

SECOND TAXING DISTRICT COMMISSIONERS
Special Meeting
June 28, 2011

Present:	Mary E. Burgess Al Ayme Maria Borges-Lopez Mary Geake Mary Mann	Chairperson Vice Chairperson
Also Present:	John M. Hiscock Gwendolyn Gonzalez Kevin Barber	General Manager Asst. District Clerk
Absent:	Sherelle Harris Cesar Ramirez	
Public Present:	Mayhew Seavey	

Call To Order

Chairperson Mary E. Burgess called the Special Meeting of the Second Taxing District Commissioners to order at 7:00 p.m. on Tuesday, June 28, 2011. The meeting was held at South Norwalk Electric and Water, One State Street, South Norwalk, Connecticut.

Acceptance of the Minutes

Commissioner Burgess: "I will call this Special Meeting of the District Commissioners, Tuesday, June 28th, 2011 to order. I need a motion for acceptance of the minutes of April 26, 2011."

Commissioner Ayme: "So moved."

Commissioner Borges-Lopez: "Second."

Commissioner Burgess: "All in favor?"

Commissioners simultaneously: "Aye."

Commissioner Burgess: "Abstentions?"

[No Abstentions]

Commissioner Burgess: "Okay, the next thing on the agenda is the Electric Rate Study Discussion. John."

REGULAR AGENDA:

Mr. Hiscock: "Tonight we're going to be talking about cost of service, rate analysis for the electric department group. I think you are all aware we had multiple discussions. We hired a rate consultant. We haven't changed our basic rate design since the 90's. I mentioned to you quite a few times. It's been antiquated and needs to be dealt with. So we hired a well known and very capable rate consultant to look at our information and do some analysis and work with us on coming up with a modern rate design. The purpose of this evening is so that the commission understands what we go through when we design rates, what the principals are, what the process is and then what the options are and to try to get some feedback from the commission about the options which we should consider further, because there are many ways that you can go about doing this. There are many ways to come up with rate design. So, at this point I would introduce Mayhew Seavey and you might as well all come up to the table since we don't have public....or just a little closer."

Mr. Mayhew: "Yes, yes."

Mr. Hiscock: "PLM Electric Power Engineering. We start down that end - Commissioner Chairman Burgess, Vice Chairman Ayme, Commissioner Mann, Commissioner Borges-Lopez, and Commissioner Geake."

Mr. Mayhew: "Good Evening."

Simultaneously: "Good Evening."

Mr. Mayhew: "I'm going to try to get this done in less than an hour and a half and without putting any body to sleep. There is quite a bit of material to cover and although all the agenda said questions at the end, if you have questions at any point, just ask, because this is a lot of material and it's really technical in nature. So, I'll try to, I'll try to make it as understandable as possible."

Mr. Hiscock: "Yes."

Mr. Mayhew: "We're going to start. I'm going to start off by just talking about the general principal of how we design electric rates. Electric rates are the price that you sell your products to the public at. And like any business, setting the price is an important business decision. What's the basis for setting that price, then when we start out, if you look at page 4, there are basically 5 objectives that we have in designing rates. We want the rates to be adequate, we want them to be fair, we want them to be competitive, we like them to be stable and we like them to be clear. Now, what do we mean by those things? Well, adequacy means that the rates have to be the, we collect enough revenue to cover your operating expenses and provide a little bit more to cover renewals and expansions of the plan and in order to continue to be able to provide reliable service. The way we measure the adequacy of rates is the overall, what we call the overall rate of return that the rates produce. And we express that as a percentage and so it's a percent of that the figured net income revenues minus expenses. What that net income represents as a percentage of the total plant that you have installed, the value of your plants of all pole wires, buildings, etc., so, the overall rate of return. The Connecticut Statutes says that, that should be between 5 and 8% so that's the kind of ball park figure you have to work with in terms of designing rates. When we talk about fairness, what we say is that the rate paid by each class of customer should reflect the cost of providing service to that class of customer. It costs you more to provide service to a house then using a small amount of electricity, and tend to use electricity when it's most expensive, than it does to provide

electricity to a large industrial customer or a supermarket or somebody that uses a large amount of electricity or tends to use over it time, constantly over time. So we try to reflect that in a price that we charge our customers. And so we calculate the rate of return, not only for the utility as a whole, but for each class of customers individually. And you want those rates of return to be relatively uniform but there are variations that we'll talk about. We also would like your rates to be competitive. That is that customers paying, your customers should pay a rate that's comparable to or competitive with the rates that they would pay if they were the customer of competitor utility, in this case Connecticut Light and Power as being your geographic, geographically immediate competitor. And we looked at, when we do that we put together a typical bill comparisons that show for different level of usage, how your rates compare to the rates of competitors. That's one of the measures that we use when we look at whether the rates are fair. We would like to have rates that are stable, that is, that the average cost of electricity paid by customers shouldn't fluctuate too much from month to month. Now, we know that customers bills tend to go up in the summer time and down in the Spring and Fall and customers sometimes have trouble understanding that, but you would like that, that there aren't big fluctuations from month to month in the average process that customers pay. And so you try to design rates better that are stable and finally you want the rate and particularly the bill to be understandable by the customer. You don't want it to be so complicated that the customer has no idea what they are paying for and how much they are paying. So, the test for that is if you know when you see it. And if you've seen it, if you've seen the typical investor owned utility bill then you'll know that's not clarity but those that are the joys of the deregulations of the 21st century and hopefully you can continue to be better than that. Now the way we, the way we start to measure the cost of service is to allocate the cost, your cost of doing business to each of the different classes of customers. We allocate the expenses to different class and when we talk about classes basically you have I think 7 classes of customers. And in reality there are probably only 4 and within, there are some fine distinctions between some of them. You have residential and then you have small medium and large non residential customers. So you have small businesses, you have your medium size businesses and then there is large commercial which are broken out now into different rate categories on the basis of what voltage they get delivery at and whether or not they own a transformer. And hopefully part of our profits here will be simplifying that a little bit so that there will be only one rate with only a few bells and whistles. So, when we allocate cost and what that means is that, let's say you paid 11 million dollars for purchase power. You needed to know how much of that 11 million dollars is attributable to the residential customers, how much its attributable to the small business, etc. So that's what we mean by allocation. We take each type of expense that you have and we attribute that expense to customers on the basis of how the customers are causing that expense. And there are 3 basic categories of expense, they're customer based expenses. They are what we call demand based expenses and there are energy based expenses. Customer cost are costs that you incur that are related to just generating a bill and sending out. So they are related to the cost of metering, the cost of producing a bill and also that the expense associated with carrying the plant that you, the facilities that are used so that the service lines to the house to the meters, all those are really functions of how many customers and has nothing to do with how much electricity customers use. It costs you a certain amount of money to send out a bill whether or not that customer uses any electricity or not. So those are what we call customer related expenses and most of your customers account expenses, metering and billing and etc. The second overall category are all about demand, cost, demand related cost and those are the costs that are related to the maximum rate at which the customer uses electricity so that a large industrial customer might use 1000 kilowatt in an hour at the most. And so because of that you have to have transformers that will be able to provide that. You have to have wires that will be able to do that and so a lot of the equipments that you have, the size of that equipment is based on how what the maximum rate is that the customer uses electricity. Even if the customer uses only

that 1000 kilowatt for 3 hours a month you still have to have a transformer there to do that. So, those are demands related costs and so we allocate those costs on the basis of the demand that the customer is putting on those facilities. And the last one is just energy and energy is not the same as demand. Energy is the kilowatt hour of what flows through the filament of light bulbs or what the turns the motors, what you pay for when you pay. When you get your residential bill you're paying so many cents per kilowatt hour and that's an energy charge and the energy related costs are basically your purchase power costs. Anything that you pay for the electricity that buy wholesale and you sell it to customers most of those costs are energy related costs and so you just spread those across customers based on what number of kilowatt hours that they use. So, we take all that information and we perform what's called Fully Allocated Cost of Service Study and we take your, for the initial cost of service study we call it historic test year. We take a full year of actual, actual data from your financial records from your billing records and we allocate the expenses to your customer classes and we calculate the revenues that the rates would generate by applying your retail rate to the number or kilowatt hours that you sold and we compare the revenues that are produced by the rates to the expenses that we've allocated. So, if you had, if your residential rates produced 5 million dollars in revenues and we've allocated 6 million dollars in expenses, then you lost a million dollars selling kilowatt hours to the residential customers. And so we calculate the rate of return that way. We also perform a, once we've essentially used a historic test year to, two reasons, (1) we want to see how the rates are performing. Are some of our customer classes paying more than their fair share, are you overall losing money, are some of the classes losing money and some of them making more money than they should. And we also use it to calibrate the model. We want to make sure that we can calculate using the computer model how much revenue you're actually collecting from each class of customers because we're going to use the same model to predicate the revenues that our new rates that we're going to propose. So it's important to know that the model is capable of calculating revenues that are produced by the rates. When we then turn to designing rates we looked at a future year. In this case, we're looking at fiscal 2012 so we're going to predict what the performance of the rates will be compared to your budgeted expenses for the fiscal 2012. We want to develop some rate designs that will produce adequate revenues and that will also send correct price signals to the customers. There are three main objectives we would like that we have to balance the designing rates. You would like the rates to be fair. That is you would like every rate to produce exactly the same rate of return. You would like your rates all to be equally competitive, either you know, all 10% below Connecticut Light and Power rates or all 10% above. They are all uniformly competitive and if you're having the increase or decrease rates you'll like all the customers to be impacted about the same. You can't do all three of those things, because in reality you're going to have to choose which objectives you want to meet and how you're going to meet them. Once you set the objectives your goals for what the rates are whether there's going to be, whether you're going to have a 10% increase across the board, whether you're going to have more of an increase for some customers. You then need to develop a specific rate design and what we like to do is develop an unbundled rate. The current rates are all bundled rates. You have a meter charge, an energy charge, a demand charge and a purchase power charge. And what we like to move towards in slide 19 is unbundled rates. You'd like to have a separate charge for meter charge, which is what we currently call customer charge. We would like to have a distribution charge which isn't going to get energy for kilowatt hour charge for residential small business customers and a demand for large customers. And then you have a purchase power charge and each of them reflects a different cost only. The meter charge is how you recover the cost of the meter and billing customer service from time [inaudible] cost earlier and you'll like to have a rate that charges as close to the cost as actually doing as as possible. The reason that you want to do that is because otherwise, and one of the things you always try to avoid is having one group of customers subsidizing another group of customers. If it costs you \$10 to send out a bill and you're only

charging \$5 meter charge, then customers who aren't using very much electricity are essentially getting a free ride. They are not paying the full cost of the bill. So, you like to have that full cost being reflected in the rate. And always in setting a price you want to be sending the right price signal to customers. That's the main part in economics theory and it's also important overall, because the customers are making decisions about using more or less electricity. If you're charging them, if that next kilowatt hour that they are buying from you costs, is costing them less than is costing you to provide, then you're losing money on that extra kilowatt, on that next kilowatt hour, so you want to try to set the rate to actually reflect the cost of delivering the electricity, otherwise you can get into trouble. The distribution charge is the second part of the unbundled rates is a charge that basically recovers your cost of running the utilities. In the business sense your distribution company you buy power at wholesale. You distribute it across your wires. You sell as retail to the customer. The cost of running the electric utility, the poles operating and maintaining the poles and wires, substations, and transformers, reading meters, setting up bills, that's your cost of doing business and that's what we like to recover through the distribution charge. And the reason you want to unbundle that in addition to the fact is just is good to know what that cost is. It's essentially the private utilities, the investor utilities have been billing their customers since the beginning of deregulation and you might then be able to compare Connecticut Light and Power bill to your bill and say 'hmm, were only paying 3 cents for distribution and Connecticut Light and Power is 4 cents'. That tells the customers how good a job you're doing at running a distribution company. That's your, that's the thing you could do something about. The price of electricity wholesale, you know, the market force could determine that to a large degree and to some degree your power supplier can do something but there is very little you can do about that. But you can manage the cost of running the utility and if you don't have a clear, if the customer doesn't have a clear number to look at they don't know how, you know, there is no way to compare how good a job you're doing there. And in addition, the distribution charge is where you earn, basically where you earn your income. You need to be able to earn enough money and the distribution charge to produce your net income. The way we unbundle it is to get all the purchase power costs out of the base rate and put it into a separate generation charge or the purchase power charge. It makes, it's good from accounting standpoint because you're now charging for purchase power separately from providing distribution service and it does mean that you, that you occasionally have to continue to monitor the performance of your distribution rates because if you start to lose money you will have to adjust those rates and you have to then have to do another rate study or study [inaudible] new rates. You can't just adjust your purchase power charge anymore and it means your bottom line. And the final element of the unbundled rate design is the purchase power charge. And that's just a pass through of all your purchase power cost and you can set that up as a formula rate and adjust it monthly, quarterly, annually however you want to do that. Annually is better for the customers because it's a little much more stable price and so if you can manage that its always good to have a stable purchase power charge and its better, it points out there that you want to have the purchase power charge vary and that's actually a good thing. And its something that you miss out in a conventional purchase power adjustment because it does actually cost you less to provide purchase power to those already large industrial customers. And if you can, if you can break that charge out in your demand charges and your energy charges once again you're not having one group of customers subsidizing another. So that's the end of part one. Any questions so far?"

Commissioner Ayme: "In the beginning when you said between 5 and 8%, that's the, how much we can charge above the cost or are you talking about the increase."

Mr. Seavey: "That's how much you can earn over and above expenses."

Commissioner Ayme: "Over and above expenses. Okay, alright."

Mr. Seavey: "It's not an increase."

Commissioner Ayme: "Is there a limit on the increase?"

Mr. Hiscock: "No."

Commissioner Ayme: "No limit on the increase."

Mr. Hiscock: "And that 5 to 8% is a number that sat. It had been in the Connecticut Statutes for virtually forever."

Commissioner Ayme: "Forever."

Mr. Hiscock: "It's something that no one has really ever addressed in recent time, nobody. You know it's just one of those things we had all accepted. So it is a starting point."

Mr. Seavey: "It isn't enforced in any way, is it?"

Mr. Hiscock: "No. Connecticut, I'm not aware of any point where anybody has ever enforced it."

Commissioner Ayme: "So going [inaudible] would not be a violation. Would it?"

Mr. Hiscock: "It probably, if from the strictest stance, if you read the statutes, yes, a violation of the statute that allows municipal electric companies to exist."

Commissioner Ayme: "Would they enforce it?"

Mr. Hiscock: "It's one of the reasons you're not rate regulated by the DPUC."

Commissioner Ayme: "Oh, I see."

Mr. Hiscock: "There's some basis, but as I say, I mean, all of this is ancient and Connecticut doesn't have a, first of all there are only 6 munies in the state, so Connecticut just doesn't have a history of interfering with municipal rate structures. But that's what statute..."

Commissioner Ayme: "We're not aware of anytime that it has been enforced."

Mr. Hiscock: "No."

Commissioner Ayme: "No."

Mr. Hiscock: "No."

Commissioner Ayme: "In theory it would be a violation. Wouldn't it?"

Mr. Hiscock: "I think, that's something to think a little bit about. If we decided for some reason, we wanted 12% return, you might, you could conceivably run into a situation where a larger

customer might challenge you in court, saying that you're obtaining excessive returns. That's about the only place it would ever happen. This state is not going to step in."

Mr. Seavey: "They might be able to file a complaint with the DPUC and that would open an investigation. They might order something, but typically, if you did earn that level of return, I think you could probably even get around that by essentially an accounting change that would take the excess amount and put it into a reserve fund for rate stabilization purpose. There's nothing wrong about that, so, you can always address that without getting the DPUC involved."

Commissioner Ayme: "Okay."

Mr. Seavey: There is a tension between earning, earning a larger rate of return in increasing rates. Most municipal utilities try to set rates that really are designed to produce a level of income that they need to fund operations rather than try to max. It's not quite the same as business in a way to maximize your return."

Commissioner Burgess: "Any other commissioners have questions? No?"

Mr. Seavey: "Alright then I'm going to move on and talk about the results of the fiscal 2010 test year cost of service study. We started out with a very comprehensive set of accounting reports. Actual expenses and plant in service and billing data for South Norwalk which we fed into our cost of service computer model. The largest, the most difficult part of performing a cost allocation for the municipal utilities is the availability of good customer load shape data. If you're going to, if you visualize, what you're trying to do is to allocate costs to customers on the basis of how much electricity they are using during the hottest hour of the summer, for instance. You don't meter individual customer at that level of detail and so getting hold of good detail hourly consumption data is very difficult. We're fortunate in that with deregulation. The regulated utilities like CL&P have to, have to do very expensive detail metering and publish that information on their website. So we now have access to that data which could have cost a lot of money to generate years ago for the utility. So we use that CL&P's customer data to do this and I think that it really improved the accuracy of the results. So you know, thank you CL&P for this. We use the model to approve tested revenues to compare the revenues that the model calculated for fiscal 2010 and the models are able to calculate the revenues that were essentially exactly the same as the and within a 1/10 of a percent overall within three customer class 3/10 of a percent of what you actual booked for that period of time. So we have a good level of confidence that the customer service model will actually predict how much revenue new rates for this. Page 26 shows the results. This is about the results for 2010. And so I'll walk you through what it shows. Across the column heading you can see the 1,2,3,4,5,6,7 customer classes that we have broken out into residential, small general service, medium general service, municipal and then the three large classes, secondary with or without their own transformer and then the primary one here. The first line is the total revenues for the year, the fiscal year. The second line is the total expenses for the year and so revenues, revenues are actual and of course expenses are allocated expenses. So we've gone through all the expenses. And there may be a hundred different line items that each one is allocated to using the appropriate allocation factor and the difference is the net income or return. And so overall expenses were greater than revenues by about \$448,432 and that's 3% of the total by total plant in service the total gross plant at value, book value of all the poles and wires and transformers. That was a negative 3% rate of return for fiscal 2010 and the individual class rates of return are, of course this is where it gets interesting. The residential class has a negative 16.5 rate of return and in fact if you look at the net

income by class, all the other classes may earn money in fiscal 2010 and residential class lost money. So.”

Mr. Hiscock: “Let me interrupt you for a minute. And we talked a lot about how we set the rates up and what our targets have always been, and this sort of bares out that at least the targets as we talked about them over the years, are working. You know, you’ve indicated that we try to keep residential 30% below CL&P and the commercial is 10% below CL&P and this sort of bares out that we’ve done a reasonable job of doing that. Now, this is always what comes up when we deal with rate design. It’s just something for you to note that what we have talked about over the last couple of years is really very evident in this chart.”

Mr. Seavey: “And I would also hasten to add that this is not at all a typical for municipal utility cost of service. Typically, if we adjusted the overall rate of return up to 5%, if you just gave everybody uniform increase, you’ll still see a slightly negative rate of return on the residential, but what I typically see in municipal utility cost of service is a residential class that somewhere between zero and minus 5% and small commercial will be anywhere between 15 and 25%. That’s the class that tends to have the highest rates and then usually it goes down medium, will be around 10 to 12% rate and then the large customers are pretty much always at the overall average because your large customers are, you know, will typically be half of your usage and they can’t really be very far away from the overall average. So, the only thing that’s at all unusual that I see here is that the small and medium general service is kind of in reversed. In general, has a high rate of return and a small [inaudible]. But everything else is very typical for, I mean as for utility and nothing to be alarmed about. We all went through the use of the operating budget of the fiscal 2012 operating budget. And plug that into the model and the current rates and the power adjustment to predict what will happen in the next fiscal year there is no change in rate. Observations on page 28 about what changed between fiscal 2010 and fiscal 2012, kilowatt hour sales are higher by about 4% which represent about 2% a year which seems about right. Revenues, because of the increase sales and because there was an increase in the purchase power just half way through fiscal 2011, revenues are up by about \$900 thousand. Expenses are up by about \$2 million and that \$2 million is spread between purchase power cost, distribution costs, customer sales and administrative costs. So, the big increase there is, is in purchase power distribution, but as you expect, since revenues are increasingly less than expenses when we get to the bottom line, you have a situation that’s a little worse than last year and clearly some action needs to be taken. The overall of rate return dropped down to a negative 9% and the class relatively needs to be turned around. I also would add that all of these numbers are preliminary. We haven’t fine tuned them in any way and we’re presenting this for sort of general information because what we’re going to do next is to look at some of the options for addressing the rate changes. Any questions at this point?”

Commissioner Ayme: “Yes, I do through the chair. Page 29, this is a production right?”

Mr. Seavey: “Yes, it is based on the budget....”

Commissioner Ayme: “Based on performance. The other question I have is that, the comparisons made on page 26, this [inaudible] non-profit, not profit corporations? On page 26.”

Mr. Seavey: “On page 26. Yes.”

Commissioner Ayme: “This is all based on non-profits.”

Commissioner Mann: "No."

Mr. Hiscock: "This information comes of from our audit for fiscal year 2010."

Commissioner Ayme: "From our records."

Mr. Hiscock: "Right."

Commissioner Ayme: "All from our records."

Mr. Hiscock: "Yes, these are our numbers, our information, everything out of our audited last month's statement."

Commissioner Ayme: "Because you were talking about a comparison with CL&P."

Mr. Seavey: "Oh, right, yes, that was because some of the, not the operating data, but the load shape data was from CL&P and we had actually, we haven't compared to CL&P yet. We'll get to that. But I haven't looked at how we rate compared to CL&P rates."

Commissioner Ayme: "Oh okay, because my impression was that this was not from SNEW but from another corporation."

Mr. Seavey: "These are our figures."

Commissioner Ayme: "Our real figures."

Mr. Hiscock: "Our real numbers off the audit, yes."

Commissioner Ayme: "Oh, okay."

Mr. Seavey: "So, the 26 is actual and the 29 is forecast. Everything else between the two is comparable."

Commissioner Ayme: "Right, okay."

Mr. Seavey: "So, I'm going to present now five different scenarios. I'm looking at these in overall terms, not specific rate numbers, but what will, what would happen under different scenarios. So, the first scenario we're going to look at is the base case which is no change from the present rates. So if we don't make any changes we will have a situation where we have rates of return that vary between negative 22% for residential up to 9 % for medium and losing 1.4 million and most of your rates are significantly below CL&P. We look at 32. This is the format that we're going to present each of these scenarios. And what we have here is in the upper left hand corner there is a table that shows for each class the rate of return and the overall rate of return so the residential is negative 21.7%. The next two columns are going to show the change in revenues from a proposed rate change. And the last column shows how these rates compare to CL&P's rates. And then each of the 3 graphs show where the current rates and the proposed rate how they compare to CL&P, what the rate of return is, what the present rates and the proposed rates and then the rate of impact, in the lower right hand corner. Because these are the present rates there is no rate impact and there is no change between the present and proposed but you can see graphically for instance on the rate

of return graph, the negatives and the positives how some of the rate of the residential in particular have a negative rate of return and some of them are positive and also how, you know, some of them are significantly lower than CL&P's rates. So the first alternative scenario that we looked at is, what would happen to the rates if we decided that we wanted all the rates to have the same rate of return, they all have the same level of profit of return. So, we design these to produce an overall 5% rate of return, that means because their loss, some revenue gets lost in the street lighting rate which is giving lights, that each class has to produce 7 1/2% to make up for that and it's a revenue increase of about 14% and that's 2.2 million dollars on a class by class basis the residential rate would have to increase by 29%, the Medium General would decrease by 0.7%, the Municipal Class wouldn't change at all and the other, the large portion of it would increase between 5 and 11%. One of the highlights is that the residential rates would be 15% higher than CL&P. So if you look at that visually you could see from the lower right hand corner the red bars are the rate of return for the proposed rates and the blue bars are the rate of return for the present rates. You can see that the red bars are all the same and the 7 1/2 % return. You can see at the bottom right hand corner the visual representation of the rate impact and you can see that in this case the rate impact is just proportionally on the residential class because there is a loss to begin with. Also the competitiveness of the residential suffers the most. So, clearly to move immediately to uniform rate of return is probably not a good idea. But at least this is what would happen if you were to do that. The next scenario to look at, why don't we just increase the rate uniformly, so every class has a 14% increase. That's the same 5% overall rate of return. This will be a \$2.2 million dollar increase in revenues. Under this scenario, the residential rate would still be negative but it would be much closer with only minus 8%. The medium general and the municipal would jump up to 25 to 30% rate of return. The Small General would end up being 20% higher than CL&P and the Medium General would be lower than CL&P. So there are some competitiveness issues. When you look at the graph the rate impact in this case scenario is in the lower right hand corner. All three are the same for everybody. The rates of return are, they're sort of everything just gets sort of moved a little to the right, so the residential is less negative, the rest of them are more positive. This is actually not a, not a terrible alternative. It certainly is fair in the customer's perspective and everybody here bares the same level of [inaudible]. It's not quite as fair that the rates of return is a skewed, but it's not a bad starting point for making changes. It's certainly better than trying to go through uniform rate of return right away. The third scenario we looked at is uniform competitiveness. What if we just, what if just matched CL&P's rates. It turns out that that's pretty much what it would take to get to a 5% overall rate of return would be for each class to have to retain the same as CL&P. So you will be matching you know.... What's interesting to observe here is what happens to the rate of return because presumably if your rates are the same as CL&P than the rates of return produced by your rates are probably but should reflect what their rates are producing, in terms of rate of return. So this tells me that CL&P is losing money on their residential customers as well. It's a negative 9% rate of return. And in their case the Medium General are the ones who are contributing the most. It makes sense to a certain extent too. An industrial, their industrial customers are the larger portion of customers that are producing a very low rate of return. And it looks to me to make a lot of sense. And this is what looks to be a fairly typical pattern for utilities rates of return. And this is also not a bad starting point for the changing rates. The rate impact is not as uniform as in case 2 where there were earning 14%. In t his case the Medium General would be over 20% and some of the others would be smaller. But certainly shows a direction that you can move in. So the last scenario that we looked at is kind of a, my best suggestion as to a solution that gets you moving in the direction that you want to and it might prove to be politically acceptable. So that the criteria here were first to move the residential to a break even, not to earn a rate return but to at least have the residential rates recover the cost. That results in a 22% increase and results in being a percent above CL&P. I've adjusted the remaining rates of

return to reflect what's more typical for municipal utility practice where the Small General has a higher rate of return than the Medium General and the Large General. So those are rates of return. Small General gets a 17%, medium 13%, Large General 10%. And the increases there are all in the 10% range. The Medium General has smaller increases, only a 5% because they are at their highest level already. The largest increase is the residential. So this is kind of what we call a straw man proposal. I propose it and then you get to knock it down and make your own proposal. And finally, the last slide. I got to talk about this, just a few specific rate design objectives that we talked about. Up to now, we just talked in general terms of overall rate levels and rate levels by customer class and getting their detail sign of some of the things we want to do and in designing specific rates. And I won't get very specific about this but to give you an idea of what we're looking at. We want to try to develop time of use rates because that's the direction that the industry is moving in and it's also part of sending that price signal that we talked about earlier. Electricity costs, has different costs at different times. It's very expensive in hot days in the summer time. It's less expensive at night in the fall and spring. And you would like, in theory you want your rates to reflect as closely as possible so that the customers can make an intelligent decision about usage. Right now there are issues involved and actually they will implement that because the price that you pay your wholesale supplier doesn't reflect that time of used variation. So a large part of the price signal that is out there in the wholesale market isn't getting delivered to you. But there are other ways to begin to send the time of use price signal and we're going to explore ways to doing that and I understand we are also exploring ways of getting the wholesale supplier to begin to price the wholesale electricity. So we like to have rates ready to go to implement when that happens. I talked to you earlier about unbundled rates. We'll develop a set of unbundled rates. You may actually be able to implement them, but at the very least you want to have them available to implement when the billing system is able to accommodate them. Critical peak pricing is a variation of time use pricing. It's sort of a first step where you want to be able to get even more focused on pricing and send a much higher price signal to customers during certain hours particularly during the summer time when supplies of energy gets tight and you want to encourage people to use less electricity. We're going to explore billing, what's called KVA billing for reactive power and we're looking over hauling street lighting rates and finally we will be proposing some net metering rates for renewal energy for customers generating their own electricity. So those are some of the specifics that will begin, and that lasted an hour."

Commissioner Burgess: "Can I ask one question? On page 39, Large General used to balance revenues, does not say how much above CL&P it will be. Do you have any idea what that figure is?"

Mr. Seavey: "Yes, it's in the 0.5% range."

Commissioner Burgess: "Okay, thank you."

Mr. Seavey: "The numbers are in the table on slide 40."

Commissioner Burgess: "Thank you, I just needed the..."

Commissioner Ayme: "Through the chair, 'how much'? What's the gap between SNEW and CL&P right now. Because it used to be like 25 - 30% but I don't think the gap is that large right now."

Mr. Hiscock: "It varies widely, depending on the, we'll pick residential. Residential varies widely because our customer charge, our meter charge is very low in relation to CL&P, so that at low energy purchases we're extraordinarily cheaper than CL&P. That disappears rapidly though and examples at 100 kilowatt hours a month it's like 50% below. That's because the customer charge being very, very low. And at the very upper end, I think it's something like 3 or 4% below CL&P, based at least on the last information I saw from Mark Harris. And that has a lot to do with the fact that our residential rates inclined. We have an increasing block structure. That's something we really haven't talked about here and I think it's maybe a little bit early to talk about it. But an interesting block rate structure really is difficult on electric heat customers."

Commissioner Burgess: "And poor customers. Our customers are not the wealthiest in Norwalk."

Mr. Hiscock: "That's for sure. Yes, there's no doubt about that. And that's something that we're going to have to talk about going forward if want to continue to do things like that. I mean, it's a little early to get into that issue but, yes, so that as our price per kilowatt hour increases and CL&P's I believe is flat, yes, CL&P's is flat so that makes an approach. That's an issue."

Mr. Seavey: "And increasing block rates are politically popular these days because they are discouraging the usage of energy. So they consider it to be a conversation rates. But frankly, they're very difficult to justify it on an economic bases, because there isn't any real increased cost associated with increasing energies unless you are looking at a very long term perspective, like 20 years."

Commissioner Burgess: "Obviously, look at me. I'm not looking at 20 years."

Mr. Seavey: "Considerably, electric heating has been problematic from the beginning. You and I were talking earlier about public hearings and I have to say that the ugliest public hearing I ever went to was the municipal utility that had just eliminated the special electric heating rates. And they had, I think, every single senior citizen in the entire town. They came out of the neighborhood really angry, because a lot of people built or bought houses with the expectation that the electricity would be inexpensive. They know when you are making a long term capital decision on the base of electric rate, the utility does end up with an obligation, you know, some sense of obligation, to continue to honor that expectation even though it's no longer cost effective to do. Electric heating is a problem. You don't have electric heating rate anymore."

Mr. Hiscock: "No we do not."

Mr. Seavey: "And I'm sure it was eliminated years ago. But you still have electric heat customers and they don't experience any joy from the increasing block rate."

Mr. Hiscock: "Yes. It's an issue that we do, so that you understand the dynamics of this is for varies reasons. The developers sometimes put in electric heat into their units. One is, it's a lot less expensive to install initially. They are not worried about the long term cost. Another situation is some of the developers who develop for rental purposes will put electric heat in as opposed to oil heat because the poor customers get protected from shut off's by the electric utility in the winter time. But yet they can't compel private oil businesses to deliver oil and not be paid for it. So there is a tendency to move in that direction. There are a lot of issues related to that, that we are really going to have to talk about."

Commissioner Ayme: "One thing that had me worried for quite some time was a future contract that we have, the future contract that we have purchased. Do you follow what I am saying?"

Mr. Hiscock: "Yes, and that's our wholesale rate and has to do with gas futures and..."

Commissioner Ayme: "How, I understand we are not doing that anymore."

Mr. Hiscock: "The co-op is still doing it but to a much lesser extent."

Commissioner Ayme: "Okay."

Mr. Hiscock: "And most of our expensive gas rolls out in the middle of 13."

Commissioner Ayme: "How is that going to influence, because I know that we were facing some losses in that sense."

Mr. Hiscock: "I think what Mayhew is talking about from at least my perspective is, if we have an unbundled rate it's going to be easier to adjust to price changes in things that come back from the cooperative. So that's kind of an important issue."

Commissioner Ayme: "So that's not going to be a major factor in terms of the..."

Mr. Hiscock: "No, I think it will allow us to respond better."

Commissioner Ayme: "Oh, okay."

Mr. Hiscock: "And it will also make our distribution charge vs. our expenses sort of more in line with each other so that we can deal with the portion of the rate structure so that we can modify or you know, for way out of line distribution charges, we are going to have to do something about it. It's sort of a cost containment thing from our perspective. For years you know that we have had very cheap rates from CMEEC because rates were increasing gas prices were increasingly have a lot of good hedges, and the market price went way up and we were stable. But, and that's great in an incline market isn't it? But it's not so good in declining market. And that's where we find ourselves. It's a big issue. So, there is not much hope of our wholesale prices decline over the next year and a half to two."

Commissioner Ayme: "Oh, okay. It's pretty much leveled."

Commissioner Burgess: "Any of the other commissioners have any questions of the consultant? We can all grill John later on."

Mr. Hiscock: "We will be back for this issue a few more time I think."

Commissioner Ayme: "Oh, you will be coming back? [question was addressed to Mr. Seavey]."

Mr. Hiscock: "Oh yes."

Mr. Seavey: "I will be coming back with specific recommendations."

Commissioner Ayme: "Oh, okay. That's good."

Commissioner Burgess: "Thank you very much."

Mr. Hiscock: "I have a few things that the commissioners need to think about going forward. One, we have to think about if we're going to continue the practice into what degree of, and you are on the public record, but going out of our way to keep residential rates as cheap as they are maybe that's a good way to say it. And it's going to have a lot to do with some of the decisions you are going to have to make going forward. And that's an important issue."

Commissioner Ayme: "Okay."

Mr. Hiscock: "And you all have to think about that issue."

Mr. Seavey: "And that can be done in phases. It doesn't have to be adjusted all at once so you can decide that, you know, over three years you're going to have to face the residential rates up to 0% return, and then over that period of time I suspect that the wholesale prices will be back in line with CL&P."

Mr. Hiscock: "Probably,"

Commissioner Burgess: "Hopefully."

Mr. Hiscock: "The other issue that will be exploring with CMEEC and its going to be discussed at the July meeting, at the end of July, is maybe making a significant withdrawal from the municipal trust, stranded cost issue. Our stranded cost goes through 17 because we bonded out of the millstone project, okay, and CL&P's stranded cost just disappeared. Who knows what's going to happen with the state budget and the rate making. They were trying to take electric rates roll it into the budget. I mean there's at least from my perspective, some ugly things going on with legislature. But right now, CL&P's stranded costs have disappeared. Their rates will be dropping. And it was going to be sort of not giving us trouble because the state was going to take that money and use it for economic recovery bonds. The original municipal trust was created for exactly this time period, from when CL&P's stranded cost were rolling off and ours were not, so that we can believe now that the competitive trust, to try to keep ourselves competitive with CL&P. That issue is starting to surface at CMEEC because Norwich is higher than CL&P right now. Jewett City is slightly above CL&P, Groton has some rate structures that are significantly above CL&P and the only one that's doing really well is Wallingford, okay. So there are, and Wallingford is not a member of the CMEEC. They're only participants. So there are some discussions that are starting about drawing the municipal trust. It's not going to solve the problem by any means because we are only talking. I mean even if we did it over the next five years it would be about a million dollars a year, somewhere in that range, which could have some impact."

Mr. Seavey: [Inaudible]

Mr. Hiscock: "Yes, exactly. So some of those things may be occurring, not only pressure from myself, but Norwich, and to a lesser extent, Groton, and definitely Jewett City are really talking about that structure, so maybe we can, you know mediate some of the impact here."

Commissioner Burgess: "Thank you. Anyone else have questions?"

Commissioner Ayme: "No questions."

Commissioner Burgess: "Thank you. Then we will see you again."

Mr. Seavey: "See you all. Thank you all."

Commissioner Borges Lopez: "Thank you."

Commissioner Mann: "Very good presentation."

Mr. Hiscock: "Thank you."

Commissioner Burgess: "Well, Mike Geake is not here so there's no public."

Mr. Hiscock: "One of the issues that I do want to mention that may come up, and I'm looking at it with council and the basic question is 'are we going to need to do a Public Hearing.'"

Commissioner Burgess: "Oh."

Mr. Hiscock: "And there is a possibility of that. We are examining that..."

Commissioner Burgess: "For this rate thing?"

Mr. Hiscock: "Yes, because we are not doing a uniform increase, we are not doing a percentage increase. We are not doing one of those adjustments like a purchase power adjustment where it's already in the rate structure. We're talking, as you can see, significantly modifying the rate design. The question comes up, our Charter vs. the Statute. And we don't want to make a mistake here. Because we don't want the largest customer to come back and challenge what we are doing on something as simple as failure to file the rates in draft form holding hearing and then going back and adopting. Now..."

Commissioner Burgess: "Well, do you have any indication we have to have a Public Hearing?"

Mr. Hiscock: "Not yet, because it really has a little bit to do with where we are heading here."

Commissioner Burgess: "Okay, okay."

Mr. Hiscock: "So, I don't have a strong..."

Commissioner Burgess: "Okay, you're just warning us."

Mr. Hiscock: "I'm warning you that there is a possibility."

Commissioner Burgess: "Okay,"

Mr. Hiscock: "Okay, but you certainly don't want procedural form, that's for sure."

Commissioner Ayme: "Do you have any idea to the extent of the increase?"

Mr. Hiscock: "No."

Commissioner Ayme: "Okay."

Mr. Hiscock: "I think we have goals that we all recognize and we recognize our competition. Mayhew, as you can tell, has gone through that thinking about all of those related issues pure rate making vs. how you deal with the competitors. I mean, it's sort of laid out. You know you can go all over this again and think about it, but over the next several weeks we'll be chatting back and forth with Mayhew about the topics. The things on the last page, while they are interesting things they really don't affect the bulk of what we are doing, okay. The time of use rates, the unbundled we're going to do, we need to do so you can compare with CL&P. Pricing, KVA billing, setting street lighting rate even though we may pay it ourselves and net metering. They don't involve a whole lot of customer bills."

Commissioner Ayme: "Well, I mean, that's going to, let me ask another question. Do you have a time frame for the implementation?"

Mr. Hiscock: "I originally wanted to implement in the beginning of the fiscal year that we just started. That isn't going to happen. I'm thinking this is going to be working through the summer and then do it in the fall, the early fall, maybe a final adoption by the September meeting, something along that line. That's sort of what I am thinking about. There have been a few developments that have occurred that have been at least a little bit helpful to us. One is that the typical situation that we get with CMEEC. They produce a budget. We state our purchase power adjustment based on that budget. We didn't change ours this year because we're anticipating doing this, but they have been performing reasonably well. Even though we got high rates they are not quite as bad as we thought in looking forward vs. the actuals. So that's going to help a little bit. Our rates stabilization fund is not declining where we thought it would be declining. All of these little things will add up and help out. And certainly the issue of the competitive trust, we can join from that, is an important issue. Those are big dollars."

Commissioner Mann: "Well, one of the things that, that's really concerning me is the recommendation of residential 22% increase. I just..."

Mr. Hiscock: "Yes, I understand that."

Commissioner Mann: "It's a major concern."

Mr. Hiscock: "Yes. These are going to be difficult topics."

Commissioner Mann: "They really are."

Mr. Hiscock: "Because you don't want, and certainly it's my opinion, but don't want to unbalance yourselves in the direction that we unbalanced in 2000, 2001, 2003, when we first got involved here, when everybody in town knew that all the rates in all the classes other than residential were higher than CL&P's. You were dealing with just the very, very beginning of rate regulations, deregulation. There wasn't much anybody could do about it. Nobody cared about it. But we're now in an environment where everybody gets the flyers in the mail even though you are not allowed to change suppliers in South Norwalk. Everybody gets those flyers in the mail. Everybody knows

what everybody else is paying. It's very open, very transparent and if we unbalance to the point where, or non residential rates are significantly higher than CL&P we could end up with political pressure and political pressure that could be costly in the long run if for some reason somebody decides that the munies in Connecticut need to be regulated by the DPUC."

Commissioner Burgess: "All right."

Mr. Hiscock: "Then there is no control then that's a difficulty. Now, we also heard Mayhew say, and it's shown in this analysis, that CL&P is also discounting their residential rates from standard rate making policy. And I think you can fully appreciate that, that's probably political also, because you know as much as the DPUC are a professional department their commissioners are political animals. They are appointed by the government and the legislature in various ways and I don't know exactly how they get appointed. And I'll give you a personal side, not the company's position, but had in the eighties and nineties, the political pressure in the state to keep residential rates low, and it happened in many states in the northeast, we might have never had deregulation. We might have been the old style entities, but political pressure forced residential rates extraordinarily low in relationship to their value and commercial rates and industrial rates became the victim very high and that unbalanced us with respect to large manufacturing. I mean politically you can lay this all back on a bad attitude in the eighties and nineties about this. Expediency hurt."

Commissioner Ayme: "Maybe they can afford to play the political game, but we're not..."

Mr. Hiscock: "It's not CL&P, it's the regulator."

Commissioner Ayme: "The regulator."

Mr. Hiscock: "CL&P will do whatever the regulator wants just as long as long as he gets his rate of return."

Commissioner Mann: "Absolutely."

Commissioner Ayme: "Yes."

Mr. Hiscock: "The average rate of return is all they care about. The class is irrelevant to them. I don't mean that to criticize."

Commissioner Burgess: "Anybody has anything else?"

Mr. Hiscock: "I do agree with the sentiment. We have a residential issue we have to deal with."

Commissioner Ayme: "I agree with Commissioner Mann who said that 22% is we have to have time to talk about it."

Mr. Hiscock: "Oh yes, we absolutely do, and as you noted it was the starting point that we're all going to work from and as you understand the commissioners sentiment with respect to that. And hopefully the mitigation will be the competitive trust because if it is a two million dollar increase in the competitive trust provides a million, that's a huge difference."

Commissioner Mann: "Seven percent."

Commissioner Ayme: “Yes. Alright, well, move to adjourn.”

Commissioner Geake: “I second it.”

Commissioner Burgess: “Second.”

Commissioner Burgess: “All in favor.”

Simultaneously: “Aye.”

Adjournment

The meeting adjourned at 8:03 p.m.

Attest:

Gwendolyn Gonzalez
Asst. District Clerk

Transcribed by: Connie Farrugia
Reviewed by: Gwendolyn Gonzalez