVPS goal of delaying public recognition that the return sale would be at less than CVPS's purchase price -- and that CVPS had agreed to accept that condition *before* it needed to make a binding commitment to the overall Contract.

During hearings in August 1991 on its request to increase its rates, CVPS did not offer the testimony of a Company official who was directly involved in the return sale negotiations with HQ. At that time, the record in this case demonstrates that upper management and the Board of Directors were fully aware that Hydro-Quebec had set out a bargaining position that would require CVPS to pay a higher price for power than Hydro-Quebec would itself pay for that same power. However, even in response to the Board's clear and repeated questions on this topic, the Company's testimony in August 1991 on this point was uninformed, equivocal, and misleading. There is no point in debating whether this was because of a lack of personal knowledge by the Company's witness at that time. That witness, the Director of Integrated Resource Planning, was sponsored by the Company, which asked this Board to rely upon his competence; he testified in the presence of the Company's legal staff; and CVPS, as a corporate entity, was responsible for ensuring the presentation of a knowledgeable witness upon this point

---

63. Likely transaction costs and delays are appropriate considerations in any business decision; and reasonable estimates of regulatory needs fall in that category. However, an unanalyzed desire to avoid regulatory review cannot support a decision to seek only a five-year return sale when a longer contract would have reduced excessive power costs.

64. Sale of corporate assets (including contractual rights) are covered by a very different statute, 30 V.S.A. § 109, which probably would not have applied to a return sale of the size and duration at issue here.

or, at a minimum, expediently correcting inaccurate statements in Mr. Bentley's testimony.

We must note that we did *not* find that CVPS's return sale to Hydro-Quebec was in error when we reviewed it in October 1991. At that time we appropriately found that:

> The [second return sale] Agreement is expected to increase the net present value of Contract power to CVPS by approximately $19 million.
>
> • • •
>
> In sum, the record demonstrates that the total price for capacity and energy to be paid by HQ under the Agreement exceeds CVPS's projected avoided costs for this type of power during the Agreement's five-year term. . . . Speaking accurately, no loss is caused by this sale. It is a sale of committed but unneeded power at well above prevailing market prices; thus the sale represents a gain, rather than a loss.

Docket 5330-C, Order of 2/11/92 at 18, 20. A key distinction in our findings here is that the cited Order reviewed CVPS's options *after* it was committed to the Contract; in contrast, we are now reviewing CVPS's actions prior to its agreement to lock in the Contract, when different data and options for action were available to the Company. We had offered CVPS on numerous occasions clear notification that their actions and analyses during this crucial time frame would likely be subject to regulatory review. Despite these warnings, the Company either did not prepare or did not maintain various data and documentation in support of its decisions. In other factual circumstances, this may have been considered an understandable omission. In the context of this case, however, we must conclude, as did the DPS, that CVPS's inability to produce coherent analyses is evidence that the required analyses were simply not undertaken or were purposely not documented. These facts, along with serious misjudgments about applicable Vermont law and evidence that CVPS provided misleading statements to the Board which were not subsequently corrected, lead us to conclude that the Company made serious errors in its power supply management in the summer of 1991, errors that, at a minimum, lost for CVPS ratepayers significant opportunities for power cost savings.

We need not now speculate as to whether knowledge that the return sale would be below full Contract prices, that expected benefits of the Company's entitlements under the HQ Contract were significantly declining, and that the pay-back period was lengthening would have led us to seek a remand of the case on the overall Contract from the Supreme Court. Nor can we judge whether such knowledge would have affected the Supreme Court's decision on the remand question. The fact remains that the Company's pattern of non-disclosure and misleading statements during this period -- even in closed proceedings with sealed transcripts -- deprived the Board of the opportunity to make such a judgment prior to the date of the lock-in. Therefore, as we stated in our Order of February 11, 1992, we were unable to take evidence on the effects of the region's

changing power market and how those changes might have affected our findings on the overall HQ Contract. Docket 5330-C, Order of 2/11/92 at 14.

At this point, we need only observe that misleading the public and the relevant regulatory authorities about material facts relevant to a crucial financial commitment is, in and of itself, grounds for a substantial reduction in otherwise appropriate earnings.

Discussion re: The Department's Ratemaking Proposal

The Department asserts that CVPS's mismanagement of its overall power supply portfolio will cause ratepayers to bear excess costs over the next 30 years totaling approximately $113 million, present value (1994 $), or $19.2 million per year for nine years (levelized). DPS Brief at 97-98. The DPS proposes a particular method for removing those costs from rates. While the DPS has demonstrated that a significant problem exists, and a remedy in this rate case is proper, for the reasons that follow, we do not find that the DPS's proposed approach is the appropriate remedy to the Company's mismanagement of power costs.[65]

Specifically, the Department urges the Board to adopt an economic, or market, test to determine whether a resource or group of resources is used and useful for the purposes of setting rates. Dr. Rosen, the DPS's witness on this issue, recommends that, during a rate case, the Board perform a life-cycle cost analysis of a resource, compare its total costs (in present value terms) to the present value of the least-cost alternative method for meeting the demand that the resource in question would otherwise supply, and, to the extent that the resource's costs exceed those of the alternative, deem the excess to be a measure of the non-used and useful portion of the resource. Dr. Rosen then recommends that, as has been done in other instances, half of this excess amount should be removed from rates, effecting a 50-50 split between ratepayers and shareholders of the costs of non-used and useful investments. If, on the other hand, the resource is found to be less costly then the alternative, then no disallowance should be made. DPS Brief at 88-104; Rosen pf., *generally*.

The Company opposes the Department's recommendation, arguing that such a test:

---

65. The Department did not present evidence on the narrower question of whether the power actually involved in the second return sale, known to be surplus before the commitment was made to purchase it, is used and useful. Thus we do not rule on that question.

- Is a radical departure from the traditional regulatory model in that it treats used and usefulness as an economic, rather than physical, concept;
- Would make rational power planning impossible;
- Constitutes, in certain instances, retroactive ratemaking;
- Would increase the cost of capital; and
- Creates an asymmetrical profile of risks and rewards for ratepayers and shareholders, unfairly benefiting the former at the expense of the latter.

CVPS Brief, Vol. III at 16-17, 152-214; Laber pf. at 3; tr. 9/8/94 at 117-118.

In essence, the Department's "economic used and useful (or excess capacity) test" is a market-based approach and operates, in part, on the logic that ratepayers should not have to pay more for electricity than it would -- *at one specific point in time* -- cost to purchase on the open market. That idea has an obvious appeal, particularly in situations where embedded monopoly costs exceed market costs. However, for the reasons which follow, we conclude that under current conditions Dr. Rosen's proposed adjustment is flawed and must, therefore, be rejected.

To begin, the Company argues that the DPS proposal introduces a new, hitherto unrecognized definition of "used and useful." CVPS witness Laber states that "There is a clear distinction between an asset being uneconomic -- *i.e.*, high cost in the face of current alternatives -- and being excess or not useful to the capacity needs of the business." Laber reb. pf. at 4. He notes that, in competitive markets, if an asset is uneconomic it can still be used to produce output; the firm merely incurs the loss associated with paying higher than market costs to produce its products.[66] *Id.* at 4-5. He points out that, in these circumstances:

> The capacity . . . is used and useful; it is simply uneconomic in the face of *current* market prices. Of course, the reverse could be true: If current . . . rates are above the level in the contract, the asset is very attractive. In neither case is there excess capacity in an economically meaningful way.

Id. at 5. He goes on to argue that this example accurately describes utility power plants as well. *Id.*

Dr. Rosen asserts that excess capacity should be considered from both reliability and economic perspectives. Rosen pf. at 20. He states that:

---

66. Dr. Laber apparently assumed in this example that the firm's variable costs of production are fully covered. Actually, Dr. Laber described an example from the real estate market, but the principles apply to all competitive economic activity.

> However, simply knowing the amount of physical excess capacity on a system does not tell one whether that capacity is used and useful. . . . An economic evaluation is needed to determine the extent to which the power supply resources will likely be "used and useful" in terms of providing reasonably low-cost electricity service over the foreseeable future.

Id. at 20-21. He later asserts that an economic valuation to determine what portion of an asset is used and useful has been employed in a number of states and, therefore, there is nothing "radical" in his approach at all. Rosen reb. pf. at 2-3.

Dr. Laber recommends that the Board employ a physical, operating definition of used and useful, whereas Dr. Rosen urges adoption of an economic definition. However, Dr. Rosen's assertion that his approach is supported by a number of precedents was not borne out in our review of those cases.[67]

It is not necessary to describe those cases in detail here. Although they were resolved in other jurisdictions, they have informed our consideration of this issue. In their essential conclusions they walk part way down the path that Dr. Rosen recommends to us; but they stop well short of his specific recommendations in this case. Overall, the decisions cited by Dr. Rosen are consistent with our prior decisions in several Vermont cases that are directly relevant to our conclusions here.

Two of those cases are Docket 5132, *CVPS's request to increase rates (Seabrook issues)*, and Docket 5630 *et al.*, *VEC's request to increase rates and restructure its long-term debt*.[68] In both of these dockets, the Board found that portions of specific generating resources were not used and useful and disallowed certain costs associated with them. Those losses were calculated as the excess of embedded cost over market

---

67. The cases in question are: *Re Wolf Creek Nuclear Generating Facility*, Kansas State Corporation Commission, Docket No. 142,098-U, 70 PUR 4th 475 (Sept. 9, 1985) ("*Wolf Creek I*"); the 1986 Supreme Court of Kansas appeal of *Wolf Creek I*, *Kansas Gas and Electric Company v. State Corporation Commission of the State of Kansas, et al*, 239 Kan. 483, 720 P.2d 1063 (June 13, 1986) ("*Wolf Creek II*"); and the Massachusetts Department of Public Utilities Case, *Re: Western Massachusetts Electric Company*, Docket DPU# 85-270, 80 PUR 4th 479 (June 30, 1986) ("*Western Massachusetts*").

68. Cited as Docket 5132, Order of 5/15/87, 83 PUR 4th 432 (1987), and Docket 5330 *et al.*, Order of 12/30/93.

value, and were split evenly between shareholders and ratepayers.[69] As we recently stated in Docket 5630 *et al.*:

> Ratemaking decisions in Vermont have been consistent with those federal and other state determinations. Our decision in Docket 5132 examined those precedents in detail. . . .
>
> • • •
>
> In sum, six past precedents offer a consistent set of rules for calculating the rate effects of failed investments in major power plants:
> (i) if costs are imprudent, they cannot be included in rates;
> (ii) if costs exceed the degree to which projects are used and useful, only one-half of that excess is included in rates; and
> (iii) if an arms-length sale has occurred, the net benefits from that sale can be treated as a measure of the degree to which the project is used and useful.

Docket 5630 *et al.*, Order of 12/30/93 at 51-52 (citations omitted).

Dr. Rosen's proposal differs from our traditional method in a very critical way. He states that his test can be applied *at any time* during the life of a prudently-acquired asset to determine its used-and-usefulness; the effect would be that costs incurred at a time when the resource was deemed economically used and useful would remain at risk for a potential future disallowance. This test could also be applied to a resource portfolio as a whole, which in fact is what Dr. Rosen did in this case. Rosen pf. at 21-25, 65-73. It is this aspect of the proposal -- the life-cycle analysis of an existing resource, which includes past and projected costs -- that the Company argues constitutes retroactive ratemaking. CVPS Brief at 179. In this way, contends the Company, it is arbitrary and capricious. CVPS Brief at 155-156.

The Company's arguments have merit. As structured, Dr. Rosen's test would penalize investors for prudent investments that are, or had been, reasonably expected to yield net present value benefits over their lifetime, that are not excessive in scope, and that are still in service, but whose costs may exceed market prices at a particular moment in time. In this way, as Dr. Laber points out, Dr. Rosen's ratemaking approach may discourage utilities from making least-cost investments that fail a short-term market cost-effectiveness test. Laber pf. at 3.

When a utility petitions the Board to recognize an asset in rates, we may conduct an investigation into the prudence and used-and-usefulness of that asset. If an explicit review is conducted, those asset costs that are found to be prudently incurred and economically justified *at the time the asset is put into service* are allowed in rates. Only

---

69. In each case, this Board also found significant losses due to imprudence, and these losses were assigned fully to shareholders.

one-half of the costs associated with the non-used-and-useful portions of the asset, if any, are put into rates. Docket 5630 *et al.*, Order of 12/30/93 at 52; Laber reb. pf. at 6; CVPS Brief at 175.

After such a review, if an asset is "explicitly approved for placement in rate base" and its costs are deemed used and useful, it would be inappropriate to subject their continued recovery over many years to a year-by-year market test.[70]

Dr. Rosen's proposal also raises another concern; it would impose additional risks upon shareholders without offering commensurate returns for them. His approach provides that ratepayers will pay the lower of either embedded (historic) cost or market cost for a resource. If market cost is lower than embedded cost, shareholders will recover only one-half of the difference. In contrast, however, if market cost exceeds embedded, shareholders will recover only the full embedded costs: the difference between market costs and embedded costs flows to ratepayers in the form of below-market electricity rates.

In competitive markets, a company will not be able to recover costs that exceed the market costs of its products. Investors bear the risk that their investments will be uneconomic, in full or in part. However, that risk is symmetrical, which is to say that investors also reap additional benefits if they are able to produce their product at a cost well below its market price. Dr. Rosen's portfolio adjustment proposal does not offer CVPS's investors that opportunity and, therefore, must be rejected.[71]

For all these reasons, we decline the Department's recommendation to apply the "economic used and useful" test to previously approved portions of CVPS's overall resource portfolio.

We note, however, that our ruling in the present matter should not be construed as a finding that a market-value test is fundamentally unacceptable. As the Supreme Court pointed out in *Duquense Light Company v. Barasch et al.*, 488 U.S. 299, 316.:

---

70. *See* Docket 5132, *supra*, at 165. Our decision in the Seabrook case made it clear that we were not adopting a year-to-year market test, stating that we disagreed with the assertion "that our loss-sharing policy requires this Board to reopen old cases on the ground that previously economic investments have since become uneconomic."

71. Because we are rejecting the DPS's recommendation on this and other grounds, we need not reach a conclusion as to whether Dr. Rosen's approach would be contrary to the Vermont Supreme Court's prohibition against retroactive ratemaking.

> The designation of a single theory of ratemaking as a constitutional requirement would unnecessarily foreclose alternatives which could benefit both consumers and investors.

In a footnote to that text, the Supreme Court added that a fixed rejection of market value tests:

> would also foreclose a return to some form of the fair value rule just as its practical problems may be diminishing. The emergent market for wholesale electric energy could provide a readily available basis for determining the value of utility assets.

Id. at fn. 10. As utility markets become more open and competitive, it may become increasingly possible and, in many cases, desirable to employ market-based tests to govern the utility's total return.[72]

B. Demand-Side Management Programs

1. Introduction

In our Order of April 16, 1990 in Docket 5270, we inaugurated a major initiative designed to meet Vermont's future energy needs through utility integrated resource planning that would rigorously compare new energy supply options with conservation and load management alternatives, then select and implement least-cost resource acquisition strategies. Two years of intense consultation and formal litigation, in which Vermont utilities were fully engaged, preceded the issuance of a detailed policy statement and an extensive set of program guidelines. The Order initiated a process of planning, program design and program development in each of Vermont's electric utilities.

Subsequently, in our Order approving the Hydro-Quebec Contract, we expressly required all Vermont utilities accepting power under that Contract to implement measures to acquire all resources available from cost-effective energy efficiency. Docket 5330, Order of 10/12/90, at 40. In 1992, the Vermont General Assembly adopted amendments to Section 218 of 30 V.S.A. that obligate Vermont utilities to undertake least-cost integrated planning for comprehensive energy efficiency programs.

The introduction of cost-effective demand-side management programs has been embraced by Vermont's larger utilities with varying degrees of enthusiasm and commitment. Several have moved forward with well-designed, comprehensive programs

---

72. The Company agrees that some form of market-based regulatory regime may be appropriate in a more competitive environment. CVPS Brief, Vol. III at 154; Cater reb. pf. at 1; tr. 9/8/94 at 183-184; EMA reb. pf. at 13.

that have achieved significant cost-effective savings and reductions in energy consumption. For all, the process has been one of exploration in unfamiliar analytical territory where trial, error and readjustment have become routine.

We have provided guidelines, but not a straightjacket for utility planning and programs. Each of the larger utilities has developed its unique approach, and most are achieving substantial savings for their customers. We have not expected uniform results. We recognize that each utility has its particular opportunities and constraints reflecting size, customer characteristics, population density and dispersion, rate structure and power sources and costs. Nevertheless, at the level of overall accomplishment, we can learn a great deal by comparing the performance of any one utility against that of other utilities in its general class.

In this Docket, the DPS asserts that CVPS has mismanaged its least-cost planning responsibilites for DSM. DPS Brief at 172. Extensive evidence in this case compellingly demonstrates that CVPS has been deficient in many aspects of its approach to and execution of its demand-side management obligations. Our specific areas of dissatisfaction are discussed below. We are judging CVPS's performance on the evidence before us of consistent failure to meet the utility's own program design goals, overstated and inconsistent energy savings estimates, inadequate monitoring and evaluation, repeated non-compliance with Board orders based on alleged misunderstandings, inflated recovery claims, and unwarranted program modifications and deferrals. We also rely on record evidence of the standards and achievements of other large Vermont utilities as a benchmark for evaluating some of CVPS's programs.

CVPS assigns its principal responsibility for efficiency measures to its Vice-President for "Marketing and Public Affairs." This places it with the same officer's oversight of communications, government affairs, community relations, and an unregulated subsidiary that promotes electric appliances (Smart Energy Services). Notably, the duty to acquire efficiency resources is not treated as part of Integrated Resource Planning, which is separately assigned to the Senior Vice-President for "Engineering and Energy Resources." Exh. Board I (CVPS Organizational Chart).

This view of acquiring energy efficiency as a marketing and public affairs activity indicates senior management's resistance to acceptance of the concept that acquiring efficiency resources is an integral element in energy resource planning and management. It also raises concerns by creating an apparent incentive to implement efficiency programs in ways that will promote the profits credited to an unregulated subsidiary.

Issues relating to the design and implementation by CVPS of cost-effective fuel switching programs are being litigated in Docket 5270-CV-1&3. We do not wish to

prejudge or influence the outcome of that litigation. However, there are fuel switching elements in a number of the current programs that CVPS has included in its immediately pending claims for cost recovery and ACE treatment in this docket. Before allowing CVPS to charge ratepayers for the costs of those programs (or for power costs that might have been avoided by them), we must, of necessity, consider the evidence relating to CVPS's current rate request.

Most of the record evidence about problems with CVPS's efficiency programs relates to overstating achievements, and to failures of inaction. The record does not raise such serious concerns about the measures that the Company has, in fact, implemented. Thus, we have granted CVPS almost all of the program costs they have claimed because we find that those expenditures were made in pursuit of valid program objectives as originally described by the Company. We conclude that CVPS's programs have produced a minimally adequate amount of cost-effective energy efficiency savings, but that even that minimal level of achievement has been cost-effective when compared with supply resources and thus justifies recovery of most of the Company's program expenses.

However, the issue of excessive power costs that would have been avoided by better implementation of these programs is far more important than the direct costs of these programs themselves. Thus, we have allowed less than full ACE recovery in a number of programs. Also for these reasons, as discussed in Section VII.C., below, we have taken the Company's DSM performance into account in determining that a penalty for management deficiencies and misjudgments must be assessed.[73]

In Subsection 2 below, we review the obligations that the Company accepted when it committed to the Hydro-Quebec Contract. In Subsection 3 that follows, we discuss the problems we find with various aspects of the management of CVPS's DSM programs.

---

73. Testimony by several CVPS witnesses in this Docket argues that denial of C&LM expenditures and lost revenue (ACE) claims, or any penalty for poor performance would send a chilling and negative message to Company management, stockholders and the broader financial community. We cannot accept such an argument; energy efficiency expenditures are subject to the same level of regulatory review in rate cases as any other area of the costs of service. The record evidence documented below compels disallowances and is a strong contributing justification for reducing the Company's overall return on equity.

Subsection 4 contains our findings and discussion concerning specific programs and program issues. Subsection 5 states our conclusions.

Our intent in going into extensive detail in this Section, and particularly in Subsection 3, is not only to explain the disallowances and penalty, but also to make as clear as we possibly can the serious deficiencies in the Company's overall approach to comprehensive energy efficiency planning. We seek and would warmly welcome a manifestation of positive change in the CVPS management attitudes and intent, accompanied by a commitment to achievement regarding least-cost integrated resource planning and demand-side management programs that will reduce customer bills and long-term power costs.

2. Violation of Condition 8 of the Hydro-Quebec Contract

The Conservation Law Foundation contends that CVPS has violated a material condition of the Order approving the Company's purchases of power from Hydro-Quebec. The evidence persuades us that CLF is correct.

In this context three issues need to be addressed. The first is whether the condition is binding on CVPS. The second is whether it has been violated. The third is what, if any, penalty is appropriate.

As to the first question, the answer is clear. This Board's approval of the Hydro-Quebec Contract was conditional rather than absolute. Thus, acceptance of power under that Contract constituted an acceptance of those conditions. One of those conditions was a commitment to pursue all cost-effective energy efficiency measures. Its express terms are set out in Condition No. 8 of the HQ Contract approval order which states:

> Each Vermont utility accepting power under the authority of the Firm Power and Energy contract and this Order shall *develop and implement measures to acquire all resources from cost-effective acquisition of energy-efficiency* in accordance with the principles ordered by this Board in the final Order of April 16, 1990, in Docket No. 5270.

Docket No. 5330, Order of 10/12/90 at 40 (emphasis added).

It is beyond argument that CVPS, by accepting power under the authority of the Contract, accepted this condition and is bound by it. The issue of conditions was litigated immediately after the issuance of the Contract approval Order, and the utilities' own counsel filed briefs citing cases about the binding nature of such conditions *once the utility chose to engage in the conditionally approved endeavor.* In explicit reliance upon those filings, we accepted the utility arguments and found that such a condition:

> amounts, in essence, to a factual determination that a proposal will promote the general good if certain circumstances occur, and that it will not promote the general good if they do not.

Dkt. No. 5330, Order of 1/7/91 at 8. Three months later we again informed CVPS that we were rejecting their opponents' arguments because we would rely upon being able to enforce their commitments under Condition 8. See Dkt. 5330-E, Order of 4/30/91 at 15, reciting the full text of Condition 8 and stating:

> As the Vermont utilities have told us before, acceptance of the power implies acceptance of such conditions and renders them fully enforceable. See e.g., Order of 1/7/91, Docket No. 5330, at 8-10 (quoting VJO brief and counsel); Order of 3/1/91, Docket No. 5330-D, at 12; Order of 3/19/91, Docket No. 5270 CV-1, at 8, n.6.

The second question is whether Condition 8 has been violated. Given the explicit language of Condition 8, this must be resolved by deciding whether CVPS has:

> develop[ed] and implement[ed] measures to acquire all resources available from cost-effective acquisition of energy efficiency, in accordance with the principles ordered by this Board in the final Order of April 16, 1990, in Docket No. 5270.

In the following subsections, we review in detail the record upon the Company's management of its efficiency programs. For the reasons set out in that review, we can only conclude that the Company's current efficiency programs have not been developed and are not being implemented as parts of a good-faith effort to acquire all resources available from cost-effective acquisition of energy efficiency, in accordance with the Order of 4/16/90 in Docket No. 5270.[74] Thus, it is clear that the Company has violated Condition 8 of the Order approving the Hydro-Quebec Contract. Instead of seeking to acquire all cost-effective efficiency resources, CVPS has used budget limits, internal targets, methodological changes, deferrals and self-imposed program limitations. In practice the implementation of CVPS efficiency programs has been defined by these limitations, rather than by the scope of good faith efforts to *maximize* the net benefits of avoiding power costs.

---

74. In light of the significance of this point, we want to be very clear about the threshold standard here: we do not view Condition 8 as turning on the achieved acquisition of all such resources. Rather, its explicit terms require only the development and implementation of measures designed to do so. Good-faith efforts to develop and implement such measures constitute compliance with this condition. We have, in many other cases, seen Vermont utilities demonstrate good faith efforts to comply with this condition. However, the evidence now before us demonstrates that CVPS is an unusual exception to the general pattern of good faith compliance with Condition 8.

The third question is what penalty should be associated with such non-compliance.[75] Even before CVPS locked in to the Contract, we explicitly addressed remedies for non-compliance with Condition 8, treating it then as a hypothetical question:

> It is at least theoretically possible that a utility might accept the Paragraph 8 condition by entering into the Contract and then failing to comply with the condition in the future. If so, it is logical to presume one resulting 'risk' would be a Board order to resell some or all of the purchased power.

Dkt. No. 5330-D, Order of 3/1/91 at 12.

Sadly, that theoretical risk has become a reality. We now must decide whether to order CVPS to resell some or all of the purchased power or whether to impose a disallowance equivalent to the financial loss accompanying such a resale. Such a disallowance could lead to very serious financial implications for stockholders. Thus, we would determine the appropriate amount of such a disallowance only after more explicit consideration than it has yet been given in the record before us.[76]

Instead, given the overall balance achieved by our resolution of this case as a whole, we have decided not to impose such a penalty for past non-compliance. Instead, we will treat past non-compliance with Condition 8 as one basis for imposing a 75 basis point penalty upon the Company's overall return on equity. For the reasons outlined in Section VII, we conclude that this penalty should be imposed concurrently with that for

---

75. CLF, while urging a finding of non-compliance asserts that the penalty for such non-compliance need not be addressed at this time. We are not persuaded. Penalties for past violations should (to the extent feasible) be resolved before future rates go into effect. Continued future non-compliance, if any, will have to be addressed at some future time.

76. The Order of 5/15/87 in Docket No. 5132 concluded that the loss associated with a mandatory sale was measured by calculating the net losses from such a sale, after considering the original cost of the asset, its market value when sold, and relevant tax effects. The portion of that loss that was associated with unavoidable market changes was then divided equally between ratepayers and stockholders. Such a division would probably seem inequitable in a situation where the loss was caused by management's noncompliance with a legal condition it had previously chosen to accept.

overall mismanagement of efficiency measures and concurrently with the separate and independently justified penalty imposed for management's handling of power costs.

3. Program Design, Implementation, and Cost Recovery Issues

a. Rate Case Review

CVPS has frequently asserted in its prefiled, live and rebuttal testimony, as well as in its briefs, that CVPS's program designs were essentially collaborative, consensus programs, developed with the agreement of other parties and pre-approved by this Board. We have carefully reviewed the decisions in the cases cited by the Company (including Docket No. 5270-CV-1, Docket No. 5270-CV-3, the several proceedings in Docket No. 5270-CV-1&3 and numerous other similar proceedings involving other Vermont utilities). After doing so, we can only observe that no fair reading of those proceedings could support the issue-preclusion claims that CVPS now presses upon us.

We also note that -- at CVPS's express request -- for many of the program design issues discussed in the above Dockets, we overruled opponents' requests for pre-implementation changes in CVPS's programs and, instead, deferred to CVPS's filed program designs. As the Hearing Officer noted in Docket No. 5270-CV-1&3, Order of 5/4/93:

> The evidence in this Docket leads me to conclude that there are many outstanding questions regarding the likely success and ultimate cost-effectiveness of all of CVPS's proposed programs. However, my review also leads me to the conclusion that most, if not all, of the areas of uncertainty can be more easily resolved after CVPS gains experience through implementation of its programs. Thus, I do not agree with the DPS's proposal to withhold approval and require CVPS to re-submit new program designs (with an opportunity for comments from parties and Board hearings, if needed). Instead, I have identified the controversial issues, resolved as many as possible based on currently available information, required changes to CVPS's filed designs where appropriate, and referred many of the disputed elements to further monitoring and evaluation (M&E).

CVPS testified in this Docket that the Company is responsible for its program designs and the implementation of its programs. Tr. 9/6/94 at 170-171, 185-188. We have consistently stated our reliance upon that responsibility. We have also ruled that, *just as much as for supply resources*, CVPS's obligation to secure least-cost resources for its customers means that it cannot use the pendency of potential Board reviews of program designs as a reason for deferring implementation of programs that could avoid on-coming power costs. Docket No. 5270-CV-3, Order of 9/13/91 at 3-5; Docket No. 5270-CV-1&3, Order of 5/4/93 at 15-16.

Between our first Order accepting CVPS's program designs[77] of May 20, 1991, in Docket No. 5270-CV-3, and our last Order of May 4, 1993, we approved energy efficiency program designs for all five *other* large Vermont utilities covered by our Order of April 16, 1990, in Docket No. 5270.[78] This is significant for two reasons. The first is as a striking contrast to CVPS's inability to avoid power costs by developing and implementing programs that could do so with minimal regulatory conflict. Although all of those Orders required modification of certain elements of the proposed program designs, for the most part, we have allowed Vermont utilities to experiment with program designs that they believed were appropriate. As a result, most of them are acquiring substantial efficiency savings that will reduce the overall cost of service for their customers.

The second significance of those Orders is directly related to CVPS's current, implausible, claimed expectation that its efficiency expenditures will not be subject to review. We have clearly stated, in numerous Orders, that our approval of program designs cannot be construed as pre-approval of program expenditures. Docket No. 5270, 4/16/90, Vol. III at 161. It should come as no surprise to CVPS or any other Vermont utility that their energy efficiency expenditures -- just like their power expenditures -- will be reviewed in rate case proceedings.[79]

---

77. Allowing a program design to go forward is not the same as a ruling upon rate-recovery for that program, and it is miles away from approval of the later implementation of that design. These distinctions are fundamental, although it appears that they have received little recognition in much of CVPS's argument upon this point.

78. See Docket No. 5270-GMP-3, Order of 9/5/91; Docket No. 5270-BED-1, Order of 10/17/91; Docket No. 5270-WEC-2, Order of 1/30/92; Docket No. 5270-VGS-2, Order of 10/23/92; and Docket No. 5270-CUC-2, Order of 2/26/93.

79. Docket 5428, Order of 1/4/91 at 32-37. In Docket 5270-CV-1&3, Order of 5/4/93, at pages 109-110, we denied a request from the DPS that we determine that some of CVPS's DSM expenditures were imprudent. We said:

> The DPS will have an opportunity in a subsequent rate case to present evidence regarding the prudence of CVPS's implementation decisions. We decline to make any judgments at this time.

b. Maximizing Net Societal Benefits

A fundamental conclusion from our original, two-year investigation in Docket No. 5270 was that Vermont's utilities should seek to acquire the maximum amounts of cost-effective DSM resources as a component of least-cost planning. Docket No. 5270, Order of 4/16/90, Vol. IV at 3-7; Docket No. 5270-CV-1, Order of 3/19/91 at 3-4. This view was affirmed by subsequent Vermont legislation. See, 30 V.S.A. § 218c. It is also, for an independent reason, applicable to CVPS which, through its decision to purchase power under the HQ Contract, committed itself to Condition 8 of the conditional approval of that purchase. In Docket 5270-CV-1&3, Order of 5/4/93, the Hearing Officer reiterated this point and referenced other utility dockets where this point was made. In that Docket, the Hearing Officer reminded CVPS that we have expressly rejected CVPS's contention that program design decisions can be justified through the application of a "no losers" or rate impact test. Id. at 14-15.

Recent developments suggest that the electric utility industry may be facing some fundamental restructuring issues related to open access and retail competition. While new evidence, in future proceedings, may persuade us that rate impacts of utility activities should be given more consideration, we find that the standard against which CVPS's activities must be measured has not changed: it allows consideration of rate impacts at a program design level, but explicitly excludes rate impacts as the single and final decision tool. Ratepayer bill reduction and the achievement of a least-cost portfolio of services must also be given significant considerations.

A basic point here is that CVPS undertakes many activities, such as purchasing power, clearing its distribution lines, and operating service centers. Those operations have "rate impacts" that can far exceed those of DSM expenditures, yet the Company does not use similar arguments to avoid these responsibilities. We reaffirm, today, our support for the standard used to evaluate CVPS's initial program designs; that is:

> . . . is this program design likely to acquire the maximum amount of available cost-effective DSM resources?

Id. at 15.

c. Implementation of CVPS's Programs

CVPS contends that its C&LM programs have been, and continue to be, based on Board-approved principles of least-cost planning. In particular, CVPS maintains that changes to its initial Board-approved program designs have been based on field experience, monitoring and evaluation studies, updated avoided costs, and a deferral

analysis that demonstrates that net program benefits will be greater if certain programs are implemented in future years.

We recognize that some, but not all, of the issues regarding CVPS's program designs, and appropriate modifications to those designs, are being contested before Hearing Officers in concurrent proceedings in Docket Nos. 5270-CV-1&3 and Docket No. 5686. We anticipate a more extensive Board review of those issues when we consider the Proposals for Decision in those Dockets. Nonetheless, we have heard considerable testimony on these topics in this docket, and much of the record from Docket Nos. 5270-CV-1&3 and 5686 has been included in this proceeding.[80] In addition, many of the issues addressed in this proceeding go beyond the limited scope of Dockets Nos. 5270-CV- 1&3 and 5686. Furthermore, the Company's current rate request makes it essential to resolve some of these issues before determining what CVPS can now be allowed to recover from its captive customers. Therefore we offer the following observations at this time:

(1) The DPS raises significant concerns regarding CVPS's program design changes based on field experience. The DPS states that CVPS has made modifications to its programs that result in fewer participants, fewer measures installed, and lower total net savings. CVPS responds, in many cases, by referring to the fact that its modified programs are cost-effective, that the savings goals have been exceeded, and that utility programs costs are less than expected.

CVPS's argument requires an important observation: merely operating cost-effective programs is <u>necessary</u>, but is not <u>sufficient</u> to satisfy a utility's obligation to provide least-cost energy services to its customers. Without reaching any conclusions on specific disputes, we must remind CVPS that the achievement of self-set program goals is one important indicator of program success, but that the fundamental goal is to <u>maximize net benefits</u> through high levels of program participation and the installation of comprehensive packages of measures. Thus, programs must be cost effective and must <u>also</u> strive to acquire the maximum amount of energy savings that can be purchased for less than the cost of comparable power.

(2) The DPS criticizes CVPS for its selective implementation of monitoring and evaluation recommendations. The DPS criticisms raise the same points discussed above regarding field experience. CVPS's responses to those criticisms are similar as well. Again, without resolving case-by-case disputes, we reiterate our points, above, regarding fundamental goals of DSM program design. One additional point we are obligated to

---

80. Tr. 9/6/94 at 11; Exhibit List this Docket.

raise here is our awareness of CVPS's failure to promptly implement evaluation studies requested by the Board. One serious example is CVPS's failure to determine the impact of higher customer incentive levels for its fuel-switching measures.[81] An additional example is CVPS's failure to file an analysis of a hook-up fee approach for New Construction programs as requested in May, 1993.[82]

CVPS states that lost opportunity programs are a high priority. However, the Company's actions regarding New Construction programs do not support its claims; instead they demonstrate achievements that are, at best, rather meager. Findings 284, 286; 1993 DSM Annual Report.

(3) The DPS maintains that CVPS materially understates the avoided costs it uses to analyze the cost-effectiveness of its Amended Case programs.[83] This issue has been the subject of extensive testimony and cross-examination in CVPS's concurrent DSM Dockets. At this time, we need not reach a specific conclusion as to the precise best estimate of likely avoided costs. We are well aware that the determination of avoided costs will have a significant impact on any analysis of program cost-effectiveness and that this creates a significant motive to "game the system" by creating result-oriented avoided cost estimates. This means that the use of varying avoided cost estimates for varying purposes requires particularly rigorous justification. We add that simple intellectual consistency requires a serious degree of skepticism because of systemic incentives for a utility to allege high avoided costs to justify utility-sponsored power commitments or special discount contracts for selected customers, but to then claim low avoided costs when efficiency measures and non-utility generating projects are in issue.

---

81. See Docket 5270-CV-1&3, Order of 3/25/94. In addition, as discussed below at page 152, CVPS has only recently conducted such an evaluation.

82. In Docket 5270, Order of 5/4/93, we adopted the Hearing Officer's concerns regarding program participation levels and his recommendation that CVPS investigate a hook-up fee approach.

83. The effect of understating avoided costs is to understate the value of potential efficiency measures. Ratepayers risk paying excessive future power costs if an understated estimate of power costs leads to failure to pursue an efficiency program, followed by a "need" to acquire future power at a higher actual cost.

d. Deferral of Efficiency Programs

There is no dispute about the fact that the Company has deferred many of its efficiency programs. There is great dispute about the merits of those deferrals. CVPS's arguments regarding the benefits of program deferral have not been persuasive. In essence, CVPS maintains that delaying the acquisition of currently cost-effective resources until a later time period, when avoided costs are higher and measure costs are lower, will enhance societal benefits. CVPS's approach begins with a theoretically acceptable claim that might be valid under certain facts; however, CVPS has not taken the next step. It has not established that the deferrals recommended in its Amended case will actually achieve greater societal net benefits. In addition to the concerns related to program design changes and the accuracy of avoided cost estimates, as discussed above, we have several other concerns with CVPS's deferral approach.

First, we are not convinced that CVPS has appropriately excluded non-variable or sunk costs from the Amended case analysis. Just as the marginal cost of additional power production incorporates only the avoidable costs associated with each incremental kWh, the marginal cost of CVPS's DSM programs should include only avoidable costs associated with serving additional customers or installing additional measures. The record before us indicates that administrative overheads and monitoring and evaluation costs have been included on a per measure basis in CVPS's cost-effectiveness screening for its Amended case. Examination of CVPS witness Bentley demonstrated that the spreadsheets used to calculate CVPS's Amended case should not be relied upon. Tr. 9/13/94 at 48-56. These spreadsheets form the basis for the changes that CVPS advocates and, given their weakness, the CVPS arguments based upon them are simply unpersuasive.

Second, CVPS did not provide sufficient evidence to demonstrate that the long-term societal benefits it claims from deferring cost-effective measures will actually occur with its Amended case. The avoided costs used in exhibit CVPS-BWB-R-1 to demonstrate the benefits that CVPS claims will come from deferral are not the same avoided costs that CVPS used in its Amended case. Tr. 8/29/94 at 145.

Third, CVPS claims that approximately 94 percent of its planned transmission and distribution costs of $10 million (over the next five-six years) are not related to load growth.[84] Tr. 8/29/94 at 171-172. Yet, even the estimated cost for a single transformer

---

84. This issue is significant because load-related expenditures are included among the potential costs that could be avoided by proposed efficiency measures. Underestimating load-related costs has the

upgrade above CVPS's Southern Loop is $370,000. That upgrade is needed due to recent growth in loads on the Southern Loop.[85] In the face of data such as this, CVPS's claim that transmission and distribution costs are unrelated to load is simply not credible. CVPS asserts in this docket that total, system wide, load-related T&D expenses for the next five to six years are only $600,000 (6 percent of $10 million). Taking CVPS's own numbers at this face value, the $370,000 cost of the single Southern Loop transformer would leave only $230,000 for all load-related T&D expenditures company-wide over the next five to six years. Over-stated claims of this nature are simply unpersuasive, and reinforce our general concern about the Company's fundamental credibility on issues of this kind. Thus, we are not persuaded that CVPS has allocated appropriate T&D benefits in the DSM program cost-effectiveness screening used for its deferral analysis.

Fourth, the DPS has demonstrated: (1) that when CVPS avoided costs (corrected for undisputed errors) are used, that the DSM deferral proposal creates a loss of net benefits ($0.4 million); that using CVPS filed avoided costs with externality and risk adjustments creates a loss of net benefits ($0.6 million under the DSM deferral proposal); and, that using DPS avoided costs (developed by its consultant) creates a loss of net benefits ($7.5 million) under CVPS's DSM deferral proposal. Exhs. JJP/PLC-R-2 & 3.

Fifth, the DPS states, and we conclude, that CVPS severely biased its avoided costs downward for the early years of its analyses and that CVPS understates the cost associated with ramping down and then restarting programs. Plunkett/Chernick sur. pf. at 8.

In summary, we are unable to conclude that CVPS has properly implemented its C&LM portfolio so as to maximize total net societal benefits. Some of the specific DPS concerns regarding CVPS's changes are discussed in more detail below, in our review of individual programs.[86]

---

effect of understating the value of efficiency measures and, thus, of committing the company to unnecessary supply costs.

85. See filings and testimony in Docket 5730.

86. This discussion has focused on deficiencies on CVPS's programs during past periods, since they must be reviewed before awarding rates in this proceeding. As to the future, the appropriateness of many of CVPS's proposed changes, the DPS's criticisms of those changes, and a determination of what avoided cost values CVPS should use in its cost-effectiveness screening will have to wait resolution in other

e. C&LM Expenditures and ACE Recovery

Since 1990, we have stated on numerous occasions that approval of C&LM expenditures is an appropriate issue for rate cases.[87] In Docket No. 5270-CV-3, CVPS proposed an annual reconciliation proceeding, which we rejected, in part, because it would constitute selective ratemaking. Docket No. 5270-CV-3, 5/20/91 at 78-79. In Docket No. 5270-CV-1&3, CVPS proposed a "Regulatory Review and Oversight" procedure that, twice each year, would determine C&LM costs eligible for recovery in a rate case. We rejected that proposal, except for special circumstances that have not been met in this instant Docket. Docket No. 5270-CV-1&3, 5/4/93 at 92-94.

In this Docket, CVPS argues that the Board must approve the Company's deferred ACE amounts (and by implication its deferred C&LM expenses) in order to send a message to the Company, other Vermont utilities, and utility investors that these deferred amounts are "real" assets. CVPS Reply Brief at II-12. The fundamental purpose of ACE is to allow a utility to recover the net revenues it loses in the short-run due to measures installed by its customers through the utility's DSM efforts.

We have consistently said that deferred ACE and C&LM expenditures are appropriate for recovery in rates to the extent that the ACE amounts represent actual net lost revenues caused by the Company's own efficiency efforts, and to the extent that program expenditures have been prudently incurred and achieved appropriate results. We have also said that we are willing to grant some latitude to the interpretation of "appropriate results."[88] However, we expressly reject the automatic inclusion of any costs -- whether DSM or other -- for ratemaking purposes.

For ACE, specifically, we have allowed recovery based on stipulations between parties. Docket No. 5270-GMP-3, 9/5/91 at 65-66. We have also indicated a

---

proceedings.

87. See Docket No. 5270, 4/16/90, Vol. III at 161; Docket No. 5270-CV-3, 5/20/91 at 78-79; Docket No. 5270-GMP-3, 9/5/91 at 65; Docket No. 5270-WEC-2, 1/30/92 at 50-51; Docket No. 5270-VGS-2, 10/23/92 at 65; Docket No. 5270-CUC-2, at 75-76; and Docket No. 5270-CV-1&3, 5/4/93 at 94.

88. For example, we have said that if there was a "reasonable expectation" that programs would produce cost-effective savings or lead to the development of cost-effective programs, then the expenditures for those programs can be included in rates. Docket No. 5270, 4/16/90, Vol. IV, Appx. IV-A, Secs. 9 (a) & (b). CVPS quotes this language in its brief. CVPS Brief, Vol. II at 92-93.

willingness to allow ACE adjustments on a prospective basis only, once an agreement has been reached on appropriate initial estimates. Docket No. 5270-CV-1&3, 5/4/93 at 95-98. CVPS's proposed finding #417 ignores this essential requirement of agreement on initial estimates and thereby completely distorts that fundamental policy. Again it represents a type of "over-reaching" advocacy that ignores clear past precedents and does not enhance the Company's overall credibility.[89]

CVPS maintains that because the DPS did not attempt to litigate the thousands of per-measure savings estimates that the Company filed in its reference manuals, the DPS should be barred from raising challenges to those estimates in this Docket. CVPS further states that the DPS's request for an adjustment to ACE amounts is contrary to the Board's policy established in Docket No. 5270-CV-1&3. Gamble reb. pf. at 41.; tr. 9/6/94 at 189-196.

In addition to concern about CVPS's misstatement of unambiguous and relevant legal precedents, we conclude that CVPS's contention is impractical. If we adopted it, we would either have to allow rate recovery for any per-measure savings estimate regardless of its accuracy or probability, or we would have to have a Board investigation every time a savings estimate was proposed or revised.

We reaffirm our conclusion in Docket No. 5270-CV-1&3, Order of 5/4/93, that absent an agreement on initial savings estimates, ACE adjustments at the time of a rate case are necessary to ensure a minimal level of confidence that claimed net lost revenues bear a reasonable relationship to actual net lost revenues. As we have said before, if adverse parties can reach agreement upon initial savings estimates for the purposes of ACE, then we are willing to allow future revisions to be applied on a prospective basis only. The record in this Docket, despite CVPS efforts to argue otherwise, establishes that no agreement, or implied agreement, on ACE estimates was ever achieved with the DPS or other adverse parties. CVPS's per-measure savings estimates, therefore, are subject to review and modification in this Docket.

f. Least-Cost Planning and Rate Impacts

---

89. This does not mean an inability to seek to change past rulings. Instead it means that the company, like any litigant, has an obligation to acknowledge relevant precedents and candidly seek to change them, rather than asking a tribunal for rulings that contradict precedents that it has not ignored.

In its reply brief, CVPS lists four criteria that should be used to evaluate its commitment to integrated resource planning:

> (1) the formulation of screening tools to determine the societal cost-effectiveness of the Company's program designs and field testing of efficiency measures; (2) the establishment of a program tracking system and other essential tools for the oversight and management of program activities; (3) the institutionalization of management systems and corporate structures which have been designed to ensure that supply and demand-side options are integrated on an equal footing; and (4) the creation of a program monitoring and evaluation capability so that management can be kept abreast of program performance and be assured of a reliable flow of information which is necessary to enable it to prudently review and improve program designs and implementation strategies.

CVPS Reply Brief at II-62.

We find that CVPS's efforts, judged by its own four standards, have been deficient in several respects. First, the record in this and other incorporated Dockets has established that CVPS has used questionable screening practices, some of which have required specific Board corrections. Second, CVPS's tracking system has some deficiencies, as established by the DPS's evidence, although they do not appear to be major flaws. Third, CVPS has not persuaded us in this Docket, or in other proceedings, that "management systems and corporate structures" have been developed to ensure comparable evaluation of demand and supply-side options. See p. 144, below. Fourth, CVPS has been sanctioned for not conducting an essential evaluation related to a fuel-switching stipulation approved by this Board. Furthermore, the DPS has identified numerous concerns with CVPS's monitoring and evaluation efforts and the Company's interpretation of those evaluations. Therefore, we expressly reject CVPS's claim that its decisions have been fully consistent with the goal of minimizing the long-run costs of providing adequate and reliable energy services to customers. Id. at II-62.

g. Targets and DSM Decisions

251. CVPS alleges that it developed its Amended case, and the deferrals of DSM programs, based on a bottom-up analysis and without specific reduction goals or targets from CVPS management. Tr. 7/18/94 at 122, at 166. The record reviewed below shows that this testimony is not credible.

252. At a later hearing, in response to a similar question on CVPS's cost-reduction efforts, a member of CVPS's senior management team stated:

> I would observe that what we really did was provide guidance to staff as to what we thought the targets should be, and then we did what I would call a top down and bottom up approach where the staff then went back and examined whether those savings that we had set out as targets could

> be achieved. Certainly if those targets were not achievable, they would have been modified.

Tr. 8/19/94, Vol. II at 163-164 [emphasis added].

253. In October, 1993, CVPS issued a press release stating that it had set a target of reducing operations, maintenance, and DSM costs by $5 million. When questioned about this press release, CVPS's witness stated that the $5 million dollar figure was a target. Id. at 165-168.

h. Rate Impacts and DSM Decisions

We begin by observing that rate impacts and overall costs are both extremely significant, but that they are not equivalent. We have addressed this issue at length in prior cases and, here, repeat only the basic arithmetic fact that a substantial increase in energy efficiency can lead to lower energy costs, even if per-unit prices rise somewhat. Utility management should be concerned about the per-unit rates charged to customers. We share that concern, and recognize that it may become increasingly important if competitive pressures increase. That concern, however, cannot become a single-test that drives all decisions and leads to outcomes that actually increase total costs for captive customers. Thus, it must be balanced with the long-term benefits of improved customer energy efficiency, which include the avoidance of future power purchases that are likely to raise CVPS's costs and, ultimately, its customers' rates.[90]

CVPS disputes the DPS's contention that the Company has improperly based decisions on rate impact tests. CVPS Reply Brief at II-45, 49. The essence of CVPS's defense is that the DPS has not provided specific examples of an actual CVPS software

---

90. We note, for example, that CVPS recently spent approximately $50,000 per "down-sized" employee to reduce its workforce with the intention of reducing long-term costs. We support such efforts and have included a reflection of the costs and savings in rates. However, CVPS has not offered any convincing arguments as to why spending money to save money is wise in this instance (down-sizing), yet unwise in obtaining energy efficiency resources. Similarly, we are troubled by an apparent inconsistency between the Company's explicit recognition that non-price factors such as reliability and diversity are a valid reason to increase the rate impacts of supply choices, and its apparent belief that efficiency measures with similar benefits must be avoided because of similar rate effects.

program for cost-effectiveness screening that is driven by the rate impact measure (RIM) test. However, the evidence cited in the following findings demonstrates that, on a management level, rate impacts, not net societal benefits, are the driving force behind CVPS's decisions on DSM expenditures.[91]

254. In June of 1993, CVPS testified that it was "very concerned about rates and what that does to our customers." Docket No. 5270-CV-1&3, tr. 6/17/93 at 176. In a press release that same month, CVPS stated:

> In its efforts to control rates, Central Vermont Public Service has proposed consideration of a "cap" for the future rate increase impact of energy efficiency programs and "fuel-switching" actions taken with individual customers.

Exh. DPS-SHP-2 at 6.

255. In a discussion with employees on 9/9/93, CVPS President Tom Webb stated that due to the economic downturn, the Company will need to cut back on the number of people working on DSM:

> We will propose gearing down our DSM due to [the] current economic situation, excess generating capacity and the impact on rates.

Id. at 18. No mention is made of whether "gearing down" is related to avoided costs, societal cost-effectiveness testing, or total net benefits.

256. In a similar discussion in October, 1994, CVPS President Webb stated that the Company is going to take some risks, that the DPS may disagree with CVPS's changes to its programs and may ask CVPS to prove that the cost-effectiveness formula has changed. CVPS's President added that CVPS may face financial penalties, but "we think it is worth taking the chance". Id. at 19.

---

91. In its reply brief, CVPS argues that the DPS's criticisms of management's policies demonstrate only that:

> . . . Company managers are concerned about the level of CVPS's rates and have taken decisive action to control them.

CVPS Reply Brief at II-49. The record does not persuade us that CVPS has succeeded in reducing costs through comparable "decisive actions" to control the far greater costs that it is incurring for supply-side expenses.

4. Program Issues

a. Residential High Use

i. Implementation of cost-effective recommendations

257. CVPS has consistently overstated the achievements of its Residential High Use Programs. Parlin pf. at 22.

258. CVPS's December 1993 Implementation Analysis asserts customer acceptance rates for fuel-switching of 23 percent and 16 percent for space and water heating, respectively. Parlin pf. at 24.

259. CVPS's 1993 DSM Annual Report indicates that customer acceptance rates for fuel switching are 20 percent for space heating and 19 percent for water heating (after adjusting for customers who install competing conservation measures). CVPS 1993 DSM Annual Report at 16-17.

260. The customer acceptance rate is an appropriate standard for comparison with other utilities because it minimizes the effect of utility-specific factors. Parlin pf. at 25.

261. After correcting for these overstatements and despite inadequacies in program design and implementation, CVPS's program expenditures for the Residential High-Use program have achieved sufficient cost-effective savings to justify the recovery of CVPS's expenditures for this program. This demonstrates that the expended costs benefitted ratepayers and should be recognized. However, even after giving due consideration to the testimony of the Company, we can only conclude that CVPS has not aggressively pursued all the efficiency savings that could have been cost-effectively acquired. Gamble reb. pf. at 28; findings above.

Discussion

CVPS's implementation analysis asserts that among customers for whom cost-effective fuel-switches were recommended, 23 percent implemented space heat fuel-switches and 16 percent implemented water heat fuel-switches. CVPS's 1993 DSM Annual Report indicates (after excluding customers who implemented competing conservation recommendations[92]) that during 1993, 20 percent of customers with space

---

92. As discussed below, the DPS has presented strong evidence that CVPS overestimated savings from conservation measures and, therefore, may have biased customers towards conservation installations rather than fuel-switch installations. For the limited purposes of this discussion, we have assumed that CVPS did not bias any customer towards conservation measures.

heat recommendations and 19 percent of customers with water heat recommendations implemented those measures. Exh. DPS-JFG-2; CVPS 1993 DSM Annual Report at 16-17. GMP, which also operates a program without customer financial incentives, has achieved an implementation rate of almost 20 percent for single family space heat fuel-switching. Docket No. 5270-CV-1&3, Parlin pf. at 5.

WEC and BED both operate fuel-switching programs that incorporate shared-savings mechanisms. They have both achieved significantly higher implementation rates. For WEC, customers with cost-effective fuel-switching recommendations have installed alternate systems at a rate of 75 percent for space heating and 58 percent for water heating. For BED, customers with cost-effective fuel-switching recommendations for space heating have installed alternate systems at a rate of 68 percent. Parlin pf. at 24.

We recognize the difficulty in trying to compare customer choices in various service territories. Certainly relative electric rates and alternate fuel costs can have some impact on customer decisions to implement cost-effective recommendations. However, the extreme variance between utilities without customer incentives and those with customer incentives seems to correlate better than high residential rates (which both CVPS and WEC have relative to GMP and BED) or access to natural gas (which BED has in general, CVPS has in the St. Albans area, GMP has for some customers, but WEC does not).

In addition, we have considerable difficulty accepting CVPS's argument that market forces are encouraging significant cost-effective fuel-switching.[93] CVPS states that it is unnecessary and inappropriate for the Company to offer customer incentives in light of a mature market for fuel-switching. Gamble reb. pf. at 29; CVPS Reply Brief at II-39. If the market is mature and there are no barriers, we find it difficult to understand why 75 percent of the participants in CVPS's program are not implementing cost-effective recommendations. WEC, which claims that there are financial barriers to implementing fuel-switching, and offers a customer incentive and on-the bill financing, achieves a 75 percent acceptance rate.

The evidence in this proceeding does not compel a finding that CVPS can only achieve cost-effective fuel-switching by implementing a program similar to WEC or BED; however, we are persuaded that CVPS has not achieved satisfactory levels of cost-

---

93. CVPS also claims that some market driven fuel-switching is non-societally cost-effective. If such examples exist, we share CVPS's concern. Our discussion here, however, refers only to cost-effective switches.

effective fuel-switching with its own current program designs. If CVPS continues to offer fuel-switching measures to its customers, some form of a program with better financing or incentives may be appropriate. The resolution of this issue, as well as other issues related to fuel-switching program designs, will be deferred until the completion of current proceedings in Docket No. 5270-CV-1&3.[94]

Despite our numerous concerns regarding this program as designed and implemented by CVPS, we conclude that CVPS should recover the costs of this program in rates since there were customers albeit a limited number, who benefitted and some significant power costs have been avoided.

ii. CVPS's Savings Estimates

262. CVPS's per participant savings estimates for conservation measures were significantly higher than those claimed by other utilities. These savings were adjusted to compare gross kWh savings for all utilities. Parlin pf. at 35; Docket No. 5270-CV-1&3; exh. KEP-4.

263. CVPS claimed savings for unverifiable and undocumented measures. Many of these measures reflected behavioral or life-style changes for customers. Parlin pf. at 35.

264. In CVPS's database, 28 out of 375 installed weatherization measures are claimed to have annual savings of 3,000 kWh or more at a cost of $600 or less. The WEC collaborative estimated average savings from insulation measures to be 1,000 kWh for $1,200 of investment. The gap in the savings-to-cost relationship between CVPS's estimates and the planning assumptions of the WEC collaborative is too large to be explained by utility-specific factors. Parlin sur. pf. at 13; tr. 9/1/94 at 125-126.

265. An overstatement of savings has several implications for program performance: it encourages the installation of sub-optimal conservation measures; it understates the value of other potential efficiency measures, it falsely increases program savings and misstates program performance; it results in a bias against the measure; and

---

94. We are mindful that some of the recent intervenors in Docket No. 5270-CV-1&3 have indicated their opposition to CVPS offering any fuel-switching services due to concerns over rate impacts, alternate fuel-cost risks, air quality impacts, and other issues. Our findings and conclusions in this Docket relate to CVPS's current programs, only. Final determinations regarding CVPS's future program designs will be made in subsequent proceedings.

it may influence the customer's choice in favor of alternate conservation measures with fewer societal benefits. Parlin pf. at 22, 33-36.

266. CVPS's per participant ACE savings for some standard DSM measures were inflated. Id. at 51.

267. Fifty of the 71 measures identified for ACE recovery were not documented in CVPS's Reference Manual. CVPS included entire categories of end uses, such as clothes dryers and refrigeration, in the installed measure list despite the fact that they did not have any mention in the Reference Manual. These measures account for 20 percent of the total program savings. Parlin sur. pf. at 16-17.

268. The Department reduced CVPS's claimed per participant savings for five measures with highly excessive savings. The reductions were conservative and allowed for variations due to site specific situations. Id. at 13-14.

269. CVPS has claimed fuel switching savings for each and every participant who had switched fuels following the audit and informed CVPS of this fact, regardless of whether the customer received any additional services from CVPS or even whether analysis showed that the installation was cost effective. Tr. 9/6/94 at 112.

270. Only 25 percent of the participants who were claimed as fuel switches in the Residential High Use Program received a post installation inspection. Tr. 9/1/94 at 162.

271. CVPS's ACE savings for this program should be reduced by 56 percent. This results in a reduction of 1,802,454 kWh in ACE savings for the Residential High Use program. DPS br. at 157; exhs. KEP-9 & 10.

Discussion

The DPS asserts, and has persuasively demonstrated, that CVPS has systematically exaggerated the savings that can be achieved through the conservation measures CVPS offers for electrically heated homes, has exaggerated per-participant savings estimates, and has claimed savings for undocumented and unverifiable measures, such as customer life-style changes. Parlin pf. at 35-36; exh. KEP-9. In comparison to other Vermont utilities, CVPS estimates of per-participant kWh savings for lighting and water heating conservation measures are twice that of the next closest utility and three to four times higher than most of the other utilities. Docket 5270-CV-1&3, exh. KEP-4.

CVPS responds to the DPS concerns by stating that it agrees with some of the DPS's claims, but that the Board should make adjustments on a prospective basis only, due to the DPS's failure to raise its concerns earlier. Gamble reb. at 33-36. As we have stated, above, page 141, we have consistently and repeatedly rejected this general approach absent a specific agreement that establishes baseline assumptions.

We find it is appropriate to include as program savings those measures that have documented energy savings such as energy efficient lightbulbs, weatherstripping, and low-flow showerheads. We are not persuaded by CVPS claims that program savings and ACE should be based simply on customer declarations that they will wash their clothes in cold water, reduce their hot water usage, or manually turn back their thermostats without some documentation that those statements are reliable indicators of actual savings.

We further find that comparisons to other utilities' savings estimates are one appropriate method for gauging the reliability of a particular utility's claims. In this case, the magnitude of the difference between CVPS's savings estimates and those of other Vermont utilities persuades us that the DPS's recommendations are far more consistent with the record evidence. Docket No. 5270-CV-1&3, exh. KEP-4.

Finally, we conclude that the DPS has presented persuasive expert testimony challenging CVPS's claim that conservation measures for electrically heated homes, which are generally better insulated than average Vermont homes, can achieve 30 percent reductions in annual heatload requirements. While there may be special circumstances where this level of reduction can be achieved, we feel the burden is on CVPS to document those situations. Parlin pf.at 35-36

Therefore, we conclude that the DPS recommendation to reduce CVPS's ACE amounts for the Residential High Use program by
56 percent, as documented in exhibit KEP-9, is appropriate.

iii. CVPS's Failure to Conduct Evaluation

272. In approving CVPS's 1991 stipulation for the provision of fuel-switching services, the Board required CVPS to monitor the fuel-switching component of its programs closely to determine whether incentives should be restructured and/or strengthened and to submit an assessment of program performance prior to the 1992-1993 heating season. Docket No. 5270-CV-1&3, Order of 7/12/91.

273. When CVPS failed to conduct an appropriate analysis of customer incentives for fuel-switching, the Board found that failure to be the result of conscious managerial inaction and imposed sanctions upon CVPS with a fine of $5,000.00. Docket No. 5270-CV-1&3, Order of 3/25/94.

274. During the hearings on proposed sanctions, CVPS stated that it had misunderstood the Board's Order of 7/12/91, that it was willing to conduct an analysis of whether higher customer incentives would effect the implementation of measures, and that such an analysis was more appropriate for a focus group evaluation. Tr. 6/17/93 at 60, 256-258.

275. During hearings in this Docket, CVPS stated that it did not ask direct questions regarding higher customer incentive levels for fuel-switching as part of a fall, 1993 focus group evaluation on fuel-switching. CVPS asserted that such direct questions are inappropriate for focus group evaluations because they could bias the responses. Tr. 7/18/94 at 173-175; Gamble reb. pf. at 32.

Discussion

We note that CVPS has only recently completed a limited evaluation of the issue of whether higher customer incentives for fuel-switching measures would be appropriate. That evaluation was done as part of a survey in June/July 1994. Tr. 7/18/94 at 173-174. At the show cause hearing in June, 1993, CVPS stated that it intended to incorporate questions on the issue of higher customer incentives as part of a focus group evaluation. Tr. 6/17/93 at 256-258. Yet, despite CVPS' hearing room commitment on this point, when CVPS conducted focus group evaluations in the fall of 1993, that issue was not discussed. In this Docket, CVPS now disavows its former commitment and testifies that asking such questions is inappropriate for a focus group evaluation. Gamble reb. pf. at 32.

We are disturbed that CVPS appears to be unable to perform essential evaluation studies in a timely and effective manner. We were told, based on CVPS's testimony in June, 1993, that the Company's failure to conduct the analysis required by our Order of 7/12/91 in Docket No. 5270-CV-1&3 was the result of a misunderstanding, not an attempt to evade the requirements of a Board Order. CVPS's conduct since then, and its testimony in this Docket, leads us to conclude that CVPS has consciously failed to meet its responsibilities to conduct the evaluations necessary to make appropriate and timely adjustments to its DSM programs.

b. Residential Direct Install

276. Of the 6,994 participants in CVPS's Residential Direct Install program in 1993, 4,043 were electric water heating customers. Among those 4,043 customers, CVPS identified 214 customers who were either dissatisfied with their electric water heaters or wanted information about water heating options. CVPS contacted 141 of those customers, of which 96 requested site visits. In 1993, CVPS completed 96 site visits, which resulted in 29 recommendations for cost-effective fuel conversions. Of all these customers, CVPS is unaware of any customers who have actually implemented fuel conversions as a result of this program. 1993 CVPS DSM Annual Report at 21, 24.

277. Since the inception of this program, CVPS has not reported a single cost-effective fuel conversion as a result of its efforts. Id. at 21; 1992 CVPS DSM Annual Report at 20.

278. CVPS's per participant savings for DHW conservation measures are assigned on a prescriptive (i.e., average or non-site-specific) basis. CV's prescriptive savings for these measures in this program are much higher than those estimated in CVPS's Residential High Use Program and much higher than those used by other utilities. Parlin 5/27/94 pf. at 54.

279. CVPS's water heater conservation measure savings estimates should be reduced by 30 percent to reflect CVPS's own discrepant estimates. This will result in an overall reduction of ACE amounts in the Direct Install program of 25 percent, or 318,522 kWh. Id. at 54-55; DPS br. at 160.

280. Despite the specific shortcomings outlined above, CVPS's program expenditures for the Residential Direct Install program have achieved sufficient cost-effective savings from non-fuel-switching measures to justify the recovery of CVPS's expenditures for this program. Gamble pf. at 35; 1993 CVPS DSM Annual Report at 21.

Discussion

CVPS's Residential Direct Install program raises two major concerns.

First, CVPS maintains that its program provides fuel-switching analyses and services for customers and that the process is simple and straightforward. Gamble pf. at 35; Gamble reb. at 37-38. In response to DPS criticisms that the program is so burdensome that customers are discouraged from pursuing fuel-switching options, CVPS reiterates its claims that the program is well run and cost-effective through proposed findings 114-122 in its brief. CVPS br. at 35-37.

When we review CVPS's DSM Annual Reports for 1992 and 1993, we discover that not a single customer has implemented a recommendation for cost-effective fuel-switching. We will concede that CVPS may be technically correct when it states that it "offers" fuel-switching analyses and services to its customers through this program; the real question, however, is not what the Company *offers*, but what power costs it could avoid by *acquiring* cost-effective energy savings. In the face of data showing no participants, we simply cannot credit CVPS's claim that it does not believe that the services it is offering are ineffectual and does not acknowledge that changes should have been made to this program. Appropriate changes would enable the Company to acquire even more cost-effective customer resources than it is currently achieving through other elements of this program.

We do conclude that the non-fuel-switching savings CVPS did achieve through the Residential Direct Install program are sufficient to support recovery of the Company's program expenses. However, this is merely a conclusion that what the Company did was useful; it does not address the inefficiencies that lie in what the Company did not do. Those concerns are part of our overall evaluation of management effectiveness addressed in Section VII.

Our second concern relates to CVPS's savings estimates for water heating measures. CVPS uses a per-participant savings estimate for a water heater tank wrap of 630 kWh per year for this program. For its High-Use program, CVPS uses an estimate of 422 kWh per year for a similar tank wrap. GMP and Citizens, for the same measure, use estimates of 400 kWh per year. BED conducted an impact evaluation that estimated savings to be 100 to 200 kWh per year. Finding 278.

The DPS recommends a reduction of 30 percent to CVPS's estimates for savings from its water heating conservation measures. We conclude that the DPS's recommendation is reasonable for two reasons. First, it conservatively reflects the differences in CVPS's own savings estimates in its two programs for the tank wrap measure.[95] Second, CVPS's overall water heater conservation estimates are significantly higher than those of most other Vermont utilities. See Docket 5270-CV-1&3, exh. KEP-4. CVPS's contention that the High-Use estimates are too low is not contradicted by the weight of the evidence in this Docket. Arithmetically, a 30 percent reduction in those estimates leads to a 25 percent reduction in ACE recovery calculations for this program. Therefore, we conclude that CVPS's ACE amounts for the Residential Direct Install program should be reduced by 25 percent to reflect over-estimates for water heating conservation measure savings.

c. Residential Energy Efficient Products

281. CVPS used the same excessive, prescriptive savings for the Residential Energy Efficient Products program as in the Direct Install program, above. Parlin pf. at 55.

282. CVPS's water heater conservation measure savings estimates should be reduced by 30 percent to reflect the discrepancy between CVPS's own estimates. This

95. 630 kWh - 422 kWh = 208 kWh; divided by 630 = 33 percent. In addition, one would expect the High-Use program participants to have greater savings than those in the Direct Install program.

will result in an overall reduction of ACE amounts in the Energy Efficient Products program of 25 percent, or 616,372 kWh. Id. at 55; DPS br. at 160.

283. CVPS's program expenditures for the Residential Energy Efficient Products program have achieved sufficient cost-effective savings to justify the recovery of CVPS's expenditures for this program. Gamble pf. at 39; 1993 CVPS DSM Annual Report at 33.

Discussion

For the same reasons discussed above, regarding the Residential Direct Install water heating conservation measures, we conclude that CVPS's savings estimates for its Residential Energy Efficient Products program should be reduced by 25 percent. We also find the program expenditures should be allowed.

d. Residential New Construction

i. Program expenditures

284. CVPS's program design for the Residential New Construction programs estimated a maximum penetration rate of 30 percent. Tr. 9/6/94 at 217.

285. During the hearings on CVPS's program designs, the DPS claimed that CVPS's projected penetration rates were low and that the design of CVPS's program made even those low penetration rates unlikely. The Board directed CVPS to immediately seek ways to improve its projected penetration rates. Parlin pf. at 17; Docket No. 5270-CV-1&3, Order of 5/4/93 at 64.

286. CVPS's program resulted in installations in 2.5 percent of the new construction market in 1992 and approximately 13 percent in 1993. CVPS Residential New Construction Implementation Analysis of December 29, 1993; Parlin sur. pf. at 1.

287. In Docket No. 5270-CV-1&3, CVPS was told to investigate the applicability of a hook-up fee for residential new construction and to be prepared to implement such a program. Docket No. 5270-CV-1&3, Order of 5/4/93 at 67, fn 44. CVPS has not produced any results from its investigation to date. Gamble reb. pf. at 21-22.

288. Despite inadequacies in program design and implementation, CVPS's overall program expenditures for the Residential New Construction program have achieved sufficient cost-effective savings to justify the recovery of 100 percent of CVPS's 1991 expenditures and 50 percent of CVPS's 1992 and 1993 expenditures for this program. Parlin pf. at 19-21; 1993 CVPS DSM Annual Report at 33.

Discussion

CVPS's actual achievements in the Residential New Construction program were 2.5 percent of residential new construction in 1992 and 13 percent in 1993. These actual achievements were far below its formal projections for both those years. It was also

below CVPS's self-set overall goal of 30 percent penetration; a goal that had previously been ruled to be inadequate. Finding 286; Docket No. 5270-CV-1&3, Order of 5/4/93 at 64.

CVPS claims that it achieved 40 percent greater participation then projected for 1993. Chamberlain reb. pf. at 14. This claim appears to be based on a mixture of housing rehabilitation ("rehab") data and actual new construction data. While we are not disparaging CVPS's efforts to address the needs of customers undertaking substantial rehab projects, we think it is important for CVPS not to use rehab data to distort its success, or lack of success, in the new construction market. When rehab projects are excluded, CVPS actually achieved installations in 33 percent fewer homes than its own projections for the new construction market. Parlin sur. pf. at 2.

We conclude that a portion of CVPS's program expenditures for 1992 and 1993 should be disallowed due to the Company's lack of achievement in its Residential New Construction program. We reach this conclusion, in part, because the evidence demonstrates that CVPS was on notice by both the DPS and the Board that its 30 percent penetration target was insufficient.[96] Another consideration is that the failure to achieve high penetrations in this program is likely to create significant lost opportunities to ever realize significant portions of the energy efficiency savings potential available. In addition, CVPS was directed to consider a hook-up fee approach in May of 1993 and has

96. CVPS was not lacking in early notice upon this issue. The DPS testified to its concerns during the 1992 hearings in Docket No. 5270-CV-1&3. See Order of 5/4/93 at 63-64. The Hearing Officer stated:

> I am concerned that CVPS, when designing this program, may not have placed sufficient emphasis on the need for high penetration levels. . . . I recommend that the Board require CVPS to closely monitor participation rates in its Residential New Construction program, to immediately seek ways to increase penetration rates, and to be prepared to stand behind its commitment to allocate sufficient resources to avoid the creation of lost opportunities.

Id. at 64.

not filed an evaluation of such an approach to date. It is likely, therefore, that CVPS will continue to operate a sub-optimal program for the months ahead.[97]

We are not establishing a rule that lack of achievement, by itself, will always be an appropriate basis for denial of program expenditures. We want to reassure CVPS and other Vermont utilities that we will allow substantial leeway for programs and experimental approaches that may not achieve all appropriate cost-effective savings or may exceed estimated expenditures. We have granted CVPS exactly this consideration in regard to many of the programs and measures reviewed in this Docket.

Nonetheless, when the evidence demonstrates that a utility has repeatedly been negligent or imprudent regarding its obligation to implement programs to maximize net societal benefits, we must take appropriate action. In this instance we reduce CVPS's 1992 and 1993 program expenditures for its Residential New Construction program by 50 percent, as a reflection of the Company's failure to reach even fifty percent of its initial low target penetration estimates for residential new construction in its service territory, and its failure to undertake the appropriate analyses to improve its poor performance.

ii. Fuel Choice Freeridership

289. CVPS's 1992 Energy Survey indicated that less than 2 percent of the new construction market installed electric space heat and less than 20 percent installed electric water heat. Parlin sur. pf. at 4-5.

Discussion

Until May of 1993, CVPS claimed every new residential unit that did not install electric space or water heat as an installed fuel choice measure participant, regardless of whether CVPS had actually provided fuel choice services to that customer. In other words, CVPS did not distinguish between those customers whose choices were altered by CVPS's actions and those customers whose actions were unaffected by the Company's actions. Members of the latter group are referred to by CVPS as "free riders". CVPS then adjusted this number downward by 95 percent for space heating and 60 percent for water heating, based on a 1990 survey on the saturation of electric devices. Parlin pf. at 4-5; Parlin sur. pf. at 4-5.

After May of 1993, CVPS, for ACE purposes, claimed as participants those customers who were initially uncertain of their fuel choice and did not install electric

---

97. For comparison, WEC has implemented a modified hook-up fee approach Residential New Construction program that targets 100 percent of the new homes in its service territory.

space or water heat as an installed fuel choice measure. CVPS then adjusted this number downward by 90 percent for space heating and by 20 percent for water heating. Id.

CVPS's 1992 Energy Survey determined that 2 percent of new homes were built with electric space heat and that 20 percent of new homes were built with electric water heat. Parlin reb. pf. at 4-5. The Board directed CVPS to prescreen customers for fuel-choice measures, beginning in May, 1993. Docket No. 5270-CV-1&3, Order of 5/4/93 at 25-26.

Based on the evidence available to us in this Docket, we conclude that CVPS must revise its method of calculating freeriders for fuel choice measures. CVPS should only offer fuel-choice measures to pre-screened customers who are considering the installation of electric space or water heat. CVPS must then determine, through monitoring and evaluation, what percentage of those pre-screened customers are likely to install such measures regardless of utility action. The remaining (non-freerider) participants, when compared to CVPS's entire Residential New Construction market, should not exceed 2 percent for space heat and 20 percent for water heat (based on the 1992 Energy Survey). If a new Energy Survey indicates that saturation rates have changed, then comparisons should be made based on the new Survey.

iii. Savings Estimates

290. The per participant fuel choice savings estimates used in CVPS's Annual Report and for ACE calculations were overstated by more than 100 percent as indicated by CVPS's Residential New Construction Implementation Analysis of December 29, 1993. Parlin pf. at 4-8; exh. KEP-3.

291. The per participant fuel choice savings used in CVPS's DSM Annual Report and for ACE calculations were estimated on a prescriptive basis and were at least 100 percent greater than the average space or water heating usage as determined from CVPS's 1990 FERC form. Parlin pf. at 6 and 7; tr. 7/19/94 at 115.

292. CVPS acknowledges that its fuel choice savings estimates were too high for 1992 and 1993. Gamble reb. pf. at 18; tr. 9/6/94 at 109.

293. CVPS claimed fuel choice savings prior to the completion and occupancy of some buildings. Parlin pf. at 5; tr. (Gamble) 9/6/94, pp. 169-170.

294. CVPS's fuel choice measure savings should be reduced by 100 percent to reflect the serious flaws in CVPS's initial program designs and implementation procedures and for CVPS's failures to take appropriate remedial steps. This will result in an overall reduction of ACE amounts in the New Construction program of 1,158,186 kWh. Welch pf. at 16; DPS br. at 160.

Discussion

In this docket's claims for cost-recoveries from Vermont ratepayers, CVPS has overstated its per-participant savings estimates for fuel-choice measures by more than 100 percent for this program, based on CVPS's own estimates reported to FERC and based on CVPS's Residential New Construction Implementation Analysis. Findings 290 and 291. Savings from fuel-choice measures account for 90 percent of CVPS's 1992 savings for this program and 86 percent of the 1993 savings.[98] Parlin pf. at 8.

CVPS acknowledges that its estimates are too high, but maintains that retroactive adjustments are inappropriate. Gamble reb. pf. at 18. CVPS's Implementation Analysis made a specific observation regarding fuel-choice participants:

> It should be noted that filling out the fuel-choice part of the application for water heating and space heating was considered an installed measure by the Company.

Implementation Analysis for Residential New Construction, December, 1993, at I-7. In addition, CVPS, while disputing the magnitude of the problem, acknowledges that it probably claimed fuel-choice savings prior to the completion and occupancy of some buildings. Finding 293.

We conclude that CVPS's savings estimates for fuel-choice measures are completely unreliable. CVPS has not demonstrated that its free-rider factors are reasonable; CVPS has overstated per-participant savings by 100 percent or more; CVPS has not improperly verified many of its claimed installations; and CVPS has admitted that some of its savings are for buildings that were not completed at the time the savings were claimed. As we have previously stated in this Order, we are not persuaded by CVPS's argument that changes to its savings estimates should only be applied on a prospective basis. The evidence regarding savings estimates for this program is a compelling reason why CVPS's contention is unacceptable.

e. Residential Appliance Recycling

Findings

295. The Company spent $34,663 in 1993 to operate a Residential Appliance Recycling Program, which removes spare, working refrigerators and freezers from the homes of customers who were selected to participate. During 1993, CVPS found only 58 customers who were eligible to participate. Owen pf. at 10, 14.

---

98. Our independent calculation from the 1992 and 1993 DSM Annual Reports indicates that the percentages are 95 percent and 87 percent, respectively.

296. Largely because of CVPS's strikingly low ability to find participants, the Company's Appliance Recycling Program did not avoid cost-effective levels of power costs. CVPS witness Gamble testified that a Company analysis of the program indicated it might fail a cost-effectiveness test even before the service was offered. Gamble pf. rebuttal at 39.

297. Rather than continue with a risky program, the Company should have re-designed it with the intent of improving its cost effectiveness. Owen sur. pf. at 7-8.

298. Three other Vermont utilities have operated appliance recycling programs with reasonably strong participation. Washington Electric Cooperative and Citizens Utilities Company recycled as many appliances as CVPS, even though they have far fewer customers. Moreover, CVPS's cost per recycled unit was three times more expensive than GMP's and seven times more costly than WEC's. Owen pf. at 14, 15.

299. Due to CVPS's mismanagement of the Appliance Turn-In program, CVPS's 1993 program expenditures of $34,633 should not be recovered in rates. Owen pf. at 10.

Discussion

CVPS initially offered its Appliance Turn-In program to 5 percent of its customers, selected through a bill insert survey. CVPS restricted eligibility by eliminating certain refrigerator and freezer models regardless of their consumption characteristics. As a result, many customers who sought to participate in the program were turned away. In fact, 70 percent of the customers denied participation in the program were turned away because their models were excluded. Some of those models would probably have met CVPS's stated eligibility criteria of 1,200 kWh of annual consumption. Owen pf. at 11-13.

CVPS was aware, before the program was implemented, that it might fail a cost-effectiveness test. Gamble reb. pf. at 39. CVPS did not take steps to redesign the program to improve its cost-effectiveness. Owen sur. pf. at 7-8.

CVPS solicited 5,500 customers as a result of its bill attachment survey. 150 requested services and only 58 were allowed to participate. Largely because of low-participation rates the program was not cost-effective, so CVPS dropped the program.

The DPS's testimony identified a series of CVPS errors that included postponing the program during the more advantageous summer months, failing to try to increase customer participation, and failing to revise eligibility criteria to avoid cream skimming. Owen pf. at 10. When compared to other utilities' appliance recycling programs, CVPS's program collected fewer appliances at a much higher per-unit cost. WEC acquired 62 appliances at a per-unit cost of $74; GMP acquired 1235 appliances at a per unit cost of $213; CVPS acquired 58 units at a per-unit cost of $597.

We conclude that CVPS seriously mismanaged this program. It was aware of problems with cost-effectiveness and failed to take timely steps to address those problems. The Company could have chosen not to implement the program at all, it could have modified the program through expanding advertising or revising eligibility thresholds. Perhaps most promisingly, CVPS could have originally designed the program with a greater emphasis on achieving savings and a lesser focus on (ultimately self-defeating) efforts to limit "over" participation. Evidence from other utility programs clearly demonstrates that far better results could have been achieved at far less cost. We therefore disallow $34,633; that is, 100 percent of CVPS's cost, to implement the Residential Appliance Turn-In program.

More disturbing than the small amount at stake for this failed program, is its consistency with a general pattern in which CVPS's efficiency measures appear to have been designed and implemented with a self-defeating emphasis on limitations rather than upon achievements.

f. Large C&I retrofit

300. CVPS has not substantiated the economic basis for modifying its approved programs in order to reduce the pace of acquisition of discretionary retrofit resources. The Company has not justified the pacing modifications as being enhancements that improve program cost-effectiveness and increase total net benefits. Lloyd pf. at 13; Plunkett/Chernick sur. pf. at 5-6, 10-12; exhs. JJP/PLC-R-2 and 3.

301. CVPS has not presented defensible documentation and evaluation studies regarding the use of a 20 percent freerider estimate for fuel-switching projects in this program. The evidence supports a default 50 percent freerider factor for fuel-switching projects to account for the different incentives and program services offered for fuel-switching measures. This adjustment reduces ACE by 554,512 kWh. Lloyd pf. at 15-16; Lloyd exh. DPS-REL-2; tr. 8/17/94 at 4.

Discussion

i. Program design issues

CVPS supports increasing its customer incentive buy down from 1.5 years to 2 years by contending that the Company will be able to spend its limited pool of rebate dollars on more cost-effective projects while maintaining high participation rates to avoid creating lost opportunities. Cost-effective retrofit measures not included at this time will be acquired at a later date. Gamble reb. pf. at 53; CVPS reply bf. at II-34.

We conclude that CVPS's proposal, in essence, suggests that a few measures with high benefit-cost ratios are preferable to comprehensive measures that will increase total

net benefits. This approach advocates "cream-skimming", a policy that we have specifically rejected as an appropriate basis for program design. Docket No. 5270, Order of 4/16/90, Vol. III at 46-47. We are uncertain why CVPS is claiming that its pool of rebate dollars is limited; we have consistently held that utilities should allocate sufficient resources to acquire societally cost-effective energy efficiency resources.

It is possible that requiring customers to contribute a larger portion of measure costs is an appropriate program modification. We cannot conclude that CVPS has presented adequate justification, at this time, for modifying its customer incentive in this program. Nonetheless, we conclude that CVPS's program expenditures are eligible for recovery in rates.

ii. Adjustment to ACE Amounts

The DPS maintains that the freeridership adjustment for customers who implement fuel-switching measures should be higher than the 20 percent that CVPS uses for its non-fuel-switching measures. The DPS notes that CVPS provides no incentives for fuel-switching measures, nor has the Company provided any evaluation studies supporting its 20 percent freeridership factor. The DPS supports a 50 percent freeridership factor and adjustments to CVPS ACE amounts based on that percentage.

We conclude that until CVPS can demonstrate how its program efforts are influencing customer choices for fuel-switching measures, 50 percent is an appropriate default estimate. CVPS's extensive arguments regarding the impact of market forces and price signals on customer decisions in the residential class are appropriate to consider for commercial and industrial customers, too. Those market forces, along with the absence of any customer incentives for fuel-switching measures, convince us that 50 percent is a reasonable starting estimate, and may prove to be too low.

Therefore, we conclude that CVPS ACE amounts for its Large C&I Retrofit programs should be modified by 554,512 kWh.

g. Small Commercial Retrofit

302. Under CVPS's Amended Case only 61 customers out of the approximately 8,500 customers identified in the original program design would be eligible for installations each year. The Company has not provided a meaningful analysis of how much discretionary DSM resources should be procured or at what cost. CVPS Petition of 12/14/93; tr. 8/17/94 at 172-173; Gamble reb. pf. at 54; Plunkett/Chernick sur. pf. at 5, 10-12, 29.

303. Comprehensive results have not been achieved. 93 percent of 1993 annualized savings were attributable to lighting measures, despite a number of other possible measures. Gamble exh. JFG 9-11; Lloyd pf. at 16-17.

304. In the absence of impact evaluation findings and a quality control review of both the energy estimating procedures and the use and application of the reference manuals, the DPS supports changing the confidence factor for this program from 1 to .85. Lloyd pf. at 20-21; exh. DPS-REL-3; tr. 8/17/94 at 157-158.

305. Due to the lack of defensible documentation and evaluation studies regarding appropriate freerider estimates for fuel-switching projects, the Department supports a 50 percent freerider factor for fuel-switching projects to account for the different incentives and program services offered for fuel-switching measures. Lloyd pf. at 21; exh. DPS-REL-2.

306. These two adjustments reduce ACE for this category by 296,662 kWh. Tr. 8/17/94 at 7.

Discussion

i. Program design issues

This program has experienced a high non-install rate. Rather than attempting to correct the problem of low installation rates by smaller customers, CVPS finds "no problem" with its performance regarding participation levels for these smaller customers. Lloyd pf. at 17-19; Plunkett pf. at 25; Gamble reb. pf. at 55; Plunkett/Chernick sur. pf. at 19, 23.

We conclude that CVPS should take steps to improve both the participation rate for customers with less than 100 kW of demand and to expand the implementation of measures other than lighting. We further conclude that, while this program has not avoided the maximum cost-effective amount of power costs, it has achieved sufficient savings to justify the recovery of CVPS's costs for the Small Commercial Retrofit program in rates.

ii. Adjustment to ACE Amounts

The DPS maintains that the confidence factor for CVPS energy efficiency savings should be reduced from 1.0 to .85 to reflect inadequate documentation of its engineering estimates, the method used to calculate those estimates, and the absence of any impact evaluations to support those estimates. In addition, the DPS supports increasing CVPS's freerider estimates to 50 percent for fuel-switching measures. Lloyd. pf. at 20-21; tr. 8/17/94 at 157-158.

We accept the DPS recommendation to reduce the confidence factor from 1.0 to .85. Engineering estimates are well documented as being generally exaggerated and in

need of updating through monitoring and evaluation studies. We also accept the DPS's recommendation to increase the freerider estimate to 50 percent for fuel-switching measures. See discussion above, p. 164.

Therefore, the ACE amounts for CVPS's Small Commercial Retrofit program shall be reduced by 296,662 kWh.

h. Commercial Remodelling and Equipment Replacement and Energy Efficient Motors

307. CVPS has not conducted sufficient market research and resource characterization to determine if it is obtaining a reasonable level of lost opportunity resources from the equipment replacement and remodeling markets. CVPS has not completed process or impact evaluations for these programs. Lloyd pf. at 23; Lloyd sur. pf. at 2, 7, 12; exh. DPS-REL-3.

308. The Amended Case does not demonstrate a commitment to meet the Company's stated goal to "aggressively pursue market driven lost opportunity programs." CVPS has introduced substantive reductions in its plans and commitments to acquire cost effective lost-opportunity resources from these programs. Lloyd pf. at 24-26.

309. In the absence of impact evaluation findings, and a comprehensive quality control review of the energy estimating procedures and the use and application of the reference manuals, the DPS supports changing the confidence factor for this program from 1 to .85. This adjustment reduces ACE by 266,925 kWh. Lloyd pf. at 28; exh. DPS-REL-3; tr. 8/17/94 at 7.

Discussion

i. Program design issues

The DPS is concerned that CVPS has not achieved sufficient participation or savings in these two lost opportunity programs. The programs have not reached the target levels established in the collaborative process three years ago. Ninety percent of the savings from the Remodelling program are from lighting measures, a finding that demonstrates the inadequacies of the program as to all other measures. CVPS lacks market data to determine the percentage of opportunities it is acquiring in its Motors program. The DPS states that actual savings have lagged behind projections. CVPS's response has been to continue to lower its savings projections, rather than improving program performance. Lloyd pf. at 22-25.

We conclude that the DPS has identified serious concerns with these two programs. We direct CVPS to work with the DPS and other Vermont utilities to identify ways that its program designs can be improved. Despite CVPS's failure to achieve the installation of comprehensive measures in its Remodelling and Equipment Replacement program and its failure to achieve projected savings amounts in its Energy Efficient Motors program, we conclude that sufficient savings have been achieved to justify the inclusion of CVPS's cost for these two programs in rates. As in other cases, the problem is not what has been accomplished, it is what has not been done.

ii. Adjustment to ACE amounts

The DPS recommends a reduction in the confidence factor for savings estimates from 1.0 to .85, due to CVPS's failure to document or provide a quality control review of its engineering estimates, estimating procedures, and algorithms used to produce the savings estimates for these two programs. Lloyd pf. at 28.

For the reasons stated above, p. 165, we accept the DPS's recommendation and reduce CVPS's ACE amounts for these two programs by 266,925 kWh.

i. C&I New Construction

310. CVPS has not provided adequate documentation which explains the basis and rationale for the material changes and reductions made to these programs in its Amended Case. CVPS Petition of 1/14/93; Lloyd pf. at 29-31.

311. The process evaluation of May 1993 for these programs indicates that significant savings opportunities exist beyond those proposed in the Amended Case. CVPS's Evaluation of the Indirect Participant Savings of February 94 concludes that "improved success could be achieved in ensuring a comprehensive design" and that lighting lost opportunities were common. Additional opportunities for increased efficiencies for other end-uses were found. CVPS 1993 C&LM Annual Report Vol. II; CVPS Petition of 12/14/93; Lloyd pf. at 31.

312. CVPS's program did not participate in Act 250 proceedings in a manner which would satisfy the Board's Order regarding Act 250 and ACE accruals. CVPS's study did not identify any DSM program interaction with these customers or document CVPS's intervention in other proceedings which CVPS claims produced savings for these customers. Consequently, the DPS supports reducing the ACE amounts by 50 percent, or 287,911 kWh. Docket No. 5270-CV-1&3, Order of 5/4/93 at 67-68, 99-101; CVPS 1993 DSM Annual Report Vols. I & II; Lloyd pf. at 32-35; Gamble reb. pf. at 43-44.

Discussion

Based on the DPS's testimony in this Docket and CVPS's evaluation of its C&I New Construction programs, we are concerned that CVPS is not acquiring the maximum amount of cost-effective DSM resources with its current program designs. We are particularly concerned about the lost opportunities that may be created due to the lack of comprehensive programs. We direct CVPS to immediately seek ways to ensure that all appropriate cost-effective measures are included in new buildings. Nonetheless, we conclude that CVPS has achieved sufficient energy efficiency savings to justify the inclusion of its cost for its Commercial and Industrial New Construction programs in rates.

We find the DPS's evidence convincing regarding CVPS's claimed indirect savings for C&I customers who did not participate in CVPS's program. The DPS states that CVPS's failure to conduct a societal analysis of those non-participant's installed measures and its failure to correlate those savings or measures with any of its customers who actually participated in its programs, justifies a 50 percent reduction in ACE amounts claimed for non-participants. Lloyd pf. at 33.

We agree. Although 50 percent is an arbitrary adjustment, it is not a capricious one. CVPS's own failure to provide any documentation on the cost-effectiveness of its claimed savings is what makes a more precise estimate impossible. CVPS's ACE amounts for indirect energy efficiency savings in its C&I New Construction programs are reduced by 50 percent, or 287,911 kWh.

5. Recurring C&LM Expenses

313. CVPS's recurring C&LM expenditures could increase or decrease as a consequence of proceedings in this and other Public Service Board dockets. Welch pf. at 6; Welch sur. pf. at 6.

314. CVPS's requested recurring C&LM costs in this Docket are reasonable given CVPS's expected C&LM costs in this and future years. Gamble reb. pf. at 4, 48; tr. 9/6/94 at 1158-160.

Discussion

CVPS requests that recurring C&LM expenditures, based on its Amended case, be included in rate base. CVPS maintains that these amounts meet the known and measurable standard. If changes are made to CVPS's Amended case, including the elimination of fuel-switching measures, the Company maintains that overall program expenditures will remain about the same. Gamble pf. at 8, 21; Gamble reb. pf. at 48; tr. 9/6/94 at 159-160, 247.

The DPS contends that CVPS has not provided timely and adequate documentation of its recurring expenditures, that many of those expenditures in its Amended case are subject to change by the Company, and that those expenditures may further change based on DPS recommendations in other Dockets. Welch sur. pf. at 5-7.

We conclude that despite the possibility, or even likelihood, that CVPS's C&LM programs will change in this and subsequent years, the amounts requested in the rate year are appropriate for inclusion in rates. However, as we have done in other situations where we wish to ensure that specific allowed expenditures are actually used for specific purposes, we direct CVPS to dedicate all C&LM dollars included in rate base to its C&LM programs. Any amounts not expended in a particular year shall be held for use in subsequent years or for eventual return to ratepayers. See Docket No. 5372, Order of 5/31/90 at 28.

6. Conclusions and Penalty Options

The DPS's expert witnesses have strongly recommended that CVPS be subject to significant disallowances as well as a 25 to 100 basis point reduction in the return on equity because of mismanagement of its energy efficiency programs. Plunkett/Chernick pf. passim. CLF, in addition to endorsing that testimony, also recommends that we find a violation of Condition 8 of the Company's Hydro-Quebec Contract obligations, and we have found that the evidence supports this finding. CLF has stated that a calculation of the penalty for this violation should await a future case; however, we conclude that penalties for past action should (to the extent feasible) be resolved before future rates go into effect.

We have previously stated that utility performance regarding DSM activities is subject to review in rate cases and that poor performance may be penalized. Penalties for poor performance may include one or all of the following:

(1) a disallowance of all or a portion of program expenditures;
(2) a disallowance of purchased power that could have been avoided through non-installed DSM measures; and,
(3) a reduction in authorized return on equity.

Docket No. 5270, Order of 4/16/90; Docket No. 5656, Order of 1/26/94 at 102. Penalties for violation of the Hydro-Quebec Contract provision could include a mandate to resell the purchased power, with any loss attributable to management rather than to ratepayers. See Docket 5330-E, Order of 4/30/91 at 15, fn. 11, and discussion, above.

In this Order, we have disallowed a portion of CVPS's program costs for its Residential New Construction program and all of the program costs for its Residential Appliance Turn-In program. For other DSM programs, we have concluded that the most

significant problems are those of omission rather than of commission and, therefore, we will allow CVPS to recover its direct costs for those programs.

As the record reviewed above demonstrates, serious problems exist as to the design and performance of many of the Company's programs. There is substantial evidence that CVPS has failed to implement its programs in a manner that would maximize net societal benefits, that it failed to make timely adjustments to its programs that would increase net benefits, that it failed to conduct required evaluations in a timely manner, that it deferred program implementation without adequate documentation, and that it acts to modify its programs upon the basis of unilateral changes to least-cost planning principles. The same evidence also demonstrates a failure to comply with Condition 8 of the HQ Contract approval Order.

The record demonstrates that these problems rise above the level of specific minor implementation errors and, instead, indicate a deficiency in senior management's commitment to the acquisition of all cost-effective energy efficiency resources available to the Company. As the Department's testimony notes, these problems both expose the Company to a risk of excessive power costs, and also require the application of a financial penalty directly related to management's responsibility for these matters. The DPS and CLF have recommended a 25 to 100 basis point reduction in CVPS's otherwise allowed return on equity because of these issues. For the reasons outlined above, we find these arguments to be strong and persuasive. However, for the reasons outlined in Section VII.C., we will limit the relevant penalty to 75 basis points, applied concurrently with an equivalent (but independent) penalty for deficiencies related to the management of power costs.

C. Conclusion Re: Resources and Cost Management

The Department has demonstrated that CVPS's power supply costs are untenably high. This issue is far more significant than any of the secondary issues to which the Company devotes greater attention in its briefs, and it needs to be squarely faced for the benefit of both ratepayers *and* stockholders, because it is critical to the long-term financial viability of the Company. The Company's mismanagement of its power supply and energy efficiency programs has imposed substantial excessive costs on its customers. It is our responsibility, as a matter of fairness, to ensure that ratepayers do not solely bear the financial consequences of those improvident management decisions; the Company must bear a substantial share of the consequences of its own actions.

According to Dr. Rosen, CVPS's excessive power supply costs amount to more than $9.0 million annually; CVPS's annual costs for Hydro-Quebec alone may be more

than $3.9 million greater than its market value. In addition, the Department argues, and we find, that customers are paying excessive bills because of the Company's failure to aggressively pursue all cost-effective energy efficiency opportunities as required by Vermont law, and as committed to by the Company as a condition of entering into the Hydro-Quebec Contract. For all of these reasons, the Department recommends a disallowance of $9.6 million dollars due to excessive power costs, and a reduction in return on equity of 25 to 100 basis points. Intervenors recommend an ROE reduction of 100 basis points.

Upon consideration of all of these factors, and the extensive evidence in the record, we conclude that it is just and reasonable to reduce CVPS's allowed return on equity in this docket by 75 basis points (.75 percent). This reduction should remain in place until the Company demonstrates, through tangible results, that it has eliminated the excessive power costs imposed on customers by ineffective and improvident management decisions, or that it is on a reasonable and equitable path towards doing so. As stated at the outset of this Order, the Board is prepared to work with the Company, the Department and other interested parties to chart a clear and positive path out of CVPS's presently untenable situation.

In setting the return on equity in this case, we exercise our obligation to balance a number of factors, including the interests of the Company and its investors and those of its ratepayers -- who, unlike consumers in competitive markets, cannot choose a different supplier. It is appropriate in this setting to distinguish between the fair rate of return that we determine for rate-setting purposes and the cost of capital to the utility. The cost of equity capital is the starting point, but not necessarily the ending point in that analysis.

The United States Supreme Court has observed that public utility commissions must consider the "broad public interests" when establishing allowed rates of return. *Permian Basin Area Rate Case,* 390 U.S. 747, 791 (1968). The general rule in this area has been summarized as follows:

> A firm is entitled to earn a rate of return "adequate, under efficient and economical management, to maintain and support its credit . . .", *Bluefield Water Works & Improvement Co. v. Public Service Commission, supra*. The phrase "under efficient and economical management" is an important qualification. If an agency finds that a firm is not being managed efficiently and economically, it can lower the firm's allowed rate of return below the level otherwise required to meet the comparable risk test. *See Market Street Railway v. Railroad Commission*, 324 U.S. 548 (1945); *D.C. Transit Systems, Inc. v. Washington Metropolitan Area Transit Commission*, 466 F. 2d 394 (D.C. Cir.), cert. denied, 409 U.S. 1086 (1972).

Gellhorn & Pierce, Regulated Industries (2d Ed., 1987) at 141; *see also*, Phillips, The Regulation of Public Utilities (3d Ed., 1993) at 402 and cases cited therein.

Numerous decisions in other states have explicitly adjusted equity returns because of management failures to provide adequate service, to manage power costs, and to secure energy efficiency resources that would lower customers' bills. As the Maine Commission has recently noted:

> the fair rate of return goes beyond the mathematical calculation of costs and considers the qualitative aspects of the utility's operations. Such may include, but may not be limited to, adequacy and reliability, consideration of service, management and operational efficiency, and the interest of ratepayers.

Re Central Maine Power Co., Docket No. 92-345, Slip op. at 18 (Me. P.U.C. Dec. 14, 1993).[99]

Vermont law also makes it clear that adjusting a utility's rate of return is among the tools that regulators may employ in setting just and reasonable rates that will balance the interests of investors and consumers. The leading case is *In Re NET&T*, where the Vermont Supreme Court ruled:

> a fair return to investors is not necessarily fair to consumers. "Regulation does not insure that the business shall produce net revenues". *Fed. Power Com. v. Natural Gas Pipeline Co., supra*. Rates follow service and a poor standard of service may afford a basis for a denial of a request for higher rates. A utility must be efficiently and economically managed and operated as a condition to the exercise of this right to impose rates adequate to cover the full cost of service and thus satisfy the investor requirement. So here, *if it should appear that consumers are not being adequately served because of fault on the part of the company, due to inefficiency or improvidence or other like reasons*, the commission should take such inadequacy, and its extent, into consideration in determining the rates to be fixed to the end that a reasonable return, under the circumstances, will result.

---

99. *See, e.g., Re Central Maine Power Company*, Docket No. 92-102 (Phase II) (Me. P.U.C. October 28, 1993) (50 basis point penalty due to utility's unreasonable failure to control power costs); *Re Bangor Hydro-Electric Company*, Docket No. 86-242, Slip op. at 17-50 (Me. P.U.C. Dec. 22, 1987) (25 basis point reduction because of inefficiency in credit, collection, and energy efficiency services); District of Columbia and Massachusetts cases cited in Plunkett pf.; *Re Virginia Electric*, N.C.U.C., Dkt. No. E-22 (1981) (550 basis point penalty for lack of efficiency); and *In Re Iowa Gas*, 76 PUR 4th, 425 (1986) (100 basis point penalty for inefficiency).

Petition of New England Tel. & Tel. Co., 115 Vt. 494, 513 (1949) (citations omitted, emphasis added); followed, *In Re Arlington Water*, 136 Vt. 495 (1978) and *In Re Young's Community TV*, 141 Vt 57 (1986).

The result we order today is also consistent with prior Board orders with respect to cases of utility mismanagement involving other companies. In 1985, for example, this Board reviewed a rate increase request filed by the Continental Telephone Company. We found that:

> Until the Company's service reaches an acceptable level, it cannot expect to charge its subscribers the same rates that would be permitted if the Company's service were up to par, for that would be to reward the Company for its past neglect and to encourage mismanagement in the future. Therefore, we will reduce the Company's return on equity by 75 basis points.

Docket 4997, Order of 12/9/85 at 10. *See, also*, *In Re NET&T*, above; *In re Young's Community TV Corp.*, 141 Vt. 53, 57 (1986).

In the context of this case, we also note that the Vermont General Assembly has emphasized the importance of least-cost power supply and energy efficiency programs. In addition to the Board's general authority to establish just and reasonable rates, including rates of return, Vermont law explicitly authorizes the Board to establish "*rates of return*, rates, tolls, charges or schedules" to encourage implementation of energy efficiency programs. 30 V.S.A. § 218(a) (emphasis added). The Board relied, in part, on this authority when offering utilities the opportunity to earn *enhanced* returns for superior performance in delivering energy efficiency programs; the converse must also be true.

In the present case, we conclude a reasonable starting point for the cost of equity capital to the utility would be 10.75 percent, but that the fair rate of return for ratemaking purposes is 75 basis points lower, or 10.0 percent. We note that the record contains sufficient evidence to support two different 75-basis point penalties of this nature, each supported by adequate and independent evidence. There are two reasons for this penalty. One is the Company's mismanagement of power supply options; the second is the Company's failed efforts to acquire all cost-effective energy efficiency resources. Our detailed findings on these issues are set out in the preceding sections.

Despite these two independent bases for 75-basis point penalties, we have nevertheless made only one 75-basis point adjustment in this case. We judge that this adjustment adequately reflects our findings and serious concerns regarding the Company's management decisions while avoiding unintended harm to the financial health of the Company by impinging on its ability to raise capital. Our goal is not to impair the financial health of the Company but, rather, to promote improved performance for the

ultimate benefit of ratepayers and the Company itself. We repeat that we stand ready to remove this penalty in future rate proceedings, following a tangible demonstration of the Company's efforts to resolve the problems noted above.

VIII. CONCLUSION

We have considered the evidence and arguments presented by the parties in this case. They have led us to the findings of fact and conclusions of law set out above. Upon those bases, we conclude that just and reasonable rates for Central Vermont Public Service Corporation require an increase in test year revenues of approximately $8,575,000 or 4.27 percent.[100] See Attachment A.

IX. ORDER

IT IS HEREBY ORDERED, ADJUDGED AND DECREED by the Public Service Board of the State of Vermont that:

1. Central Vermont Public Service Corporation is entitled to rates which will produce additional retail revenues in the approximate amount of $8,575,000 or 4.27 percent above existing base rates, on service rendered on or after November 1, 1994.

2. Central Vermont shall, on or before November 9, 1994, make a compliance filing, calculating the precise increase authorized by the decision above, and comparable to the content of Attachment A.

3. Central Vermont shall file tariffs in conformance with the above findings, by November 9, 1994.

3. Copies of the compliance filing shall also be served on the parties to this proceeding.

DATED at Montpelier, Vermont, this 31st day of October, 1994.

s/Richard H. Cowart) PUBLIC SERVICE
s/Suzanne D. Rude) BOARD
s/Leonard U. Wilson) OF VERMONT

100. A precise calculation of this amount should be included in the compliance filing required by the following Order.

OFFICE OF THE CLERK

FILED: October 31, 1994

ATTEST: s/Susan M. Hudson
Clerk of the Board

NOTICE TO READERS: This decision is subject to revision of technical errors. Readers are requested to notify the Clerk of the Board of any technical errors, in order that any necessary corrections may be made.

Appeal of this decision to the Supreme Court of Vermont must be filed with the Clerk of the Board within thirty days. Appeal will not stay the effect of this Order, absent further Order by this Board or appropriate action by the Supreme Court of Vermont. Motions for reconsideration or stay, if any, must be filed with the Clerk of the Board within ten days of the date of this decision and order.