STATE OF VERMONT
PUBLIC SERVICE BOARD

Amended Joint Petition of Central Vermont Public Service Corporation, Danaus Vermont Corp., Gaz Métro Limited Partnership, Gaz Métro inc., Northern New England Energy Corporation for itself and as agent for Gaz Métro Limited Partnership's parents, Green Mountain Power Corporation and Vermont Low Income Trust for Electricity, Inc. for approval of: (1) the merger of Danaus into and with Central Vermont, (2) the acquisition by Northern New England of the common stock of Central Vermont, (3) the amendment to Central Vermont's Articles of Association, (4) the merger of Central Vermont into and with Green Mountain, and (5) the acquisition by VLITE of a controlling interest in Vermont Electric Power Company, Inc.	)	Docket No. 7770

INITIAL BRIEF OF THE PETITIONERS

The Petitioners[1] submit this Initial Brief to address several issues that require extended legal and policy analysis. As explained below, (1) Petitioners' proposal to guarantee $144 million in savings, in combination with other benefits of the transaction, satisfies CVPS's so-called windfall sharing obligation, (2) the proposed Community Energy & Efficiency Development ("CEED") Fund independently satisfies the windfall sharing obligation, (3) the Petitioners' proposed savings sharing plan is supported by sound public policy and applicable precedent, and (4) the proposed conditions relating to control of Vermont Electric Power Company, Inc. ("VELCO") assure that GMP will not control VELCO. The Brief also addresses several issues raised by the Vermont Public Service Board ("Board") or by other parties during the hearings.

As an initial matter, Petitioners have demonstrated that the proposed acquisition of CVPS and the merger of GMP and CVPS meet the criteria set forth in 30 V.S.A. §§ 107, 109, and 311.

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[1] Central Vermont Public Service Corporation ("CVPS" or "Central Vermont"), Danaus Vermont Corp. ("Danaus"), Northern New England Energy Corporation ("NNEEC"), for itself and as agent for the direct and indirect upstream parents of Gaz Métro Limited Partnership ("Gaz Métro"), Gaz Métro, Gaz Métro inc. ("GMi"), Green Mountain Power Corporation ("GMP" or "Green Mountain Power"), and Vermont Low Income Trust for Electricity, Inc. ("VLITE").

In particular, as a result of the acquisition and merger the surviving company (1) will be technically competent, (2) financially sound, (3) will act as a fair partner in business transactions with the citizens of Vermont, (4) will create efficiencies that benefit customers, and (5) will not impair or obstruct competition in the energy markets.[2] The evidence, as summarized in the discussion section of Petitioners' Proposed Decision, amply demonstrates that the acquisition and merger will result in a financially stronger and more efficient company, lower rates and higher quality service, and no adverse impact on competition. In particular, the proposal results in $144 million in guaranteed savings to customers, implements a minimum of $25 million in efficiency and weatherization benefits, results in a stronger GMP, avoids any layoffs (except for executives) or mandatory relocations, continues CVPS's strong support to the Rutland area economy, and provides many other benefits to Vermont. Moreover, the acquisition and merger have already received approval from the Federal Energy Regulatory Commission ("FERC"), the Committee on Foreign Investments in the United States, the Federal Communications Commission, and the Maine Public Service Commission, and waivers from the New York Public Service Commission and the Federal Trade Commission.[3]

I. THE PETITIONERS' ORIGINAL PROPOSAL TO GUARANTEE $144 MILLION IN SAVINGS, IN COMBINATION WITH OTHER BENEFITS OF THE TRANSACTION, SATISFIES THE WINDFALL SHARING OBLIGATION

In its Docket Nos. 6460/6120 Order, the Board established the following requirements for the so-called windfall sharing obligation:

1. Trigger: Merger of CVPS with another company, acquisition of control of CVPS requiring Section 107 approval, and sale or lease of CVPS assets requiring Section 109 approval;
2. Cap: $16 million in year-2001 dollars (*i.e.*, adjusted for inflation);
3. Beneficiaries: CVPS customers during the period the value is returned to customers;
4. Specific Procedure: To be determined in a future proceeding; and

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[2] *Joint Petition of Green Mountain Power Corp.*, Docket No. 7213 (Vt. Pub. Serv. Bd. Mar. 26, 2007) at 9-10. The discussion section of the Proposed Decision also addresses the remaining criteria, relating to transaction terms and impact on customers, impact on employees, and consistency with 2005 Vermont Electric Plan.

[3] Powell-Reilly reb. pf. at 5 (Powell); tr. 3/21/12 at 161-62 (Reilly); exh. WEC-Cross-14.

5. Constraint: Sharing mechanism will be designed not to undermine CVPS's access to capital markets.[4]

These requirements are, except for the cap, identical to the windfall sharing obligation that the Board imposed on GMP in Docket 7213.

As the Board stated in the Docket 6460/6120 Order, the "benefit provided to ratepayers" in satisfaction of the windfall sharing obligation must be "in addition to (rather than a replacement for) other benefits appropriately assigned to ratepayers at the time of the first triggering event."[5] The triggering event consists of "a financial windfall for shareholders as the result of an acquisition offer or asset sale at substantially above book value."[6] The triggering event in this case is the acquisition of CVPS, which results in the payment in excess of book value to CVPS shareholders.

The benefits associated with the acquisition of CVPS in the absence of a merger are very limited. For instance, they would have amounted to only $3 million per year if Fortis had acquired CVPS.[7] The unique merger with GMP, in contrast, creates substantial additional benefits, including the $144 million customer savings guarantee, the additional on-going savings to customers (approximately $500 million over twenty years),[8] the Rutland area benefits, and the many other benefits associated with the merger. These benefits created by this unique merger are in addition to the benefits arising from the triggering event, and therefore satisfy the windfall sharing obligation requirements. In this case, the Board has the benefit of a clear comparison to

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4 *Tariff Filing of Central Vermont Public Service Corp.*, Docket Nos. 6460/6120, (Vt. Pub. Serv. Bd. June 26, 2001) ("Docket 6460/6120 Order") at 60-66.

5 Docket 6460/6120 Order at 65.

6 As the Board stated in the Docket 6460/6120 Order, the windfall sharing obligation is "a mechanism to protect against the unjust enrichment of CVPS's shareholders at the expense of CVPS's ratepayers," which could result where inclusion in rates of above-market costs "lead[s] to a financial windfall for shareholders as the result of an acquisition offer or asset sale at substantially above book value." Docket 6460/6120 Order at 58-59. The event triggering the obligation is any one of the following: (1) any merger of [CVPS] with another company; (2) any acquisition of control of [CVPS] that requires Board approval under 30 V.S.A. § 107; and (3) the sale or lease of any of [CVPS's] assets so substantial as to require Board approval under 30 V.S.A. § 109.
Docket 6460/6120 Order at 60 (quoting *Tariff Filing of Green Mountain Power Corp.*, Docket No. 6107 (Vt. Pub. Serv. Bd. Jan. 23, 2001) ("Docket 6107 Order") at 112 (footnote omitted)).

7 Tr. 3/21/12 at 167 (Reilly).
A review of Exh. Pet.-DDB-2 also demonstrates that most of the customer benefits in this case relate to the GMP-CVPS merger, rather than the acquisition of CVPS. Without the merger, CVPS would continue to exist as a separate company and there would be no elimination of costs associated with duplicate management, boards of directors, audits, and regulatory filings, which are on the order of at least $40 million over the first ten years following the acquisition. Similarly, the balance of the $144 million in projected customer savings can be achieved only through the complete integration of personnel, systems, and assets into a single company, which cannot occur in the absence of a merger.

8 Bugbee pf. at 2-4.

the Fortis acquisition proposal—against which to measure the benefits appropriately assigned to ratepayers at the time of the first triggering event.

There is also no basis for claiming that the acquisition and merger are a single triggering event. They are separate transactions that will occur several months apart.[9] In addition, only the acquisition includes the critical characteristic of a triggering event: the transfer of above-book consideration to CVPS shareholders that the windfall sharing mechanism was designed to address. The CVPS shareholders receive no consideration or other benefits whatsoever from the merger; instead, all benefits to CVPS shareholders occur "at the time of the first triggering event."[10]

For these reasons, the many benefits associated with the proposed merger satisfy the windfall sharing obligation.

II. THE CEED FUND INDEPENDENTLY SATISFIES THE WINDFALL SHARING OBLIGATION

In response to testimony of the Department of Public Service ("Department"), the Petitioners proposed a CEED Fund in rebuttal testimony as an additional means for satisfying the obligation. The proposed CEED Fund is very similar to the Efficiency Fund approved by the Board in Docket 7213. The two plans, for instance, include (1) a "but for" test for selecting projects, (2) a minimum investment requirement, (3) rate recovery of investments, (4) measurement and reporting methodology, (5) a seven-year deadline for achieving the required

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[9] As the Board stated in reviewing a prior transaction, "[s]trictly speaking, the acquisition of Allied by CVPS could be approved, but the merger not. In such circumstances, Allied would continue to be operated as a distinct entity, but its owners would be CVPS' owners." *Re Central Vermont Public Service Corp.*, Docket No. 5396 (Vt. Pub. Serv. Bd. July 18, 1990) ("Allied Order") at 13. The Board noted, however, it is likely that the companies would be merged, given the geographical and contractual relationships, especially since the Allied service territory (in the Pittsford, Vermont area) is surrounded by the CVPS service territory. *Id.*; exh. Pet-BO-1.

In other cases, two utilities that became affiliates as a result of an acquisition were not merged, even though they were in the same industry and operated in the same state. *E.g.*, *Re Comm South Companies of Virginia, Inc.*, Case No. PUA010012 (VA State Corp. Comm'n. May 31, 2001) 2001 WL 812235, at *2; *Joint Petition of Comm South Companies, Inc., etc.*, Case No. 01-C-0351 (N.Y. Dept. Pub. Serv. May 4, 2001) 2001 WL 1734754, at *1; *Re AquaSource Utility, Inc.*, Case No. PUA980048 (VA State Corp. Comm'n. March 8, 1999) 1999 WL 288883, at *1; *In re: Joint Petition for Approval of Transfer of Controlling Stock Interest in the Florala Telephone Company, Inc., etc.*, Docket No. 951133-TV (Fla. Pub. Serv. Comm'n. Dec. 15, 1995) 1995 WL 762236, at *1.

[10] Docket 6460/6120 Order at 65

level of benefits, (6) Board approval of methodology for calculating net benefits, and (7) a plan to address the consequences for failure to achieve required investment or benefits.[11]

In connection with the Memorandum of Understanding dated March 26, 2012 ("DPS MOU"),[12] the Petitioners and the Department agreed to several changes to the CEED Fund. The changes are identified in the marked version of the CEED Fund filed with the Board and the parties on March 29, 2012. Among other improvements, the revised CEED Fund requires net benefits totaling at least 20% more than the amount of the windfall sharing obligation, and the DPS MOU requires an accelerated investment of at least $12 million in weatherization benefits before the end of 2013.[13]

Only one party, AARP, opposes the CEED Fund as an appropriate means of satisfying the windfall sharing obligation. AARP's opposition disregards this Board's decision in Docket 7213 that GMP's Efficiency Fund was an appropriate mechanism to satisfy GMP's identical windfall sharing obligation.[14] In Docket 7213, the Board twice addressed the question whether GMP's Efficiency Fund satisfied the "windfall sharing obligation." First, the Board considered and rejected AARP's summary judgment motion to preclude the Efficiency Fund and to require that GMP satisfy the windfall sharing obligation by means of a cash payment by GMP stockholders to GMP customers immediately upon the acquisition of GMP.[15] The Board carefully considered and rejected AARP's arguments. The Board noted that the Docket 6107 Order does "not definitely establish the characteristics of the windfall-sharing mechanism," "does not mandate that shareholders provide specific funds to ratepayers," and "is silent as to the source of the funds and how any sharing must occur."[16] Accordingly, the Board ruled that it

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11 Griffin reb. pf. at 11-12.

12 Exh. Petitioners-DPS-1.

13 Exh. Petitioners-DPS-1, Attachment II. The DPS MOU also provides that the weatherization investments will be deemed to have a benefit-cost ratio of 1.2. Exh. Petitioners-DPS-1 ¶ 20. Although these features differ from the Efficiency Fund approved by the Board in Docket 7213, they do not provide a basis for concluding that the CEED Fund fails to meet the Docket 7213 requirements, especially where they have been included at the Department's request and have been supported by extensive expert Department testimony. *See, e.g.*, Hopkins reb. pf. at 2-3; tr. 3/29/12 at 70-139 (Hopkins).

14 *Joint Petition of Green Mountain Power Corp.*, Docket No. 7213, Order re: Motion for Summary Judgment (Vt. Pub. Serv. Bd. Nov. 17, 2006) ("Docket 7213 Summary Judgment Order"); *Joint Petition of Green Mountain Power Corp.*, Docket No. 7213, Final Order (Vt. Pub. Serv. Bd. Mar. 26, 2007) ("Docket 7213 Final Order").

15 Docket 7213 Summary Judgment Order at 4, 7.

16 *Id.* at 6-7.

could not conclude "that the Order mandated that shareholders provide funds to ratepayers or that the return of proceeds occur in any particular manner."[17]

After the order denying summary judgment, International Business Machines Corporation ("IBM") challenged the proposed Efficiency Fund on the same grounds, claiming that "the Docket 6107 Order . . . require[d] that the Windfall-Sharing amounts come from shareholders," and seeking an order requiring "GMP to provide a refund or a bill credit to customers."[18] After hearing testimony and considering the arguments of the parties, the Board rejected IBM's challenges. The Board ruled that "GMP's proposed Efficiency Fund represents an acceptable mechanism for returning the Windfall Sharing amounts mandated by Docket 6107" and "will lead to incremental investment . . . likely to provide consumers as a whole benefits equal to or greater than they would receive through a refund, thus meeting the requirement set out in Docket 6107 as to the magnitude of the sharing."[19]

In the Docket 7213 Final Order, the Board addressed and rejected each of the claims presented by AARP's witnesses in this case. First, contrary to AARP's claim that the funds must come from CVPS shareholders, the Board stated that "[w]e are also unpersuaded that we should reject the Efficiency Fund simply because the money in the fund is not provided by shareholders ... the pivotal requirement was the mandate that ratepayers receive the benefit, not that it come from a specific source. GMP's Efficiency Fund meets this requirement."[20]

The Board rejected the claim that the windfall sharing obligation represents a loan that must be repaid to customers. The Board ruled that the Docket 6107 Order "specifically stated that the beneficiaries were not the customers who paid the higher rates, but GMP's customers at the time the Windfall Profits are distributed."[21] Unlike a loan, which involves a contract voluntarily entered into by the contracting parties, the windfall sharing obligation reflects the unilateral imposition of a regulatory requirement.

The Board rejected the claim that the windfall sharing obligation must be repaid in cash. The Board ruled that "GMP's proposal to return the Windfall Profits through the Efficiency Fund

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17 *Id.* at 7.

18 Docket 7213 Final Order at 36-37. In the interim, GMP and AARP had entered into a Settlement Agreement pursuant to which they supported Board approval of an efficiency fund that allocated $1 million to a low income pilot rate discount program. Exh. Petitioners-Cross-10. The Settlement Agreement provided that it shall not be construed as having any precedential impact on future proceedings. *Id.* at 3.

19 Docket 7213 Final Order at 37.

20 *Id.* at 40.

21 *Id.* at 38.

rather than through bill credits is a reasonable approach" and that the Docket 6107 Order "did not mandate customer refunds."[22]

The Board ruled acceptable the Efficiency Fund's design providing that GMP's investments "will not all occur in the first year of the program, but will instead occur over a seven-year program."[23] The Board rejected the argument that the Docket 6107 Order "requires prompt payment by CVPS shareholders to ratepayers unless immediate payment would impose serious financial harm on the company."[24]

Finally, the Board explicitly approved rate recovery of GMP's efficiency investments. The Board ruled that although "GMP will still earn a return of and return on its investments . . . the purposes of the Docket 6107 Order will still be achieved."[25] The Board emphasized that "[t]he effect of the inclusion of the investments in rate base is that the actual return of the financial windfall from the acquisition occurs not through the incremental investments themselves, but instead through the net benefits of each investment."[26]

AARP simply ignores the Board's decision in Docket 7213. AARP does not attempt in its current testimony to distinguish the current case from Docket 7213, in terms of circumstances, policy considerations, legal analysis, or any other factor. AARP fails to provide any reasoned basis for distinguishing the present case from Docket 7213, and AARP's witnesses utterly fail to even mention Docket 7213, except on two peripheral issues relating to generic merger approval standards and thermal efficiency measures.[27] To quote AARP's Bradford-Silkman testimony in Docket 7213, "we have seen very few such brazen attempts to ignore a clear directive from a regulatory authority."[28]

AARP's suggestion that the GMP-AARP settlement in Docket 7213[29] somehow diminishes the precedential value of the Board's Docket 7213 Summary Judgment and Final Orders is farfetched. The Docket 7213 orders establishing the GMP Efficiency Fund as a lawful and appropriate way to comply with the windfall sharing obligation were each issued after full

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22 Docket 7213 Final Order at 44.
23 *Id.* at 41.
24 Bradford-Silkman pf. at 8.
25 Docket 7213 Final Order at 44.
26 *Id.*at 38.
27 Bradford-Silkman pf. at 9; Bradford-Silkman surr. pf. at 8.
28 Exh. Petitioners-Cross-6 at 12.
29 Exh. Petitioners-Cross-10.

and complete litigation of the issues, including consideration of the same arguments advanced by AARP in this case. The Docket 7213 orders are accordingly entitled to full precedential weight.

By the end of the hearings, AARP's main argument in favor of an immediate cash repayment appeared to consist of the claim that the Petitioners are contractually obligated to complete the acquisition even if a cash repayment is required. AARP has not, however, submitted a legal analysis supporting its claim. Instead it referred in cross examination to selected portions of the Agreement and Plan of Merger ("Merger Agreement") and to brief descriptions of legal and regulatory advice provided to CVPS summarized in the Proxy Statement.[30] These references do not constitute a legal analysis of the terms of the Merger Agreement.[31] More importantly, an approval condition requiring a cash repayment would likely result in a dispute between the Merger Agreement parties, which could "end up in litigation and end up with at least a delay and potentially elimination of all the benefits of this transaction for everyone."[32]

For these reasons, there is no legal, policy, or evidentiary basis for departing from the Board's legal and policy conclusions in Docket 7213. "When an agency is changing a well established and long-standing procedure . . . it must 'supply a reasoned analysis for the change.'"[33] No such reasoned analysis has been presented in this case.

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30 Tr. 4/3/12 at 152 (Dumont).

31 The Merger Agreement provides that Gaz Métro must comply with the Board's windfall sharing order in Docket 6120/6460 and that the obligation is (when considered alone or together with other specified factors) not deemed to constitute a "Company Material Adverse Effect." Exh. Pet. Joint-2, ¶¶ 5.5(d), 8.4 (definition of Company Material Adverse Effect). The Merger Agreement also provides, however, that the government approvals required as a condition of Gaz Métro's obligation to close, shall not "impose terms or contain conditions that, individually or in aggregate, would reasonably be expected to have a material adverse effect on NNEEC, [CVPS and all NNEEC subsidiaries]." *Id.* ¶ 6.1(c); tr. 4/3/12 at 158-59 (Reilly). In addition, Mr. Reilly made clear that, based on his interpretation, the requirement to comply "doesn't say they will pay [the $21 million] directly. It says they will honor the commitment in the sharing order." Tr. 3/21/12 at 162-63 (Reilly). GMP has honored those commitments by proposing a plan that is fully consistent with the Board's Orders in Docket 7213.

32 Tr. 4/3/12 at 162-63 (Reilly).

33 *Defenders of Wildlife v. Salazar*, Civ.A. 04-1230 GK, __F. Supp. 2d__, 2012 WL 366901 *4 (D.D.C. Feb. 6, 2012) (quoting *Motor Vehicles Mfrs. of U.S., Inc. v. State Farm Auto. Ins. Co.*, 463 U.S. 29, 41 (1983)); *cf. State v. Carrolton*, 2011 VT 131 ¶ 15 ("[T]his Court is not a slavish adherent to the principle of *stare decisis*, but we will not deviate from policies essential to certainty, stability, and predictability in the law absent plain justification supported by our community's ever-evolving circumstances and experiences.").

Unlike AARP's claims, which directly and completely conflict with the Board's Orders in Docket 7213 and were unaccompanied by any evidence, the CEED Fund's changes from the GMP Efficiency Fund were supported by extensive testimony by extensive Department and GMP testimony. Griffin reb. pf. at 10-15; Plunkett reb. pf. at 4; Hopkins pf. at 14-28; Hopkins surr. pf. at 2-13. In addition, the weatherization components of the CEED Fund are conceptually consistent with thermal efficiency benefits arising in connection with programs undertaken in implementation of the GMP Efficiency Fund. *See* Tr. 3/29/12 at 122 (Hopkins); tr. 4/3/12 at 51 (Bradford).

For these reasons, AARP's proposal should be rejected and the proposed CEED Fund should be approved.

III. THE PETITIONERS' PROPOSED SAVINGS SHARING PLAN IS SUPPORTED BY SOUND PUBLIC POLICY AND APPLICABLE PRECEDENT

The Petitioners' initial savings sharing proposal provided that 10% of consolidation savings would flow to customers in the first two years, 20% of savings flowing to customers for years three and four, 33% of the savings in years five and six, and 100% of savings thereafter.[34] GMP estimated that the $144 million in customer savings sharing would amount to 57% of savings generated by the merger in the first ten years on a net present value basis.[35] If $144 million in savings were not achieved, GMP undertook to design a mechanism to be approved by the Board to provide customers with the difference between the savings that had been achieved and the $144 million.

GMP proposed to establish a base period amount of nonmerger "but-for" O&M expenses and in the future measure actual expenses against the base amount in order to establish the amount of annual savings attributable to the merger. Under the Petitioners' initial plan, the specified portion of the savings would be returned to customers for the first six years through a bill credit provided at the same time as GMP's Earnings Sharing Adjustor.[36]

The DPS MOU substantially increased the near-term savings to customers.[37] First, there will be a fixed guaranteed amount of savings during the first three years, rather than a sharing of actual savings.[38] Second, the savings to customers in the first six years is double the amount in the Petitioners' initial proposal.[39] Third, the aggregate amount of savings to customers over the ten year period increases to approximately 59% on a net present value basis.[40] Once the merger is fully implemented, moreover, the savings are largely recurring and all savings benefits accrue to the customers.[41]

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34 Powell-Reilly pf. at 10-11 (Powell); Bugbee pf. at 4.
35 Griffin reb. pf. at 2; Hevert reb. pf. at 8.
36 Griffin pf. at 2-3; Hevert reb. pf. at 10.
37 Exh. Petitioners-DPS-1 ¶¶ 15-17.
38 *Id.* ¶ 15.
39 *Id.*; Bugbee pf. at 4.
40 Tr. 4/3/2012 at 92 (Griffin); *GMP Responses to Board Record Request* filed April 6, 2012.
41 Hevert reb. pf. at 9.

The savings sharing plan set forth in the DPS MOU provides immediate, easily quantifiable value to customers, and because it requires GMP to pay customers regardless of whether savings are achieved on the anticipated timetable, it provides strong incentives for GMP to achieve savings quickly, and maintain them efficiently. The plan set forth in the DPS MOU also supports long-held state goals of efficient utility consolidation. The Department's expert witness has concluded that the plan provides an appropriate level of savings to customers as compared to the value of the transaction.[42] The Board should therefore approve the DPS MOU's savings sharing provisions.

A. The Savings Sharing Plan Is Consistent With the Decisions of the Board and Sound Public Policy

1. Cost-Saving Consolidation of Electric Utilities is in the Public Interest

The Board has emphasized in prior cases that mergers resulting in lower costs for customers should be promoted. For example, in approving the CVPS acquisition of Rochester Electric Light & Power Co. ("Rochester"), the Board stated that "consolidating the Rochester territory into CVPS's territory may advance the interest of the State in reducing the number of electric utilities while also benefitting the affected ratepayers."[43] Similarly, it stated in approving the CVPS acquisition of Allied Power and Light Company ("Allied") that although each merger proposal must be judged on its merits, "there may be significant potential for mergers of electric utilities in Vermont."[44] As the Board stated in the recent Readsboro decision, "[w]e encourage cost-effective consolidation efforts."[45] The conclusion that cost-saving mergers promote the public good is also supported in decisions from other commissions.[46]

2. Promotion of Cost-Saving Mergers through Sharing Merger-Related Savings Aligns Shareholder and Customer Interests

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42 Tr. 3/27/12 at 72, 87-88 (Wilson).

43 *Joint Petition of Central Vermont Public Service Corp. and Rochester Electric Light & Power Co.*, Docket No. 7171 (Vt. Pub. Serv. Bd. Aug. 22, 2006) ("Rochester Order") at 5.

44 Allied Order at 29.

45 *Joint Petition of Central Vermont Public Service Corp. and the Town of Readsboro,* Docket No. 7688 (Vt. Pub. Serv. Bd. July 8, 2011) ("Readsboro Order") at 13.

46 *See, e.g., In Re Connecticut Natural Gas Corp.*, Docket No. 99-09-03 (Ct. Dept. of Utility Control May 9, 2001) 2001 WL 873007, at *15 (merged company should be strongly encouraged to realize synergy savings).

Utility mergers involve significant costs and risks. In this case, for instance, the acquisition premium, Fortis break-up fee, change in control costs, and transaction costs exceed $225 million.[47] Similarly, mergers involve significant risks that are not reflected in the authorized return on equity.[48] These risks include the complexity of planning and executing the integration of two separate utilities,[49] each with its own separate billing, accounting, information technology, customer service, and information systems.[50] Utilities would have little incentive to enter into cost-saving mergers if there were no opportunity to be compensated for these costs and risks.

Sharing of merger-related savings is an appropriate means of compensating utilities for these costs and risks, aligns customer and shareholder interests, and thereby creates appropriate incentives for cost-saving mergers. Many public utility commissions have expressly concluded that savings sharing incentives are appropriate to induce utilities to enter into cost-saving mergers.[51] Where, as in this case, significant savings are likely to occur, it is important to create incentives that overcome utilities' merger-related costs and risks.[52]

The Board has permitted sharing of savings as a means for inducing electric utilities to undertake cost-saving mergers, despite the associated costs and risks.[53] For instance, in the

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47 Exh. Petitioners-Cross-13, Response No. 19; Wilson pf. at 20.

48 Hevert reb. pf. at 22.

49 Hevert reb. pf. at 9.

50 *See* Otley reb. pf. at 4.

51 *See In re PSI Energy, Inc.*, Case No. 42873 (Indiana Util. Reg. Comm'n. Mar. 15, 2006) 2006 WL 1465924, at *267 (the Indiana Commission rejected calls for higher proportion of saving to customers and noted that the savings would not have existed but for the merger); *In re Illinois-American Water Co. et al.*, Docket 00-0476 (Ill. Comm. Comm'n. May 15, 2001) 2001 WL 946389, at **266, 268, 289 (Illinois-American successfully asserted that shareholders would balk at making otherwise desirable and economic combinations if there was a lack of incentive and they were required to bear the entire burden of the acquisition adjustment); *Re Connecticut Natural Gas Corp.*, 2001 WL 873007 at *42 (merged company should be strongly encouraged to realize synergy savings); *Re Louisville Gas and Electric Co.*, Case No. 1997-00300 (Ky. Pub. Serv. Comm'n. Sept. 12, 1997) 1997 WL 740643, at **478-79.

52 Hevert reb. pf. at 22.

53 Although the Board has also reviewed and approved telecommunications mergers, they have less precedential value on the issue of savings sharing. *Joint Petition of New England Tel. & Tel., Co.*, Docket No. 5900 (Vt. Pub. Serv. Bd. Feb. 26, 1997) ("NYNEX Order"), *Joint Petition of Bell Atlantic Corp.*, Docket No. 6150 (Vt. Pub. Serv. Bd. Mar. 13, 1990 ("Bell Atlantic Order"); *Joint Petition of Verizon Communications*, Docket No. 7056 (Vt. Pub Serv. Bd. Nov. 29, 2005 ("Verizon Order"). Because the telecommunications industry is subject to far more competition than the retail electric industry in Vermont, the telecommunications merger analyses focus primarily on the merger's impact on competition. *See* NYNEX Order at 19-34; Bell Atlantic Order at 27-45; Verizon Order at 15-25. Because rates are constrained by marketplace forces to a much greater degree, the Board has devoted far less analysis to rate impacts of telecommunications mergers. *See* NYNEX Order at 39 (although savings should be directed to the benefit of ratepayers, it was "premature to delineate how NET will ensure that these savings are passed to ratepayers"); Bell Atlantic Order at 24 (no showing that merger "will produce net efficiencies cognizable under Section 107"); Verizon Order at 14 ("no evidence on which to conclude that these

Rochester Order the Board stated that it was promoting beneficial consolidation by "[a]llowing CVPS the opportunity to recover its reasonable but otherwise unrecoverable costs incurred in" completing the consolidation.[54] In that case, the Board permitted rate recovery of transaction-related costs (as distinguished from costs to achieve integration savings) associated with pole inspection and inventory, customer notices, and employment consulting.[55]

Similarly, in the Allied Order the Board denied explicit rate recovery of the $931,000 acquisition premium, but permitted CVPS to retain all of the $483,000 in annual merger-related savings due to the time lag before any rate adjustment reflecting the merger.[56] Although there was no discussion of savings sharing in connection with the Board's approval of the Citizens Utilities Company ("Citizens") acquisition of Franklin Electric Light Company ("Franklin"), the Board indicated that Citizens would save $200,000-$300,000 annually yet it did not require a rate adjustment to flow through these savings to customers.[57] The Board also permitted recovery of a portion of the acquisition premium in connection with the CVPS acquisition of the Vermont Marble Power Division of Omya Inc.[58]

The policy of permitting sharing of merger-related savings reflects the Board's conclusion that alternatives to traditional "cost of service" ratemaking often promote the public interest. For instance, the Board has permitted a utility to retain cost savings from employee reductions for one rate case cycle.[59] The Board also approved implementation of the Account Correcting for Efficiency ("ACE") mechanism, which permits a utility to accrue and recover in the next rate case, any net revenue losses specifically attributable to energy efficiency programs,

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efficiencies will translate into cost savings for residential customers"). In fact, only one of the above orders identified projected cost savings allocable to Vermont intrastate telecommunications service. NYNEX Order at 18 ($4.3 million of $600,000 million annual savings allocable to Vermont intrastate); Bell Atlantic Order at 26 ("Petitioners have not identified specific benefits flowing to Vermont consumers"); Verizon Order at 14 (no quantification of cost reductions resulting from merger). As a result, none of the merger orders prescribed the rate treatment associated with the merger.

54 Rochester Order at 5.

55 *Id.*

56 Allied Order at 14, 21.

57 *Joint Petition of Citizens Utilities Co. & Franklin Elec. Light Co.*, Docket No. 5637 (Vt. Pub. Serv. Bd. July 23, 1993) at 5.

58 *Joint Petition of Vermont Marble Power Division of Omya, Inc.*, Docket No. 7660 (Vt. Pub. Serv. Bd. June 10, 2011) at 73. The Board denied similar rate recovery in the Readsboro Order, due to the specific circumstances of that case, including the fact that rate recovery would have "the effect of rewarding [Readsboro] for a utility operation that has been deficient in its regulatory obligations." Readsboro Order at 13.

59 *Investigation into Successor Incentive Regulation Plan*, Docket 6959 (Vt. Pub. Serv. Bd. Sept. 26, 2005) at 55; *see also Petition of New England Tel. & Tel. Co.*, Docket Nos. 5001/5002/4959 (Vt. Pub. Serv. Bd. Dec. 13, 1985) at 94 (employee reductions and "other efficiencies" retained for one rate period, intended to encourage long term efficiencies that lower utility's cost of service).

which results in rate recognition of lower-than-actual revenues, and has the same effect as an above-cost rate allowance.[60] In addition, the Board temporarily permitted a utility to retain one-half of the profits associated with so-called off-system (short-term) wholesale power sales.[61] As a result, savings sharing represents a consistent Board policy of achieving positive long-term customer outcomes.

3. The Fixed Credit and Percentage Sharing Mechanisms for Sharing Savings are Consistent with Public Policy

There are generally three types of savings sharing mechanisms that have been used by public utility commissions in recent utility mergers. These include (1) savings sharing based on an estimate of actual savings (i.e., the difference between estimated costs if the merger did not occur and actual costs),[62] (2) sharing in specified proportions if the achieved return on equity exceeds a particular benchmark,[63] and (3) specified rate benefits (such as a rate freeze, rate reduction, or a schedule of credits) irrespective of the actual level of aggregate savings.[64]

The savings sharing plan reflected in the DPS MOU includes the first and third types of sharing. Consistent with the first type of sharing, the savings sharing plan provides for a fixed percentage sharing of actual savings in years 4-8.[65] Consistent with the third type of sharing, Petitioners propose to return $15.5 million to customers in the first three years following the merger.[66] The bill credits will be paid to customers regardless of the actual level of merger savings achieved.

The use of the two proposed savings sharing mechanisms is consistent with public policy. The fixed credit approach proposed for years 1-3 assures that a fixed, verifiable, pre-established

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60 *See, e.g., Investigation into Least-Cost Investments*, Docket No. 5270 (Vt. Pub. Serv. Bd. Apr. 16, 1990) at Vol. IV, 21.

61 *Petition of Green Mountain Power Corp.*, Docket No. 4865 (Vt. Pub. Serv. Bd. Sep. 6, 1984) at 55-56.

62 *See, e.g., In re Illinois-American Water Co. et al.*, 2001 WL 946389, at *274 (revenue requirement allowed to be increased to account for 50% of the demonstrated acquisition savings in rate cases filed within three years of order approving acquisition).

63 *See, e.g., In re Central Maine Power Co.*, Docket No. 2007- 355 (Me. Pub. Util. Comm'n. Feb.7, 2008) 2008 WL 704190, at *7 (merger savings above a specified ROE bandwidth will be split equally between shareholders and customers).

64 *See generally* Hevert reb. pf. at 19-20; exh. Pet.-RBH-2; *see also Re Kansas City Power & Light Co.*, Docket Nos. 172,/745-u/ 174-155-D (Kan. St. Corp. Comm'n. Nov. 15, 1991) 1991 WL 501661, at *245 (of $306-315 million in estimated savings, rates frozen for four years; during rate freeze companies issue three refunds: $8.5 million at closing, $8.5 million one year later and $15 million two years later).

65 *See* Exh. Petitioners-DPS-1 ¶ 15.

66 *Id.*

savings amount will be provided to customers during the early years, when savings will occur more slowly than they otherwise would if GMP undertook a Wall Street-type policy of layoffs to aggressively reduce costs.[67] GMP will therefore assume all of the risk associated with delivering the guaranteed savings in the early years.[68]

The annual percentage sharing approach proposed for years 4-8, on the other hand, permits customers to participate in the upside potential for greater savings. This is especially beneficial for customers since the bulk of the projected savings are expected to occur in the later years.[69]

B. The Proposed Savings Sharing Plan Is Consistent With Regulatory Precedent

1. The Allocation of Savings Between GMP and Its Customers is Supported by Precedent

The Petitioners' proposal results in an aggregate 41%/59% allocation of savings between GMP and its customers.[70] The following cases approved an allocation of savings that was less beneficial to customers:

1. Entergy and Gulf State, Louisiana, 1993: 60%(company)/40%(customer);[71]
2. PSI Energy, Indiana 2006: 58/42;[72]

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67 Powell-Reilly reb. pf. at 6 (Powell).

68 An additional incentive to realize merger savings as soon as possible results from GMP's decreasing proportion of savings. *See* tr. 3/21/12 at 70-71 (Powell). This approach is consistent with decisions by other commissions. *See Re Atmos Energy Corp.*, Docket U-25003 (La. Pub. Serv. Comm'n. Apr. 27, 2001) 2001 WL 700764, at *467 (Louisiana Commission approved a savings plan, which provided that 1) ratepayers would split the first $8.9 million in savings equally with shareholders, 2) the next $3.25 million in savings would be retained by Atmos, and 3) savings in excess of these amounts would be shared equally by shareholders and ratepayers); *see also In re Connecticut Natural Gas Corp.*, Docket 99-09-03 (Ct. Dept. Util. Control May 9, 2001) 2001 WL 873007, at **30-31 (A properly designed incentive rate plan following a merger can provide significant benefits to the company, its ratepayers and shareholders. First 200 basis points in earnings in excess of the 10.8% allowed rate of return of equity were allocated 75% to shareholders and 25% to ratepayers. The next 400 basis points were shared equally between ratepayers and shareholders. Earnings in excess of 600 basis points above allowed ROE were allocated 25% to shareholders and 75% to ratepayers.).

69 Although any savings calculation method is inherently subject to judgment because it involves a comparison of actual (merger) results with hypothetical (nonmerger) results, the percentage sharing method used for years 4-8 is the most accurate of the three commonly-used methods. Sharing of each year's earned return above a benchmark level, is premised on the assumption that all earnings above the benchmark amount are due to merger savings, and none of the increased return would have occurred absent a merger. A rate credit or rate freeze is based on estimated merger results, unlike the percentage sharing method, which is based on actual results.

70 Tr. 4/3/12 at 92 (Griffin).

71 *In re Entergy Corp.*, Docket No. U-19904 (La., Pub. Serv. Comm'n. May 3, 1993) 1993 WL 651433, at *53, Appendix 1 (60% of non-fuel O&M merger savings to shareholders).

3. Duke Energy, North Carolina, 2006: 58/42;[73]

4. Kansas City Power and Light, Kansas, 1991: 50/50;[74]

5. Louisville Gas & Electric, Kentucky, 1997: 50/50;[75]

6. Illinois American Water Company, Illinois, 2001: 50/50;[76]

7. Connecticut Natural Gas Corporation, Connecticut, 2001: 50/50;[77]

8. National Grid and KeySpan, New York, 2006: 50/50;[78]

9. Niagara Mohawk, New York, 2007: 50/50;[79]

10. KeySpan, New Hampshire, 2007: 50/50;[80]

11. Massachusetts Electric Company, Massachusetts: 2000: 50/50;[81]

12. Central Maine Power Company and Iberdrola, Maine, 2008: 50/50;[82]

13. PPL Corporation, Kentucky, 2010: 50/50;[83] and

14. New England Gas, Rhode Island, 2003: 50/50.[84]

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[72] *In re PSI Energy, Inc.*, Case No. 42873 (Ind. Util. Reg. Comm'n. Mar. 15, 2006) 2006 WL 1465924, at *260.

[73] *In Re Duke Energy Corp.*, Docket No. E-7, Sub 795 (NC Util. Comm'n. Mar. 24, 2006) 2006 WL 1559336, at *14 (42% of merger savings to customers).

[74] *Re Kansas City Power & Light Co.*, 1991 WL 501661, at **232-33, 242.

[75] *In Re Louisville Gas and Elec. Co.*, 1997 WL 740643, at *482.

[76] *In re Illinois-American Water Co.*, 2001 WL 946389, at **266, 289.

[77] *Re Connecticut Natural Gas Corp.*, 2001 WL 873007 at *42 (savings were flowed through to customers via purchased gas adjustment clause and shared with the company on a 50/50 basis).

[78] *In re National Grid PLC*, Case 06-M-0878 (NY State Dept. Pub. Serv. Sep. 17, 2007) 2007 WL 2710171, at **33, 36 (rate freeze for 5 yrs; 50% of net merger savings reflected as adjustment to revenue requirement; earning between 10.5% - 12.5% will be shared 50/50; between 12.5% - 13.5% will be shared 65/35 in favor of customer; and ROE above 13.5% will go to customers).

[79] *In re Niagara Mohawk Holdings, Inc.*, Case No. 01-M-0075 (NY St. Pub. Serv. Comm'n. Dec 3. 2001) 2001 WL 1772231, also *available at* http://www.dps.ny.gov/New_Search.html (last visited Apr. 13, 2012) at 6 (earnings over 11.75 ROE shared 50% with customers with declining percentages for excess earnings over higher ROEs in later plan years).

[80] *In re National Grid, PLC,* Docket No. DG 06-107 (N.H. Pub. Util. Comm'n. Jul.12, 2007) 2007 WL 2415854, at *35 (ratepayers will benefit from anticipated merger savings and EnergyNorth would share in proven merger savings, as ratepayers receive 50 percent of anticipated net merger savings soon after the merger is consummated and EnergyNorth stockholders share in 50 percent of proven net merger savings through a one time rate adjustment at a later date).

[81] *In re Massachusetts Electric Company*, Docket No. DTE 99-47 (Mass. Dept. of Telecomm and Energy, Mar. 14, 2000) 2000 WL 554931, at *24 (100 percent of the after-tax gained efficiencies up to $43 million, plus 50 percent of the after-tax gained efficiencies in excess of $43 million, or $66 million, as merger-related costs in its cost of service for setting distribution rates).

[82] *In re Central Maine Power Co.*, 2008 WL 704190, at *7 (50% of merger savings above an approved ROE bandwidth to be imputed as an O&M expense).

[83] *In re Joint Application of PPL Corp.*, Case No. 2010-00204 (Ky. Pub. Serv. Comm'n, Sep. 30, 2010) 2010 WL 3862870, at *302 (50% of revenue requirement equivalent of earnings in excess of 10.75 ROE deferred as a regulatory liability to be returned to customers via an annual amortization).

[84] *In re New England Gas Co.*, Docket No. 3401 (R.I. Pub. Util. Comm'n. Feb. 28, 2003) 2003 WL 1563686, at **410, 425 (50/50 split for three years followed by modified sharing if ROEs are higher in later years).

There have been relatively few cases in other jurisdictions, on the other hand, that have assigned most or all savings to customers.[85]

In connection with evaluating the Petitioners' proposed savings allocation, it would be inappropriate to take into consideration so-called double leverage, by assuming some undefined benefit associated with financing the acquisition and merger in part through debt. The ring-fencing provisions, as agreed in the DPS MOU, will both put at risk, as equity, the full investment by Gaz Métro, and will protect GMP customers from risks associated with parent operations. Accordingly, it would be inappropriate to reflect for ratemaking purposes any alleged benefit associated with double leverage.[86] The double leverage approach has been explicitly rejected by numerous state utility commissions in rate proceedings,[87] which have the same purpose and effect as the determination in this case of the appropriate sharing of savings in future rates, resulting in a partial determination of future rates.

It is also noteworthy that the Board has never adopted a double leverage approach for ratemaking purposes.[88] Nor did the Board consider double leverage as a factor in addressing shared savings in the merger decisions reviewed above. For these reasons, the Board should analyze the proposal to share savings between GMP and its customers without reference to double leverage analysis.

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85 *See, e.g., In re Exelon Corp.*, Case No. 9271 (Md. Pub. Serv. Comm'n, Feb. 17, 2012) 2012 WL 833884 (Slip Opinion) at 90 (Maryland law requires utility merger benefits to be "tangible"; immediate $43.5 million company saving contribution to Customer Investment Fund plus other long and short term contributions as a result of settlement agreement exceed company estimate of short term synergy savings estimate); *In re AGL Resources, Inc.*, Docket No. 11-0046 (Ill. Comm. Comm'n, Dec. 7, 2011) 2011 WL 6157371, at **23-24 (Stipulation settling the case provides that 100% of merger savings flow to customers); *In re Illinois Power Co.*, Docket No. 04-0294 (Ill. Comm. Comm'n, Sept. 22, 2004) 2004 WL 2208508, at **20-21 (memorandum of agreement establishes level of synergy savings with liquidated damages for failure to achieve; all savings flow to ratepayers); *In re Central Illinois Light Co.*, Docket No. 02-0428 (Ill. Comm. Comm'n, Dec. 4, 2002), 2002 WL 32702436 (Slip Opinion) at 39 (following stock purchase, CILCO to remain an independent company and modest synergy savings from enhanced purchasing power will flow 100% to customers).

86 Hevert reb. pf. at 28.

87 Hevert reb. pf. at 27-28.

88 *See In re New England Telephone*, Docket No. 4751 (Vt. Pub. Serv. Bd. Aug. 11, 1983) at 47-48 (use of double leverage in capital structure could distort investor perceptions of riskiness); *In re Vermont Gas Systems*, Docket No. 5516 (Vt. Pub. Serv. Bd. Feb. 14, 1992) (Board reluctant to apply double leverage analysis to Vermont operating subsidiaries of out-of-state corporate parents); *Tariff Filing of Continental Telephone Co.*, Docket Nos. 4997/5048 (Vt. Pub. Serv. Bd. Dec. 9, 1985) at 20 (reject double leverage adjustment as unnecessary).

2. The Percentage Sharing and Fixed Credit Mechanisms Are Also Supported by Precedent

Other jurisdictions have also adopted a non-fuel O&M-based sharing approach similar to the Petitioners' proposal for years 4-8. These include:

1. Great Plains and Aquila, Missouri, 2008 (nonmerger proxy based on nonfuel O&M costs, inflated at CPI-U);[89]
2. Ameren and Illinois Power Company, Illinois, 2004 (nonmerger proxy based on nonfuel O&M costs; Illinois Power agreed to specific O&M benchmarks and quarterly regulatory updates on milestone achievement success);[90]
3. Atmos and Mississippi Valley Gas Co., Mississippi, 2002 (nonmerger proxy based on O&M costs, inflated by 5.9% annual inflator);[91]
4. Entergy and Gulf States, Louisiana, 1993 (nonmerger proxy based on non-fuel O&M costs, inflated by CPI plus one half of growth in sales);[92] and
5. Entergy and Gulf States, Texas, 1993 (nonmerger proxy based on non-fuel O&M costs, inflated by CPI-U).[93]

Similarly, sharing savings by means of a rate freeze or fixed credit has also been approved by other commissions. These include:

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[89] *In re Great Plains Energy Inc.*, Docket No. EM-2007-0374 (Mo. Pub. Serv. Comm'n, Jul. 11, 2008) 2008 WL 2648913, at *34 (baseline selected for calculating the savings was Aquila's 2006 non-fuel O&M expense). Use of the CPI is reasonable because about one-half of the typical utility's non-fuel O&M expenses are labor-related. *Id.* at *42.

[90] *In re Illinois Power Co.*, 2004 WL 2208508, at **24-25 (Staff accepted applicants' estimate of at least $33 million of non-fuel O&M savings; Memorandum of Agreement provides for liquidated damages if savings milestones not achieved. In next electric rate case and gas rate case, will allocate savings amounts on a basis consistent with the underlying O&M expenses to which they relate.).

[91] *In re Atmos Energy Corp.*, Docket No. 01-UA-0843 (Miss. Pub. Util. Comm'n, October 31, 2002) at 3, *available at* http://www.psc.state.ms.us/ (last visited Apr. 14, 2012) (O&M benchmark based on 3/31/2002 rate filing, benchmark adjusted at 5.9% annually for five years. O&M savings are the amount by which O&M actuals are below the benchmark. Atmos will defer any allowed integration and O&M costs in excess of the benchmark for recovery out of future O&M savings.)

[92] *In re Entergy Corp.* 1993 WL 651433 at *53, Appendix 1 (approved sharing mechanism delivers approximately 60% of non-fuel O&M merger savings to shareholders.)

[93] *Re Entergy and Gulf States Utilities Co.*, Docket No. 11292 (Tx. Pub. Util. Comm'n, Dec. 29, 1993; Order on Reh'g, March 24, 1994; Second Order on Reh'g, July 1, 1994) 1993 Tex. PUC LEXIS 208, at *81 (companion regulatory plan caps GSU's rates for five years, requires the flow through of all fuel-cost savings resulting from the merger to ratepayers, and would add 50% of non-fuel synergy savings to the cost of service in GSU's next rate case). The baseline is divided into two components: (1) BYA-G, non-fuel "generation" O&M ($ 151,925,000) and (2) BYA-O, "all other" non-fuel O&M ($ 215,100,000) expenses. The two components are then separately indexed. *Id.* at **80-81.

1. First Energy and Allegheny, Maryland, 2011;[94]

2. Dominion Peoples, Pennsylvania, 2009; and[95]

3. Narragansett Electric Company, Rhode Island, 2000.[96]

Based on this review, the Petitioners' proposed savings sharing mechanisms are supported by precedent.

3. The Term of the Savings Sharing Plan is Consistent with Precedent

Petitioners propose to share integration savings over eight years and guarantee a minimum amount of customer savings over a ten year term. These proposals are consistent with the length of the savings sharing period adopted in other states. The following decisions adopted a saving sharing timeframe similar to that proposed by the Petitioners:

1. National Grid and Granite State, New Hampshire, 2007: 10 years;[97]

2. Niagara Mohawk and National Grid; New York, 2001: approximately 10 years;[98]

3. Entergy and Gulf States, Louisiana, 1993: 8 years;[99] and

4. New England Gas, Rhode Island, 2003; 8 years.[100]

As a result, the time frame of Petitioners savings sharing plan is appropriate.

Chairman Volz asked the Petitioners to address whether, in order to implement the savings sharing plan, GMP must be subject to an alternative regulation plan for the duration of

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94 *In re FirstEnergy Corp.*, Docket No. 9233 (Md. Pub. Serv. Comm'n. Jan 18, 2011) 2011 WL 722020, at *288 (company paid up-front rate credit, which combined with other cost forbearances, reflected half of the projected merger savings over the five years following the merger).

95 *Re Peoples Natural Gas Co., dba Dominion Peoples*, Docket A-2008-2063737 (Pa. Pub. Util. Comm'n. Nov. 19, 2009) 2009 WL 4087058, at *7 (Petitioners ordered to deposit $35 million into a trust on the closing day of the merger to be distributed to customers monthly via a rate credit for approximately 3 years beginning with the next rate case).

96 In *Re Narragansett Elec. Co.*, Docket No. 2930 (R.I. Pub. Util. Comm'n, Mar. 24, 2000), 2000 WL 779757, at *115 (Rhode Island Commission approved a "settlement credit" to be applied to customers' bills on a per-kilowatt hour basis, which accounted for about a third of the savings returned to customers).

97 *In re National Grid PLC*, 2007 WL 2415854, at *26

98 *In re Niagara Mohawk Holdings, Inc.*, Docket No. 01-M-0075 (NY St. Pub. Serv. Comm'n, Dec 3. 2001) 2001 WL 1772231 (Slip Copy), also *available at* http://www.dps.ny.gov/New_Search.html (last visited Apr. 13, 2012) at 44 (The New York Public Service Commission approved a joint proposal contemplating a post-merger rate plan with a term of slightly less than ten years; plan's long term needed to realize savings in which ratepayers will share immediately; plan strikes a good balance between keeping rates stable and allowing the flexibility needed to respond to changing circumstances).

99 *In re Entergy Corp.*, 1993 WL 651433 at **4, 53, Appendix 1.

100 *In re New England Gas Co.*, 2003 WL 1563686, at *413. The Rhode Island Public Utilities Chairman noted in a concurring opinion that he approved of the eight-year savings plan, noting that a shorter time period might force the utility to engage in workforce reductions. *Id.* at *427.

the savings sharing plan.[101] Because the savings sharing plan is fully consistent with traditional ratemaking, the plan can be implemented without the need for alternative regulation. As demonstrated above, for instance, the Board has permitted above-cost rates, such as the Base O&M Costs associated with the savings sharing plan, outside of the context of alternative ratemaking, where necessary to achieve its public policy goals.[102]

The flow-through of savings in years 4-8, based on the difference between Base O&M Costs and actual (i.e., updated) O&M costs could be accomplished without alternative regulation and does not constitute selective updating. Selective updating involves updating one cost factor alone, without giving attention to whether the cost factor requires adjustment (due to transitory or abnormal factors) or whether there are related, concurrent cost or revenue changes.[103] These concerns are not present where the adjustment is relatively contemporaneous with an annual general rate adjustment[104] (which would involve a review of all costs) and where the adjustment relates only to review of O&M costs on a regularly-scheduled basis (thereby avoiding the potential that the cost changes are transitory or abnormal). The flow-through of savings in years 4-8 also does not constitute prohibited retroactive ratemaking, which involves the setting of a rate surcharge to permit the utility to recover past losses or a refund to return past excess profits, under a rate that resulted in an actual return that varied from the authorized return.[105]

The prohibition against retroactive ratemaking does not preclude the annual flow through of savings for two reasons. First, because the adjustment by definition results in a rate reduction rather than a rate increase, it does not require current consumers to pay for past deficits or reduce GMP's incentive to be efficient due to guaranteed earnings. Second, the expenses associated with the savings sharing adjustment are extraordinary and therefore are subject to the retroactive ratemaking exception, because they relate to a proposed merger of the two largest electric distribution utilities in Vermont that is virtually unprecedented. Finally, the public interest

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101 Tr. 3/22/12 at 129 (Volz).

102 The requirements of the fixed rate credit and the $144 million guaranteed savings, which also represent a variation from cost-based rates, reflect obligations imposed on GMP that only benefit customers. These provisions are enforceable based on GMP's agreement to implement them and therefore do not depend on alternative ratemaking to be enforceable.

103 *In re Consol. Rate Appeals of Green Mountain Power Corp.*, 142 Vt. 373, 384 (1983).

104 Even without alternative regulation, GMP could file annual base rate adjustments similar to the base rate adjustments under the alternative regulation plan.

105 *In re Central Vermont Public Service Corp.*, 144 Vt. 46, 52 (1984).

strongly favors continuation of alternative regulation in order to avoid GMP's retention of 100% of the savings.[106]

IV. THE PETITIONERS' PROPOSED VELCO-RELATED CONDITIONS SHOULD BE APPROVED

Petitioners and the Department propose three merger conditions to address post-merger GMP control of VELCO and Vermont Transco LLC ("Transco"). First, they propose a condition requiring the transfer to VLITE of 38% of the total of VELCO Class B voting common stock[107] and 31.7% of the total of VELCO Class C non-voting common stock.[108] The transfer will reduce the combined CVPS and GMP Class B voting common stock from 78% of the total to approximately 40%.[109] Second, Petitioners and the DPS propose a condition requiring that the Petitioners take all actions necessary to assure that the Petitioners cannot unilaterally remove VELCO as the managing member of Transco or amend Section 9.3 of the Transco Operating Agreement.[110] The third proposed condition would provide that neither CVPS nor GMP will increase its ownership share of VELCO in any amount or take steps that would result in a dilution of the percentage ownership of VELCO by VLITE without Board approval.[111]

These proposed conditions are adequate to assure that GMP cannot exercise majority control over VELCO. No party offered evidence to the contrary. The Petitioners and the Department's proposed conditions accordingly represent the most effective way to assure that

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106 In connection with another issue, Ms. Tierney requested examples of rate design proceedings that were not based on immediately preceding revenue requirements determinations. Tr. 3/22/12 at 200 (Tierney). The following cases approved revised rate designs without indicating that they were addressing a recently-approved change in revenue requirements or otherwise referencing a Board-approved cost of service. *Re Green Mountain Power Corporation*, Docket No. 5744 (Vt. Pub. Serv. Bd. Dec. 2, 1994); *Re Vill. of Morrisville Water & Light Dep't.*, Docket No. 5348 (Vt. Pub. Serv. Bd. Dec. 20, 1990); *Tariff Filing of Central Vermont Public Service Corp.*, Docket No. 5294 (Vt. Pub. Serv. Bd. April 4, 1990); *Tariff Filing of Washington Electric Coop., Inc.*, Docket No. 5309 (Vt. Pub. Serv. Bd. Jan. 13, 1989); *Board Investigation in re: Dep't of Public Service's Petition*, Docket No. 5670 (Vt. Pub. Serv. Bd. Oct. 21, 1994).

Chairman Volz asked whether GMP agreed to waive the seven-month deadline under 30 V.S.A. § 227(a), in connection with its obligation in DPS MOU ¶ 32 to complete the rate design case in nine months. Tr. 4/4/12 at 34-35 (Volz). GMP hereby waives any entitlement to the seven-month deadline.

107 This requirement, contained in the DPS MOU, reflects a 5% increase from the Petitioners' initial proposal to transfer 33% of the Class B voting common stock. Powell-Reilly reb. pf. at 14 (Powell); exh. Petitioners-DPS-1 ¶ 7.

108 As required by the DPS MOU, the Petitioners will use their best efforts to obtain a waiver from other VELCO owners of their right of first refusal. Exh. Petitioners-DPS-1 ¶ 10.

109 Powell-Reilly pf. at 20 (Joint).

110 Exh. Petitioners-DPS-1 ¶ 13.

111 *Id.* ¶ 14.

GMP does not exercise majority control of VELCO. The Board should therefore approve the proposed conditions in the DPS MOU.[112]

Other potential mechanisms for addressing GMP control, on the other hand, are inappropriate and should be rejected. For instance, a requirement that the VELCO stock be offered to other VELCO owners on a *pro rata* basis would not assure that GMP would not exercise majority control, if at least 74% of the offered stock were not acquired by other owners.[113] If Vermont Electric Cooperative Inc. ("VEC") or the Burlington Electric Department ("BED") acquired their pro rata share of the 38% interest, on the other hand, their resulting ownership share would exceed the 10% threshold for Board approval under 30 V.S.A. § 107.[114] This would require a new proceeding that would delay the acquisition closing.[115] Elimination of the voting rights from 38% of GMP's post-merger shares arguably would have the same result, because the portion of total voting shares controlled by VEC and BED would "float up" by an equivalent amount.[116] More fundamentally, *pro rata* transfer of shares or elimination of voting rights would concentrate majority control in the other VELCO owners, instead of Petitioners' proposal for a distribution of ownership among the Petitioners, other VELCO owners, and VLITE, none of whom would exercise majority control.

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[112] The DPS MOU contains a number of other provisions. These include (1) the requirement that the Petitioners elect the initial VLITE directors designated by the Department, (2) the requirement that GMP, CVPS, and VLITE enter into a voting agreement providing for the designation of VELCO directors, and (3) the requirement that GMP support VELCO bylaws amendments to formalize the process of nominating and electing VELCO directors and allow Transco owners to participate in the VELCO Operating Committee. Exh. Petitioners-DPS-1 ¶¶ 8, 11-12. These obligations relate to detailed governance matters and, unlike other DPS MOU provisions (including windfall sharing, rate setting, and VELCO share transfer obligations) can be implemented without the need for Board action. All DPS MOU provisions are enforceable by the DPS MOU parties and any disputes must be resolved by the Board. Exh. Petitioners-DPS-1 ¶ 38.

[113] GMP would retain majority control if its ownership were reduced by less than 28% (*i.e.,* 78% less 28% equals 50%), which represents 74% of the 38% interest that will be transferred.

[114] VEC and BED own 8% and 6% respectively of VELCO and represent 36% and 27% respectively of the ownership interests other than CVPS and GMP. All ownership interests other than CVPS and GMP total 22% of VELCO shares. Powell-Reilly pf. at 20-21. If BED acquired its *pro rata* share of the 38% interest to be transferred by CVPS, BED's ownership interest in VELCO would increase to 16% (6% + (6/22 x38%).

[115] This would also require amendment of the FERC approval of the acquisition and merger, which was based on a transfer of VELCO shares to VLITE. *Order Authorizing Acquisition And Merger And Disposition Of Jurisdictional Facilities*, Docket No. EC11-117-000, (FERC. Mar. 6, 2012) 138 FERC ¶ 61,161 ("FERC March 6, 2012 Order"); *see* tr. 3/28/12 at 66-67 (Dutton).

[116] Section 107 defines control by reference to securities entitling the owner "to vote in the direction or management of the affairs of the company." 30 V.S.A. § 107(e)(2).

V. CONCLUSION

For all the above reasons and for the reasons contained in Petitioners' Proposed Decision, the acquisition of CVPS by NNEEC, the merger of GMP and CVPS, the acquisition by VLITE of a controlling interest in VELCO, the savings sharing provisions of the DPS MOU, and the other transactions described in the Amended Petition promote the general good of the state, will not impair competition, and should be approved.

Dated this 23rd day of April, 2012.

GREEN MOUNTAIN POWER CORPORATION, DANAUS VERMONT CORP., GAZ MÉTRO LIMITED PARTNERSHIP, GAZ MÉTRO INC., NORTHERN NEW ENGLAND ENERGY CORPORATION, for itself and as agent for Gaz Métro Limited Partnership's parents, and VERMONT LOW INCOME TRUST FOR ELECTRICITY, INC.

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