

**BEFORE THE
STATE OF VERMONT
PUBLIC SERVICE BOARD**

Amended Joint Petition of Central Vermont
Public Service Corporation ("CVPS"),
Danaus Vermont Corp., Gaz Métro Limited
Partnership ("Gaz Metro"), Gaz Métro inc.,
Northern New England Energy Corporation
("NNEEC") for itself and as agent for Gaz
Métro's parents, Green Mountain Power
Corporation ("GMP") and Vermont Low
Income Trust for Electricity, Inc. ("VLITE"),
for approval of: (1) the merger of Danaus
into and with CVPS; (2) the acquisition by
NNEEC of the common stock of CVPS;
(3) the amendment to CVPS's Articles of
Association; (4) the merger of CVPS into
and with GMP; and (5) the acquisition by
VLITE of a controlling interest in Vermont
Electric Power Company, Inc.

Docket No. 7770

Direct Testimony and Exhibits of

Michael P. Gorman

On behalf of

International Business Machines Corporation

Summary of Testimony

Mr. Gorman's testimony discusses the Petitioners' proposed savings sharing plan and the potential impact of the proposed merger on regulated utility operations and access to capital. Mr. Gorman's testimony refers to two exhibits – a summary of merger terms and conditions from merger proceedings in other jurisdictions, and Petitioners' response to discovery request Q.IBM:PET.2-3.

January 20, 2012



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Direct Testimony of Michael P. Gorman

1 Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A Michael P. Gorman. My business address is 16690 Swingley Ridge Road, Suite 140,
3 Chesterfield, MO 63017.

4 Q WHAT IS YOUR OCCUPATION?

5 A I am a consultant in the field of public utility regulation and a Managing Principal with
6 Brubaker & Associates, Inc., energy, economic and regulatory consultants.

1 **Q PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.**

2 A This information is included in Appendix A to my testimony.

3 **Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?**

4 A I am appearing on behalf of International Business Machines Corporation (“IBM”). As
5 a business electricity customer, IBM has an interest in ensuring that the proposed
6 transactions do not have an adverse impact on the reliability of its electric service or
7 its rates. Reliable delivery of electricity is critical to IBM’s operations, and electricity
8 costs represent a significant portion of its total operating costs.

9 **Q PLEASE SUMMARIZE YOUR TESTIMONY IN THIS PROCEEDING.**

10 A My testimony focuses on two aspects of the proposed acquisition of Central Vermont
11 Public Service Corporation (“CVPS”) by Northern New England Energy Corporation
12 (“NNEEC”) and the merger of CVPS into and with Green Mountain Power Corporation
13 (“GMP” or “Company”) (GMP and CVPS are referred to collectively as the
14 “Petitioners” or “Companies”):

- 15 1. The Companies’ proposed shared savings plan which includes a proposal
16 to allow for the Petitioners to retain estimated savings created by the
17 merger during the first six years of the merged company.
- 18 2. The potential impact of the proposed merger on regulated utility
19 operations, and access to capital.

20 **Q DOES IBM OPPOSE THE PROPOSED ACQUISITION OF CVPS BY NNEEC AND**
21 **THE MERGER OF CVPS INTO GMP?**

22 A No. Based on the Petitioners’ filing and data responses, the proposed transaction
23 appears to be beneficial to the State of Vermont, customers of GMP and CVPS, and

1 the investors in the two utilities. While IBM does not oppose this acquisition because
2 of mutual benefits to all stakeholders, it does recommend modifications to the
3 Petitioners' proposed regulatory plan, and proposes to continue GMP's current
4 disclosures to the Public Service Board ("Board") concerning cash movements from
5 the utility to its parent company.

6 **Q PLEASE SUMMARIZE YOUR RECOMMENDATIONS AND FINDINGS.**

7 **A** I recommend the following:

- 8 1. The Petitioners' proposed shared savings plan should be rejected.
- 9 • The proposed shared savings plan is designed to simply enhance GMP's
10 profits. Under their proposal, the Petitioners will recover all merger
11 integration and consolidation ("I&C") costs in their actual cost of service
12 before any claimed merger savings are estimated. As such, the
13 Petitioners will not be at risk of recovering their merger I&C costs, and
14 customers' rates will be designed specifically to recover all actual costs.
15 Because customers will pay all merger I&C costs, they are entitled to
16 receive all merger-related savings.
- 17 • The Petitioners' proposed shared savings plan is different than traditional
18 regulatory plans approved in other utility mergers and acquisitions. Many
19 regulatory plans in support of mergers and acquisitions allow utilities an
20 opportunity to use merger savings to recover merger-related costs. Such
21 regulatory plans expose the utilities to the risk of not recovering
22 merger-related costs if merger-related projected savings are not realized.
23 The Petitioners' shared savings plan does not have this risk-return feature.
- 24 • The Petitioners' proposed shared savings methodology is not based on
25 bonafide and verifiable merger savings. Rather, merger savings are
26 based on projections of what operations and maintenance ("O&M")
27 expenses might have been had the merger not occurred, relative to actual
28 O&M expenses incurred after the merger. The Petitioners' profits should
29 not be enhanced by such non-verifiable claims of merger savings.
- 30 • Moreover, the Petitioners' claim that customers will receive at least
31 \$144 million of merger savings over the first 10 years is largely illusory.
32 Most of the savings will not be shared with customers until after the first
33 six years of the merger. Savings projections that far out are even more
34 uncertain and problematic than the shorter-term projections during the first
35 six years. The Petitioners have not provided concrete estimates of

1 savings created by this merger, and possible customer savings are at best
2 highly uncertain.

- 3 • As a result, I recommend that all merger-related savings be passed on to
4 customers concurrently as such savings occur.

- 5 2. In approving GMP's last merger with Gaz Metro, the Board required GMP
6 to make certain disclosures and/or information filings concerning payment
7 of dividends to affiliate companies. Those disclosures and information
8 filings should continue, but the Board should also include a restriction that
9 GMP will not write loans to non-regulated affiliate companies, and GMP's
10 Board and/or NNEEC's Board should contain at least two "independent"
11 Board members, i.e., members that are not also Board members of other
12 affiliates of Gaz Metro.

13 **Shared Savings Plan**

14 **Q PLEASE DESCRIBE THE PETITIONERS' SHARED SAVINGS PLAN AS**
15 **CONTAINED IN THE PETITIONERS' FILINGS.**

16 **A** As described by Petitioners' witness Dawn D. Bugbee, at page 4 of her Direct
17 Testimony, the Petitioners propose to retain a percentage of estimated savings
18 created by the merger for the first six years following the merger implementation. The
19 proposed savings between the Petitioners and customers would be as follows:

- 20 1. For the first two years, 10% of savings flows to customers and 90% is
21 retained by the Petitioners;
- 22 2. In years 3 and 4, 20% of savings flows to customers and 80% is retained
23 by the Petitioners;
- 24 3. And finally, in years 5 and 6, 33% of the savings flows to customers and
25 67% of the savings is retained by the Petitioners.

26 After the seventh year, 100% of the savings would flow through to customers.

27 Savings would be measured by the difference between a projection of the O&M costs
28 that would have been incurred if the merger had not taken place, and the Petitioners'

1 actual O&M costs. Importantly, the Petitioners' actual O&M costs would include costs
2 related to the merger consolidation and integration.

3 **Q WHY DO THE PETITIONERS BELIEVE IT IS APPROPRIATE TO RETAIN A**
4 **PERCENTAGE OF THE ESTIMATED MERGER SAVINGS?**

5 A The Petitioners' witnesses Mary G. Powell and Lawrence J. Reilly, at page 10 of their
6 joint testimony, state that shared savings will produce an appropriate incentive to
7 induce investors to pursue mergers of this magnitude which will produce the savings
8 and other benefits that will eventually accrue to customers. (Powell and Reilly
9 Prefiled Testimony at 10).

10 **Q IS THE PETITIONERS' SHARED SAVINGS PROPOSAL REASONABLE?**

11 A No. The Petitioners' shared savings proposal should be rejected for the following
12 reasons:

- 13 1. The Petitioners did not identify the amount of merger I&C costs, but
14 instead stated that these costs would be included in the Petitioners' actual
15 O&M expense. These merger-related costs will be fully recovered in
16 GMP's annual Alternative Regulation Plan ("ARP") rate change
17 proceedings. (See DPS:PET.1-55). Hence, the Petitioners are not at risk
18 of realizing merger savings in order to recover merger-related costs.
- 19 2. The shared savings plan is designed to share savings differences between
20 projected O&M expenses as though the merger did not occur, relative to
21 actual O&M expenses. As such, savings are only estimates. The savings
22 are not bonafide and verifiable cost reductions produced by the merger.
- 23 3. Under the Petitioners' proposed modified ARP, merger I&C costs will be
24 included in O&M expense and recovered directly from customers before
25 any consideration of merger-related savings is made. As such, customers
26 will fully pay all merger-related costs, and therefore are fully entitled to all
27 merger-related savings. The Petitioners are not at risk of producing
28 merger savings to recover merger I&C costs, and therefore are not entitled
29 to any merger-related savings.

1 4. If the Petitioners are allowed to recover prudent and reasonable merger-
2 related costs, excluding an acquisition premium, in the ARP rate-setting
3 process, they would have economic incentives to pursue cost reduction
4 initiatives including mergers and acquisitions. Further, this proposed
5 merger will produce benefits to both investors and customers beyond the
6 estimated merger-related costs and benefits. Therefore, the shared
7 savings proposal is not needed to encourage the Petitioners to seek cost
8 reduction initiatives including mergers and acquisitions.

9 5. The Petitioners' shared savings plan is different than merger-related plans
10 approved for other utilities. The Petitioners have no risk of producing
11 merger-related savings in order to recover merger-related costs. On the
12 other hand, customers will be required to pay merger-related costs with no
13 guarantee (only a promise) of merger-related savings. The Petitioners'
14 proposed shared savings plan does not balance customers' and investors'
15 interests and should be rejected.

16 **Q PLEASE RESPOND TO THE PETITIONERS' CLAIM THAT A SHARED SAVINGS**
17 **PLAN IS NECESSARY TO INCENT COMPANIES TO PURSUE OPPORTUNITIES**
18 **THAT WILL LOWER COST OF SERVICE?**

19 **A**The Companies will incur costs to produce these cost savings, and I believe it would
20 be appropriate to allow them to recover those costs to the extent they are reasonable
21 and producing verifiable savings. Allowing for recovery of reasonable costs incurred
22 to produce more efficient and lower-cost operations would be consistent with cost-
23 based ratemaking, and will give utilities an economic incentive to pursue savings
24 opportunities. Further, reducing a utility's cost of service will create mutual investor
25 and customer benefits by making the utility a more efficient and competitive market
26 participant.

27 A lower cost, more competitive utility will benefit investors because it will help
28 to retain and attract new customers to its service territory, which strengthens and
29 stabilizes cash flow generation, and supports a strong credit rating and access to

1 capital. Customers benefit because they receive more competitive prices for high
2 quality utility service.

3 Designing regulatory plans that allow for full cost recovery of initiatives to
4 reduce costs benefits both investors and ratepayers.

5 **Q CAN YOU DESCRIBE SOME OF THE BENEFITS TO THE PETITIONERS AND**
6 **THEIR SHAREHOLDERS CREATED BY THIS MERGER?**

7 A Yes. Following are some comments made by some credit rating analysts concerning
8 the prospects of a merger between GMP and CVPS:

9 DBRS views the addition of CV and merger with GMP as potentially
10 positive in a number of areas, including the following: (1) increased
11 geographic, regulatory and energy (electric versus gas) diversification
12 (DBRS estimates that on a simple pro forma basis, the combined CV-
13 GMP would comprise approximately one-third of GMLP's consolidated
14 cash flow); (2) CV is a rate-regulated utility with a reasonable allowed
15 return on equity and capital structure, which should provide stable
16 business and financial risk profiles; (3) GMLP, through GMP as well as
17 GMLP's ownership of Vermont Gas Systems (a small Vermont-based
18 natural gas utility), has significant experience operating in the Vermont
19 regulatory environment; (4) potential for synergies flowing from a
20 combination of GMP and CV; (5) a potential source of regulated
21 growth, largely through what would become CV-GMP's majority
22 ownership position in Transco.¹

23 Also in Confidential Attachment A, provided in response to
24 IBM:PET.GMP.1-27.6, at page 12 of a presentation to rating agencies, the Petitioners
25 outlined many benefits created by the merger. The Petitioners have outlined all the
26 benefits created by the acquisitions. These benefits will inure to customers, investors
27 and the service area economies served by GMP and CVPS. Hence, the proposed
28 transaction has benefits to all stakeholders – not simply customers.

¹Attachment A.IBM:PET.GMP.1-27.1, DBRS Press Release, "DBRS Places Gaz Metro inc. [sic] FMB Rating Under Review with Developing Implications, Confirms CP Rating," June 23, 2011.

1 **Q IN PREVIOUS RATE FILINGS, DID GMP AGREE THAT ACQUISITION-RELATED**
2 **COSTS SHOULD ONLY BE RECOVERED THROUGH ACQUISITION-RELATED**
3 **SAVINGS?**

4 A Yes. When Gaz Metro acquired GMP, then President and Chief Executive Officer for
5 GMP Christopher Dutton, agreed that acquisition-related savings would only be
6 retained to the extent they were needed to recover acquisition-related costs. (See
7 Docket 7213, Prefiled Testimony of Christopher L. Dutton at 12).

8 **Q IS GMP'S POSITION ON ACQUISITION COST RECOVERY DIFFERENT IN THIS**
9 **CASE THAN IT WAS IN THE LAST MERGER CASE?**

10 A Yes. GMP's position in this case is very different than it was in the last case. In this
11 case, the Petitioners propose to recover all merger-related costs (consolidation and
12 integration costs) in its actual O&M expense in ARP proceedings without regard to
13 actually producing claimed merger savings. Further, its proposal for shared savings
14 is designed to enhance GMP's post-merger earnings rather than provide it a
15 mechanism to recover merger-related costs. (DPS:PET.1-59)

16 Again, the Petitioners' proposed shared savings plan is not balanced and
17 should be rejected.

18 **Q PLEASE RESPOND TO THE PETITIONERS' ASSERTION THAT THEIR SHARED**
19 **SAVINGS PLAN IS SIMILAR TO OTHER REGULATORY PLANS IMPLEMENTED**
20 **WITH MERGERS IN OTHER JURISDICTIONS.**

21 A I disagree. In many other regulatory merger plans, utilities are given an opportunity to
22 retain merger savings to recover merger costs. However, those plans typically

1 expose the utilities to some risk of recovering their merger costs if estimated merger
2 savings are not realized.

3 For example, I have outlined some of the merger terms and conditions of
4 several merger proceedings noted by the Petitioners in support of their shared
5 savings plan, as well as a few other merger proceedings currently under regulatory
6 review. A summary of the regulatory plans approved, or proposed, is included in my
7 Exhibit MPG-1.

8 As shown on that exhibit, the regulators approved merger provisions that
9 created risk to the utility of fully recovering its merger-related costs, tied largely to its
10 ability to realize expected merger-related savings. In these instances, utilities were
11 not given full merger cost recovery assurance without a demonstration of actual
12 merger-related savings.

13 For example, several acquisitions were approved with rate reductions, rate
14 caps, and/or rate freezes. Merger-related savings created during the rate freeze
15 were fully retained by the shareholders. Hence, companies are given an opportunity
16 to retain savings if they could be realized during the rate freeze period. In this way,
17 customers benefit from the proposed merger by rate reductions and/or rate freezes,
18 and utilities benefit if they can actually produce savings. In fact, rate reductions,
19 caps, or freezes were integral parts of several of the regulatory rulings cited by the
20 Petitioners in response to DPS:PET.1-80, including *Re Narragansett Elec, etc*,
21 Docket No. 2930 (RI PUC March 14, 2000); *Re Nat. Grid*, Docket No. DG 06-107 (NH
22 PUC July 12, 2007); *Re Entergy Corp.*, Docket No. U-19904 (LA PSC May 3, 1993);
23 and *Re New England Gas Co.*, Docket No. 3401, Order No. 17381 (RI PUC Feb. 28,
24 2003).

1 **Q WHY IS THE PETITIONERS' SHARED SAVINGS PLAN DIFFERENT THAN THESE**
2 **OTHER MERGER CASES?**

3 A The Petitioners' proposed shared savings plan is not designed to provide the
4 Petitioners an opportunity to recover merger costs only if they can actually achieve
5 merger savings. The Petitioners have little to no risk of recovering their actual cost of
6 service including their merger I&C costs during the shared savings period. Under the
7 shared savings plan, the Petitioners will continue to implement annual rate changes
8 under its ARP. The Petitioners' cost of service components of the ARP will include
9 full recovery of its actual O&M including merger I&C costs.

10 The proposed shared savings plan is designed to enhance the Petitioners'
11 profit, not to provide it a means of recovering merger costs.

12 **Q ARE THE PETITIONERS GUARANTEEING CUSTOMERS SAVINGS UNDER**
13 **THEIR SHARED SAVINGS PLAN?**

14 A No. There are no guaranteed benefits to customers as part of the shared savings
15 plan. Rather, customers assume all the risk that actual O&M expenses will be lower
16 than estimated O&M expenses absent the merger. Thus, it is possible that customers
17 will pay the Petitioners' actual cost of service during the six-year shared savings
18 period without any verifiable savings or benefits. Alternatively, customers could pay
19 rates above the Petitioners' actual cost of service if savings are estimated but are not
20 realized.

1 **Q DIDN'T MR. GRIFFIN ASSERT THAT PETITIONERS ARE COMMITTED TO**
2 **PROVIDING CUSTOMERS WITH \$144 MILLION IN SAVINGS OVER THE FIRST**
3 **10 YEARS OF THE MERGER?**

4 A Yes, but this commitment is far short of a guarantee that customers will benefit. As
5 described at pages 4 and 5 of Mr. Griffin's testimony, the Companies expect that
6 merger savings for customers will be at least \$144 million over ten years. However, if
7 savings estimates fall short of that amount, Mr. Griffin states that the Petitioners will
8 propose for review and approval a plan for returning the necessary value to
9 customers. Hence, the Companies' proposal represents a best effort promise rather
10 than a guaranteed level of savings to be credited to customers.

11 **Q IS THE PETITIONERS' PROPOSED SHARED SAVINGS PLAN BASED ON**
12 **VERIFIABLE SAVINGS?**

13 A No. The Companies' estimated merger savings are very loose estimates and may
14 not materialize. The claimed merger savings will be based on the difference between
15 actual O&M expenses, and projected O&M expenses assuming the merger did not
16 happen. The Petitioners proposed to estimate O&M costs absent the merger by
17 simply trending current O&M costs forward over the 10-year period where merger
18 savings will be estimated.

19 This proposed savings measurement methodology is not adequate to identify
20 verifiable or bonafide merger savings. For example, if the merger did not take place,
21 the Companies' actual O&M expenses may not escalate as the Petitioners propose to
22 assume in the shared savings plan. Further, some of the employee reductions
23 planned for after the merger may have been achievable without the merger. The

1 Petitioners' proposed method of measuring merger savings is significantly inadequate
2 to identify verifiable and actual merger savings.

3 Indeed, Petitioners' witnesses Powell and Reilly at page 14 of their joint
4 testimony, state that the Petitioners have not chosen to pursue a standard Wall Street
5 corporate merger that would produce savings through labor force reductions and
6 aggressive consolidation of facility system and technology. The witnesses contend
7 that that type of merger is not in the best interest of Vermont. To the extent these
8 efficiency enhancements to management practices can be achieved without
9 extraordinary efforts, all reasonable I&C merger-related costs should be recovered in
10 rates, and all savings should flow through to customers.

11 **Q YOU STATED EARLIER THAT YOU BELIEVE IT WOULD BE A BALANCED PLAN**
12 **TO REJECT THE SAVINGS SHARING MECHANISM AND SIMPLY ALLOW THE**
13 **PETITIONERS TO RECOVER THEIR COST OF SERVICE AFTER THE MERGER**
14 **TAKES PLACE. WHY IS THIS REASONABLE?**

15 **A** This is reasonable because most of the estimated savings identified by the
16 Petitioners relate to the normal course of business. For example, as outlined in
17 Petitioners' witness Bugbee's testimony, a large portion of the estimated savings is
18 based on labor force cost reductions. (Bugbee Prefiled Testimony at 3). As noted by
19 Ms. Powell, these labor force cost reductions will not be produced through
20 accelerated employee reductions, but rather will be produced by the turnover and
21 attrition of employees as they approach retirement age or leave the utility. (Powell
22 and Riley Prefiled Testimony at 13-14).

1 As such, ratepayers will pay for these employees while working, and pay for
2 the utility's cost of employee retirement. The merged Company's ability to forego
3 replacing these employees immediately will simply be a reduction to its cost of
4 service. Other savings opportunities relate to the elimination of redundant facilities
5 and services between the two Companies. Similar to employee costs, ratepayers will
6 pay actual costs as long as they are incurred irrespective of whether these possible
7 savings are realized.

8 **Q ARE THE PETITIONERS PROPOSING TO RECOVER FROM RETAIL**
9 **CUSTOMERS THE ACQUISITION PREMIUM GMP WILL PAY FOR CVPS?**

10 A No. (DPS:PET.1-62). This is consistent with the regulatory treatment for the
11 acquisition premium Gaz Metro originally paid for GMP in the last merger. An
12 acquisition premium reflects a payment from one investor to another investor to take
13 control of the company. This acquisition premium does not reflect an investment by
14 an investor into the operating company in order to support investments in utility plant
15 and equipment. Therefore, an acquisition premium is not a cost related to providing
16 utility service.

17 **Q DID THE COMPANIES OFFER OTHER REASONS WHY THEY BELIEVE THE**
18 **SHARED SAVINGS PLAN IS JUSTIFIED?**

19 A Yes. In response to DPS:PET.1-50, the Company asserts that the integration of GMP
20 and CVPS is not required as a result of the merger. Therefore, the Company asserts
21 that customers are not entitled to integration savings because the integration of GMP
22 and CVPS is not an acquisition requirement. (DPS:PET.1-50).

1 **Q IS THIS REASONABLE JUSTIFICATION FOR THE SHARED SAVINGS PLAN?**

2 A No. The Petitioners propose to include merger I&C costs as a component of actual
3 O&M expense and recover this expense from customers in the ARP rate-setting
4 process. (DPS:PET.1-55). Since customers will pay all merger costs, they are
5 entitled to all merger savings.

6 Further, the Companies need to demonstrate the proposed merger is in the
7 public interest. The proposed merger may have long-term competitive implications in
8 terms of ownership of the transmission system in Vermont and could create negative
9 credit rating impacts on the merged Vermont company under Gaz Metro ownership.
10 Indeed, the only measure of concrete benefit to customers is the claim (which is
11 unsubstantiated) that the merger will create cost of service savings. If the Petitioners
12 are not expecting to produce customer benefits by this acquisition, then the Board
13 should not approve the requested merger unless the Petitioners prove the public
14 interest is not harmed by the proposed acquisition.

15 **Q PLEASE EXPLAIN HOW THE CHANGE IN CONTROL OF THE VERMONT**
16 **TRANSMISSION SYSTEM COULD RESULT IN NEGATIVE IMPACTS TO**
17 **CUSTOMERS.**

18 A Under the proposed transaction, Gaz Metro will acquire CVPS's interest in Vermont
19 Electric Power Company (VELCO) and the Vermont Transco, LLC (Transco).
20 Currently, GMP and CVPS control more than 50% of VELCO, and 72% in Transco.²
21 However, 33% of CVPS's current voting shares of VELCO would be transferred to
22 Vermont Low Income Trust for Electricity, Inc. ("VLITE") and the Transco operating

²Prefiled Testimony of Powell and Reilly at 20-21.

1 agreement will be modified to prevent the combined Company from controlling
2 Transco. The transaction is structured to at least initially keep the Petitioners' control
3 of VELCO at less than 50%. (Petition of CVPS et al. at 5; Prefiled Testimony of
4 Powell and Reilly at 18).

5 The Petitioners will own a controlling interest (72%) in Transco LLC (the
6 owner of the transmission assets), and this Transco ownership is not fixed but will
7 change based on the participants' actual investment in new transmission plant.
8 VELCO is the manager of the transmission assets, under the Transco operating
9 agreement, VELCO can be replaced as the manager of Transco.

10 It is possible that the Petitioners could at a later point gain operating control of
11 the Transco assets if VELCO is replaced as the transmission asset operating
12 manager. While the revised Transco operating agreement attempts to limit the
13 Petitioners' ability to change control of Transco, the Petitioners could potentially take
14 control of the Vermont transmission assets if VELCO is replaced as the Transco
15 manager or if the Transco operating agreement is later changed to reflect the
16 Petitioners' majority ownership.

17 **Q PLEASE EXPLAIN HOW GMP'S CREDIT RATING COULD RESULT IN NEGATIVE**
18 **IMPACTS TO CUSTOMERS.**

19 **A** Potential negative impacts on GMP's bond rating can be mitigated as discussed later
20 in this testimony. However, to the extent there is inadequate separation between
21 GMP's cash flows and business interests, GMP's credit rating could be negatively
22 impacted by its affiliation with Gaz Metro and its other non-regulated operations.
23 Hence, the merger does create uncertainty and potential risk to the public.

1 **Q ARE THERE OTHER CONDITIONS THE BOARD SHOULD IMPOSE IF IT**
2 **APPROVES THE PROPOSED ACQUISITION?**

3 A Yes. If the Board approves the proposed acquisition, then it should put in place the
4 following additional restrictions:

- 5 1. The change in control costs should not be included in cost of service and
6 recovered from customers. Rather, this should be an acquisition cost that
7 should be paid for entirely by shareholders.
- 8 2. The Company states that the goodwill recorded under the acquisition will
9 be recorded on NNEEC's balance sheet and not GMP's post-merger
10 balance sheet. The Company should further guarantee that a goodwill
11 asset will not be recorded on the balance sheet of GMP, and if it is, any
12 common equity supporting that goodwill asset will not be included in the
13 capital structure used to set rates.

14 The Petitioners indicated that they do not plan to recover the acquisition
15 premium and change in control cost from customers. (DPS:PET.1-62 and 1-64). The
16 Board should require that Petitioners also commit that GMP's capital structure used to
17 set rates will not be impacted by the recording of a goodwill asset.

18 **Q PLEASE EXPLAIN WHY THE COMPANY'S CHANGE IN CONTROL COSTS**
19 **SHOULD NOT BE INCLUDED IN RETAIL COST OF SERVICE.**

20 A To the extent these merger costs relate to executive severance packages or merger
21 consultant/legal fees, then customers should not bear the costs which are not directly
22 related to providing utility service. Rather, merger costs unrelated to costs incurred to
23 directly produce utility cost reductions or savings should be borne by shareholders.

24 It is appropriate to exclude recovery of change in control cost because that
25 provides adequate incentive for utilities to negotiate no more than reasonable change
26 in control cost. If change in control expenses could be passed on to retail customers,
27 then executives would negotiate between themselves for these change in control

1 expenses with no consideration for this cost being borne by shareholders. Rather,
2 they could simply negotiate overly generous severance packages which would then
3 be passed on to retail customers. By preventing these costs from being recovered
4 from retail customers, executives have a fiduciary responsibility to their shareholders
5 to keep these costs under control and to limit them to no more than reasonable
6 amounts.

7 **Q PLEASE EXPLAIN WHY THE CAPITAL STRUCTURE USED TO SET RATES**
8 **SHOULD NOT REFLECT THE IMPACTS OF RECORDING A GOODWILL ASSET**
9 **ON THE UTILITY'S BALANCE SHEET.**

10 A If a goodwill asset is recorded on GMP's balance sheet, then common equity will be
11 written up to balance the increase to the asset side of the balance sheet with an
12 increase to the liability side of the balance sheet. If common equity is written up to
13 recognize the recording of a goodwill asset, then the capital structure used to set
14 rates would have a higher ratio of common equity as a percentage of total capital.
15 This would unnecessarily increase the overall cost of capital because common equity
16 is the highest cost utility capital component, and is also subject to income tax
17 expense.

18 Also, the increase in common equity related to recording a goodwill asset is
19 not common equity that was used to fund an investment in utility plant and
20 equipment. Rather, it is related to the cost of the merger. Therefore, the capital
21 structure used to set rates should exclude this merger cost component.

1 **Financial Integrity**

2 **Q ARE THE PETITIONERS PROPOSING ADDITIONAL PROTOCOLS OR**
3 **SAFEGUARDS TO ENSURE THE VERMONT UTILITY'S CREDIT STANDING IS**
4 **ISOLATED FROM THAT OF ITS PARENT COMPANY AND AFFILIATES OF GAZ**
5 **METRO?**

6 A No. However, in the previous merger the Company did implement appropriate
7 safeguards to create isolation in GMP's credit standing from that of Gaz Metro and its
8 affiliated companies. The Company outlines current protocols through restricted
9 movement of cash out of GMP in response to IBM:PET.2-3. This data response is
10 attached as Exhibit MPG-2.

11 **Q DO YOU RECOMMEND ANY CHANGE TO THESE CASH MOVEMENT**
12 **RESTRICTIONS AS A CONDITION OF MERGER APPROVAL IN THIS CASE?**

13 A Yes. I recommend that these conditions of the merger be expanded to include the
14 following:

- 15 1. GMP's Board should agree that GMP will not be allowed to write loans to
16 any affiliated company that is not also rate-regulated under U.S. or
17 Canadian regulatory jurisdiction.
- 18 2. The Company should agree that at least two of GMP's and/or NNEEC's
19 Board members will be independent of other Gaz Metro businesses.

20 **Q WHY WOULD IT BE APPROPRIATE FOR GMP TO AGREE NOT TO WRITE**
21 **LOANS TO NON-REGULATED AFFILIATES?**

22 A GMP will not and cannot write loans to any non-regulated affiliated entity. By non-
23 regulated, I mean any affiliate that is not regulated by a U.S. state rate regulatory
24 authority, or the Federal Energy Regulatory Commission. For any loans between

1 GMP and entities with rate regulations by Canadian rate regulators, GMP should
2 seek Board approval before any loans are written.

3 This restriction on GMP's ability to write loans to non-regulated companies will
4 provide greater assurance that all cash flows produced by regulated utility operations
5 will be used first and foremost for the cash needs of the utility. An ability to write
6 loans from a utility to a non-regulated company will provide non-regulated companies
7 access to the utility's cash flows to support non-regulated business interests. This
8 lack of restrictions on ability to move cash within Gaz Metro, provides far too much
9 management discretion to use utility cash flow for non-utility needs. This restriction
10 on utility cash movement will also support the utility's credit ratings in that it should
11 minimize the effects on the utility's credit rating from the risk created by Gaz Metro's
12 non-regulated business units.

13 **Q WHY WOULD IT BE APPROPRIATE FOR GMP AND/OR NNEEC TO HAVE TWO**
14 **BOARD MEMBERS WHICH ARE INDEPENDENT OF OTHER GAZ METRO**
15 **AFFILIATED COMPANIES?**

16 **A** Maintaining at least two "independent" Board members will ensure that there are
17 voices on GMP's and NNEEC's Boards that are unbiased in their outlook for GMP's
18 obligations to provide high quality utility service in the State of Vermont. Board
19 members who sit on Boards at GMP, Gaz Metro or other affiliated companies may
20 have conflicts of interest between their obligations to GMP and Vermont, and other
21 Gaz Metro affiliated companies' business interests.

1 This assurance of independent voices on GMP's and/or NNEEC's Boards,
2 whose only fiduciary responsibility is to GMP, will serve as additional protection for
3 utility operations, cash flow uses and dividend paying decisions.

4 **Q DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

5 **A Yes, it does.**

Qualifications of Michael P. Gorman

1 **Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A Michael P. Gorman. My business address is 16690 Swingley Ridge Road, Suite 140,
3 Chesterfield, MO 63017.

4 **Q PLEASE STATE YOUR OCCUPATION.**

5 A I am a consultant in the field of public utility regulation and a Managing Principal with
6 Brubaker & Associates, Inc., energy, economic and regulatory consultants.

7 **Q PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND WORK
8 EXPERIENCE.**

9 A In 1983 I received a Bachelors of Science Degree in Electrical Engineering from
10 Southern Illinois University, and in 1986, I received a Masters Degree in Business
11 Administration with a concentration in Finance from the University of Illinois at
12 Springfield. I have also completed several graduate level economics courses.

13 In August of 1983, I accepted an analyst position with the Illinois Commerce
14 Commission ("ICC"). In this position, I performed a variety of analyses for both formal
15 and informal investigations before the ICC, including: marginal cost of energy, central
16 dispatch, avoided cost of energy, annual system production costs, and working
17 capital. In October of 1986, I was promoted to the position of Senior Analyst. In this
18 position, I assumed the additional responsibilities of technical leader on projects, and
19 my areas of responsibility were expanded to include utility financial modeling and
20 financial analyses.

1 In 1987, I was promoted to Director of the Financial Analysis Department. In
2 this position, I was responsible for all financial analyses conducted by the staff.
3 Among other things, I conducted analyses and sponsored testimony before the ICC
4 on rate of return, financial integrity, financial modeling and related issues. I also
5 supervised the development of all Staff analyses and testimony on these same
6 issues. In addition, I supervised the Staff's review and recommendations to the
7 Commission concerning utility plans to issue debt and equity securities.

8 In August of 1989, I accepted a position with Merrill-Lynch as a financial
9 consultant. After receiving all required securities licenses, I worked with individual
10 investors and small businesses in evaluating and selecting investments suitable to
11 their requirements.

12 In September of 1990, I accepted a position with Drazen-Brubaker &
13 Associates, Inc. ("DBA"). In April 1995, the firm of Brubaker & Associates, Inc. ("BAI")
14 was formed. It includes most of the former DBA principals and Staff. Since 1990, I
15 have performed various analyses and sponsored testimony on cost of capital,
16 cost/benefits of utility mergers and acquisitions, utility reorganizations, level of oper-
17 ating expenses and rate base, cost of service studies, and analyses relating to
18 industrial jobs and economic development. I also participated in a study used to
19 revise the financial policy for the municipal utility in Kansas City, Kansas.

20 At BAI, I also have extensive experience working with large energy users to
21 distribute and critically evaluate responses to requests for proposals ("RFPs") for
22 electric, steam, and gas energy supply from competitive energy suppliers. These
23 analyses include the evaluation of gas supply and delivery charges, cogeneration
24 and/or combined cycle unit feasibility studies, and the evaluation of third-party

1 asset/supply management agreements. I have participated in rate cases on rate
2 design and class cost of service for electric, natural gas, water and wastewater
3 utilities. I have also analyzed commodity pricing indices and forward pricing methods
4 for third party supply agreements, and have also conducted regional electric market
5 price forecasts.

6 In addition to our main office in St. Louis, the firm also has branch offices in
7 Phoenix, Arizona and Corpus Christi, Texas.

8 **Q HAVE YOU EVER TESTIFIED BEFORE A REGULATORY BODY?**

9 A Yes. I have sponsored testimony on cost of capital, revenue requirements, cost of
10 service and other issues before the Federal Energy Regulatory Commission and
11 numerous state regulatory commissions including: Arkansas, Arizona, California,
12 Colorado, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas,
13 Louisiana, Michigan, Missouri, Montana, New Jersey, New Mexico, New York, North
14 Carolina, Oklahoma, Oregon, South Carolina, Tennessee, Texas, Utah, Vermont,
15 Virginia, Washington, West Virginia, Wisconsin, Wyoming, and before the provincial
16 regulatory boards in Alberta and Nova Scotia, Canada. I have also sponsored
17 testimony before the Board of Public Utilities in Kansas City, Kansas; presented rate
18 setting position reports to the regulatory board of the municipal utility in Austin, Texas,
19 and Salt River Project, Arizona, on behalf of industrial customers; and negotiated rate
20 disputes for industrial customers of the Municipal Electric Authority of Georgia in the
21 LaGrange, Georgia district.

1 Q PLEASE DESCRIBE ANY PROFESSIONAL REGISTRATIONS OR
2 ORGANIZATIONS TO WHICH YOU BELONG.

3 A I earned the designation of Chartered Financial Analyst (“CFA”) from the CFA
4 Institute. The CFA charter was awarded after successfully completing three
5 examinations which covered the subject areas of financial accounting, economics,
6 fixed income and equity valuation and professional and ethical conduct. I am a
7 member of the CFA Institute’s Financial Analyst Society.

9530/209352

Green Mountain Power Company Merger Regulatory Plans

Companies Involved	Jurisdiction	Docket Number	Date of Final Order	Description
Narragansett Blackstone Newport	Rhode Island Public Utilities Commission	2930	3/14/2000	-merged company's revenues will be reduced by an annual amount of \$2.7M, and rates frozen through December 31, 2004 -following the rate freeze period, the merged company will be allowed to retain 50% of any proven merger savings in future rate cases through 2019, under certain conditions
Energy North Keyspan	New Hampshire Public Utilities Commission	DG 06-107	7/12/2007	Granite State Rate Plan -\$2.2M distribution rate reduction for electric customers -reduced distribution rates frozen for a 5-year rate plan period, through December 31, 2012 -acquisition premiums associated with this or any prior merger will be excluded from future rate cases -after the 5 year rate freeze, Granite State can retain earnings greater than the 9.67% ROE, but must share anything over 11.0% equally between ratepayers and stockholders Energy North Merger Rate Agreement gas delivery rates frozen for 1 year post merger -exclusion of merger acquisition costs from any future rate cases -ratepayers benefit through a merger savings credit equal to \$619,000 to be reflected in the first rate case, 50% of any proven merger-related savings in a second rate case, and all merger-related savings in subsequent rate cases, until the 10th anniversary of the close of the merger.
KPL KGE	Kansas Corporation Commission	172, 745-U	11/15/1991	-KGE & KPL electric rates frozen until August 1995 -KPL gas rates frozen until August 1995 -retail electric customers receive 3 cash refunds totaling \$32M during the rate freeze period (\$8.5M as soon as merger is effective, \$8.5M in December 1993, \$15M in September 1994) -merger-related savings in excess of annual amortization amount of the acquisition premium shared between ratepayers and stockholders on 50/50 basis, beginning August 1995
Entergy GSU	Louisiana Public Service Commission	U-19904	5/3/1993	-Gulf States will flow through all Louisiana merger-related fuel savings to Louisiana customers through the fuel clause -to the extent that the merger produces non-fuel O&M savings in a year, 60% allocable to Louisiana retail operations can be included in the revenue requirement with that year as a test year -5 year rate ceiling (rates cannot be increased to a level above the rates in effect at the date of closing) -8 year rate rider that flows through COS reductions to customers (the rider cannot be a positive value during the first 5 post-merger years) -during years 6 through 8, Gulf States may request an increase in base rates, but will not be allowed to include the shared merger-related savings in the rate case
IL-American Citizens	Illinois Commerce Commission	00-0476/ 01-0556	7/16/2002	-no acquisition costs can be recovered from ratepayers -50/50 savings sharing between stockholders and ratepayers -the revenue requirement will be allowed to be increased to account for 50% of demonstrated acquisition savings only in rate cases filed within 3 years of the date of the final order.

Green Mountain Power Company Merger Regulatory Plans

Companies Involved	Jurisdiction	Docket Number	Date of Final Order	Description
New England Gas Providence Gas Valley Gas Bristol & Warren Gas	Rhode Island Public Utilities Commission	3401	2/28/2003	-immediate \$3.9M rate reduction, totaling \$11.7M over 3 years -reduced distribution rates frozen for 3 years, through June 2005 -from the end of the rate freeze period through June 30, 2010, earnings sharing on a 50/50 basis when NEGas' ROE is 11.25% to 12.25%, and 75/25 split in favor of ratepayers when ROE is above 12.25%
National Grid keyspan	New York Public Service Commission	06-M-0878	9/17/2007 BAI Project #8686	-proven synergy savings will be reflected in the revenue requirement, and flowed through to customers -50/50 savings split between customers and shareholders
Gaz Metro GMP	Vermont Public Service Board	7213	3/26/2007 BAI Project #8700	-transaction costs cannot be recovered from ratepayers -50% of savings shared with ratepayers through a total investment of \$9.3M in an Efficiency Fund that would focus on energy efficiency projects, demand response programs, renewable and clean energy, and emerging technology. If GMP fails to provide the required benefit by December 31, 2014, or fails to make the required investment by March 31, 2014, GMP must file a plan for approval specifying how the required benefits will be delivered, or how the uninvested amount will be returned to ratepayers

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- Q.IBM:PET.2-3: Please describe the following protocols between movements of cash into or out of GMP and NNEEC:
- a. Please outline conditions under which GMP can and cannot make dividend payments to NNEEC.
 - b. Please describe whether GMP can refuse to pay dividends if the earnings are needed to support GMP's financial integrity or capital expenditure program.
 - c. Please outline conditions under which GMP can write loans to NNEEC, or other affiliates.
 - d. Please outline conditions under which NNEEC will make equity infusion in GMP.

A.IBM:PET.2-3.a: As a condition of GMP's merger order under Docket No. 7213 dated March 26, 2007 with Gaz Métro:

The Company shall provide 30 days' advance notice to the Board and Department if (1) the equity proportion of the capital structure varies by more than three percent from the structure approved in GMP's latest rate proceeding; (2) its unused, short-term-borrowing capacity falls below \$15 million; or (3) GMP makes distributions to its parent company after it has been placed on CreditWatch with negative implications or if the equity proportion of the capital structure varies by more than three percent from the structure approved in GMP's latest rate proceeding.

As a condition of GMP's unsecured revolving credit facility:

Section 8.5 Dividends; Distributions. Declare or pay any dividends (other than dividends payable in shares of common stock of the Company) on, or make any other distribution in respect of, any shares of any class of capital stock of the Company, or apply any of its property or assets to, or set aside any sum for, the payment, purchase, redemption or other acquisition or retirement of, any shares of any class of capital stock of the Company, if, after giving effect to such dividend or other distribution, the result of such dividend or other distribution would have a Material Adverse Effect.

Section 8.8 Funded Debt to Capitalization Ratio. Permit the total amount of Consolidated Funded Debt to exceed sixty percent (60%) of Consolidated Total Capitalization.

In compliance with Section 6.40 of the Vermont Business Corporation Act:

That GMP has sufficient reserves and unrestricted earned surplus and is authorized to make a distribution to its shareholder.

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A.IBM:PET.2-3.b: Dividend payments are at the discretion of the GMP Board of Directors.

A.IBM:PET.2-3.c: There are no conditions addressing the extent to which GMP can write loans.

A.IBM:PET.2-3.d: There are no specific conditions other than what is stated in the March 26, 2007 order in Docket No. 7213, which highlights the following:

Findings 41. Gaz Métro and NNEEC view GMP as a long-term investment that will produce stable terms, and Gaz Métro, through NNEEC, will be a strong source of capital support for GMP where there are opportunities to grow GMP through capital investment. Gilbert pf. at 5; Despars pf. at 4, 8.

Findings 49. Gaz Métro will be the sole shareholder of GMP and will make the investments in GMP needed to maintain its service quality. Tr. 1/16/07 at 164, 168 (Despars).

Person Responsible for Response: Dawn D. Bugbee
Title: Chief Financial Officer, GMP
Date: December 9, 2011