STATE OF VERMONT

PUBLIC UTILITY COMMISSION

Case No. 18-____-___

Petition of Town of Stowe Electric Department	)
pursuant to 30 V.S.A. §§ 225 and 227(a) for a 7.9%	)
rate increase to take effect on a service-rendered	)
basis August 15, 2018	)

PREFILED DIRECT TESTIMONY OF

STAN FARYNIARZ AND MATTHEW LOIACONO

ON BEHALF OF

THE TOWN OF STOWE ELECTRIC DEPARTMENT

Summary of Testimony

The testimony of Mr. Faryniarz and Mr. Loiacono in support of the Town of Stowe Electric Department's 2018 Rate Case explains SED's reasons for the proposed rate changes, explains the rate case model employed, describes the various adjustments made from the Test Year to Rate Year, explains the process for normalizing certain income and expense items that change after the Rate Year, demonstrates that the proposed rate changes are just and reasonable, in the public interest, and consistent with historical PUC ratemaking precedent, and provides revised rate schedules ("tariffs") to implement to rate change.

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STOWE ELECTRIC DEPARTMENT

I. INTRODUCTION

Q1. PLEASE STATE YOUR NAMES, POSITIONS, AND BUSINESS ADDRESS?

A1. Our names are Stan Faryniarz and Matthew Loiacono; our titles are Principal Consultant and Consultant, respectively, with Daymark Energy Advisors, formerly La Capra Associates. Our business address is 370 Main Street, Suite 325, Worcester, Massachusetts 01608.

We will be providing testimony jointly in this proceeding as a panel, referred to by SED's other witnesses as the "Daymark Panel".

Q2. PLEASE DESCRIBE YOUR FIRM.

A2. Daymark Energy Advisors ("Daymark") is a consulting firm specializing in energy planning and market analysis, commerce within those markets, regulatory and ratemaking economics, and regulatory policy in the electricity, natural gas and water utility industries. For approximately 38 years, our firm has served a broad range of organizations involved with energy markets -- public and private utilities, energy producers and traders, financial institutions and investors, consumers, regulatory agencies, and public policy and research organizations.

Q3. MR. FARYNIARZ, PLEASE DESCRIBE YOUR BACKGROUND AND EXPERIENCE.

A3. I am an energy economist and power supply planning and management specialist with 32 years of experience in areas including electric utility cost of service and rates, power supply procurement and management, wholesale and retail power transactions, power project financial analysis and due diligence, asset and utility valuations, and integrated resource planning and analysis.

I have advised managers concerning the electric power supplies of public and investor-owned electric utilities, and have advised large industrial customers, regulators, consumer advocates, and power plant developers and owners regarding specific power projects and transactions, portfolio risk management strategies, and power markets.

I have prepared numerous valuation analyses of power projects and assets, combined portfolios of assets, and electric utilities. This work has involved power production assets in the northeastern U.S., North Carolina, Ohio, Arkansas, Wisconsin, and Canada. I have evaluated the economics, contract structure, ratepayer security, development prospects or going-forward value of dozens of renewable and non-renewable merchant, and Qualifying Facility ("QF") power projects in the northeastern U.S. and Canada. I have conducted this work for regulators and for providers of private capital and quasi-public capital.

I have prepared, have overseen the preparation of or reviewed on behalf of interested stakeholders all or portions of integrated resource plans for several Vermont utilities and for other public utilities, and I am a load forecasting specialist.

My experience includes the preparation of well over a dozen electric and water utility rate cases, allocated cost of service and rate design studies, rate unbundling studies, and rate path projection studies, for or involving utilities in most northeastern U.S. states, North Carolina and Utah.

A copy of my resume and list of proceedings in which I have provided expert testimony is included as Exhibit SED–Daymark–1.

Q4. MR. LOIACONO, PLEASE DESCRIBE YOUR BACKGROUND AND EXPERIENCE.

A4. I am a Consultant at Daymark. I work with electricity and gas clients on matters including cost of service and rates, capital expenditures, grid modernization planning and net energy metering. I have analyzed approaches to renewable resource integration and benefit-cost analyses of various modes of participation on wholesale energy market performance. I advise clients on energy procurement strategy and administer procurement approaches, including auctions, on their behalf.

My experience includes advising utilities and regulators on rate design, revenue requirements, capital expenditures, net energy metering, and natural gas and electricity power supply contracts. A copy of my resume is included as Exhibit SED–Daymark–2.

Q5. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING AND FOR WHAT PURPOSE?

A5. We are testifying on behalf of the Stowe Electric Department ("SED" or "Stowe") in support of its petition for Public Utility Commission approval under 30 V.S.A. § 225 and 227(a), to implement changes in rates and adopt revised rate schedules ("tariffs"). Marked and clean versions of the new tariffs are provided in Exhibit SED–Daymark–3.

Q6. WHAT ROLE DID DAYMARK PLAY IN SUPPORT OF THIS EFFORT?

A6. Daymark was retained by SED to:

1. Analyze its current 2017 Test Year cost of service;
2. Develop an updated revenue requirement for the largely 2018-based Rate Year, starting with historical Test Year 2017 and then making pro-forma adjustments for known and measurable changes in income and expenditures; and
3. Prepare revised rate schedules.

We oversaw the development of each of these project segments, assisted SED's other witnesses with explaining adjustments to the Test Year income and expenditures to establish the Rate Year cost of service, and sponsor the specific tariffs for which SED seeks PUC approval in this docket.

Q7. MR. FARYNIARZ, HAVE YOU EVER TESTIFIED BEFORE THE VERMONT PUBLIC UTILITY COMMISSION OR IN OTHER JURISDICTIONS ON COST OF SERVICE AND RELATED STUDIES, AND RATE DESIGN?

A7. Yes, I have presented testimony before the predecessor to the PUC (the Vermont Public Service Board) on the foregoing subjects on numerous occasions since 1986. I have also testified on these subjects before utility regulatory authorities in Maine, Pennsylvania, Rhode Island, Utah, and New Hampshire. A list of proceedings in which I have participated is appended to my resume, Exhibit SED–Daymark–1.

Q8. MR. LOIACONO, HAVE YOU EVER TESTIFIED BEFORE THE VERMONT PUBLIC UTILITY COMMISSION OR IN OTHER JURISDICTIONS ON COST OF SERVICE AND RELATED STUDIES, AND RATE DESIGN?

A8. I have not testified before the Vermont PUC, but I have testified on these subjects before utility regulatory authorities in Rhode Island. I have also provided testimony support on these subjects before utility regulatory authorities in Massachusetts, Rhode Island, Utah, and New Hampshire.

Q9. WHAT IS THE PURPOSE AND LAYOUT OF YOUR TESTIMONY?

A9. First, we discuss SED's goals and objectives associated with the change in rates. SED has not had an increase in rates since 2010. In 2014, SED implemented a decrease in retail rates that has, coupled with known and measurable changes to its cost to serve, led to a revenue requirement deficiency which would otherwise manifest itself beginning in 2018. Together with the other SED witnesses, we will show how the proposed rate increase will enable SED to recover the revenues necessary to cover its costs.

Next, we present and explain the methodology undertaken to address *known and measurable* changes in income and expenditures as shown in the rate case schedules appended as Exhibit SED–Daymark–4.

We also provide a Proof of Revenue for the 2017 Test Year and the 2018 Rate Year following the requested *uniform* rate increase. The Proof of Revenue is attached as Exhibit SED–Daymark–5.

Finally, as already noted, we sponsor the tariff sheet adjustments reflecting the uniform retail rate increase in Exhibit SED–Daymark–3, including certain non-retail rate tariffs for a few key miscellaneous charges that required updating to reflect the current cost of providing the underlying services.

We conclude that these rates are consistent with Public Utility Commission ratemaking precedent, serve the public interest and are, overall, just and reasonable.

II. SED OBJECTIVES FOR THIS FILING

Q10. PLEASE DISCUSS STOWE'S GOALS AND OBJECTIVES FOR THIS RATE INCREASE REQUEST.

A10. Stowe had several goals and objectives. These include:

- Presentation of a fair and fully documented increase in SED's cost of service for known and measurable changes since the calendar 2017 Test Year;

- Utilization of the rate case model that the PUC and Vermont Department of Public Service ("DPS") already approved for Stowe's 2014 rate decrease in Docket 8074;
- Ensuring that SED has sufficient revenue to cover its Rate Year costs, in part by including certain accounting adjustments often referred to as "normalizations" for changes in income and expenditures after 2018; and
- Ensuring Stowe has an adequate cash position over and above its Rate Year cost to serve in part by building into rates a requested times interest earned ratio ("TIER") sufficient to ensure a positive cash and retained earnings position going into the Rate Year and beyond, and which would also allow SED to secure debt financing for capital requirements necessary to meet its commitments to provide safe, reliable and cost-effective power supply and delivery services to its ratepayers.

III. STOWE RATE PATH SINCE 2010

Q11. PLEASE DESCRIBE STOWE'S RATE PATH SINCE 2010 COMPARED TO OTHER VERMONT ELECTRIC UTILITIES.

A11. As also discussed in the testimony of Ms. Burt on behalf of SED, SED has not had a rate increase since the start of the decade. In 2014, a PUC-approved rate reduction of 3.5% was implemented in Docket 8074, and despite a revenue-neutral[1] rate redesign in 2015, rates have held steady since then. Data from

[1] At the approved Docket 8074 cost of service.

Vermont DPS Electric Utility Annual Reports suggests Stowe's average rates have tracked toward the statewide average (which is dominated by the weighted effect of GMP).

Figures 1, 2, and 3 below show SED's rate path from 2010 to 2016 for Residential, Commercial, and System Wide Average Rates.

Figure 1

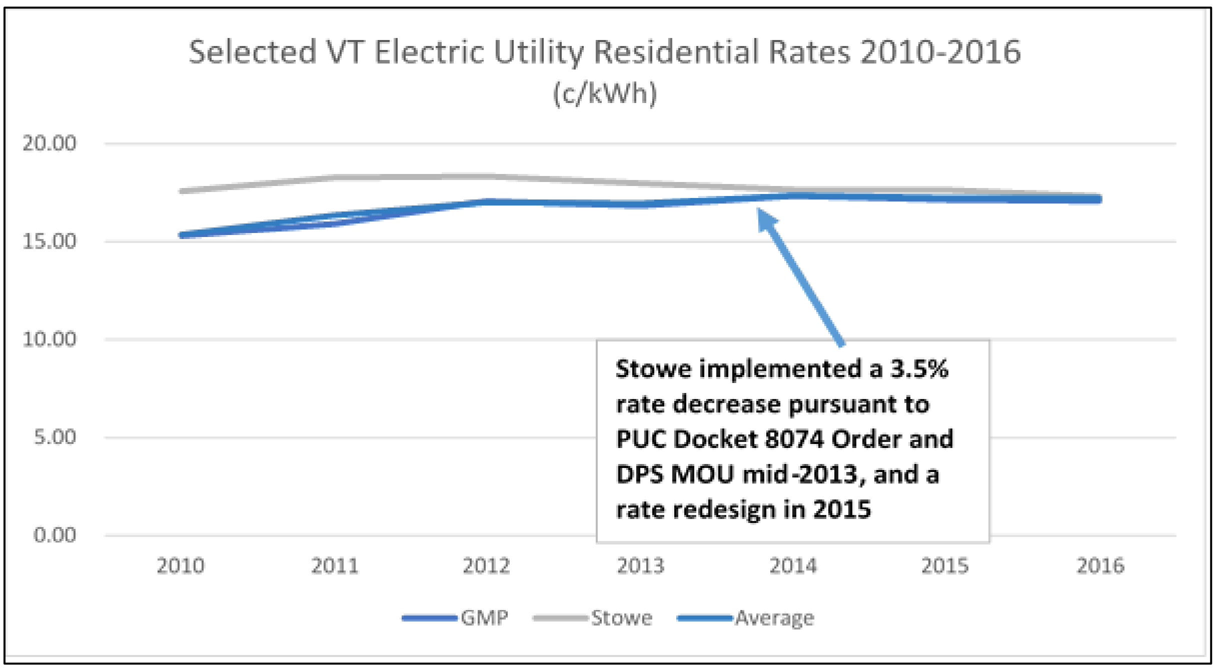


Figure 2

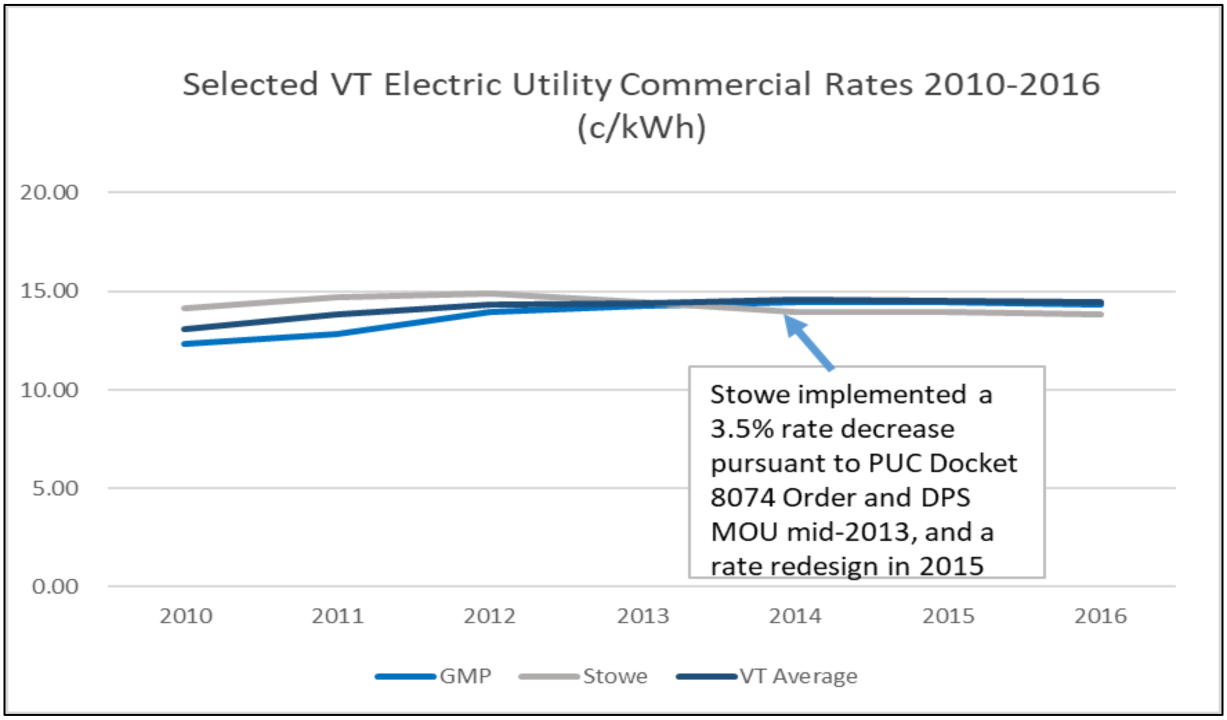
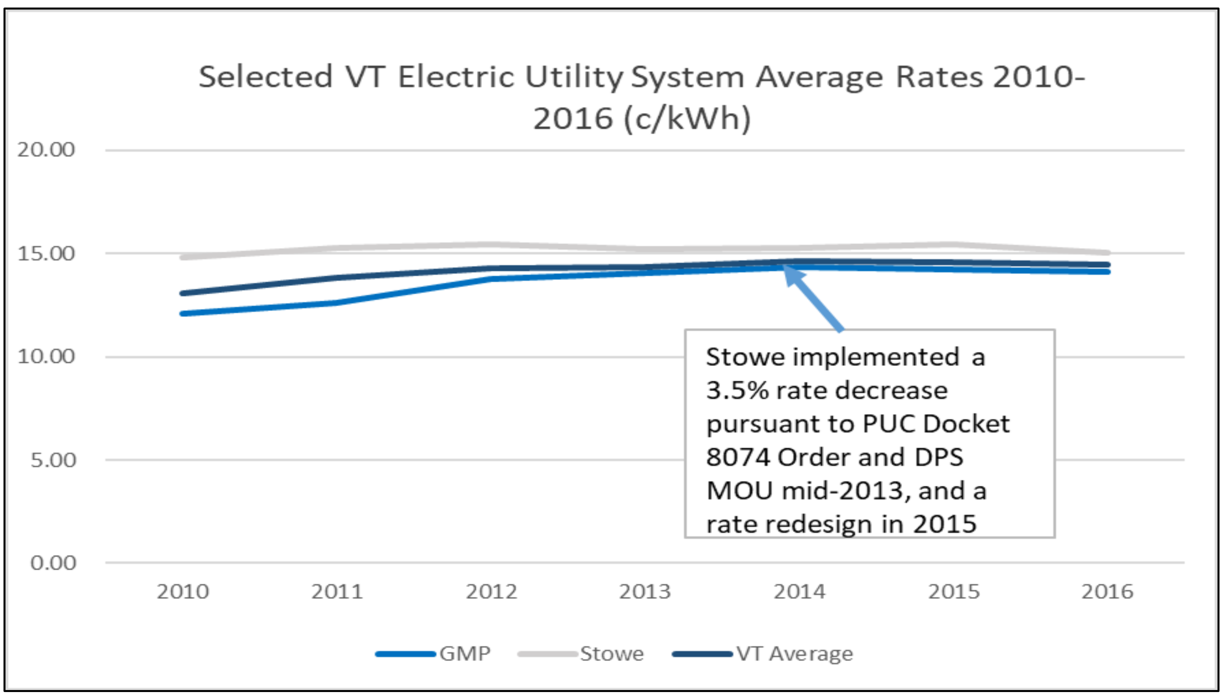


Figure 3



As of the end of 2016, the last year in which there was average rate data available from the DPS, SED's average residential rate was within 1 mill/kWh[2] of the statewide average of 17.23 c/kWh. Its small commercial average rate at 13.82 c/kWh was about 6 mill/kWh lower than the statewide average of 14.43 c/kWh, which is important because the SED system and the local economy, given that Stowe is a resort town, are dependent on a substantial number of these types of customers. Overall system rates compare reasonably well with the statewide average, and at 15.05 c/kWh, Stowe average system rate was only 6 mills higher than the statewide average system rate of 14.45 c/kWh.

Q12. HOW HAVE STOWE RATES TRACKED AGAINST OVERALL INFLATION SINCE 2010?

A12. SED average rates have escalated at well below the rate of inflation as measured by the Bureau of Labor Statistics Consumer Price Index ("CPI"),[3] as Figures 4 and 5 below indicate.

As illustrated in Figure 4, we measured the rate of escalation in the CPI vs SED's average residential and system total rates and found that the compound

[2] A mill = 1/10th of a cent.
[3] For All Urban Consumers.

(annual) average growth rate ("CAGR") of the CPI index (2018 projected based on 4 months of data), was almost 1.8% per year, while SED's average residential rate rose less than 0.85% annually and its average system rate rose by less than 1.3% annually on average, even after factoring in the requested 2018 rate increase herein of 7.9%.

Figure 4

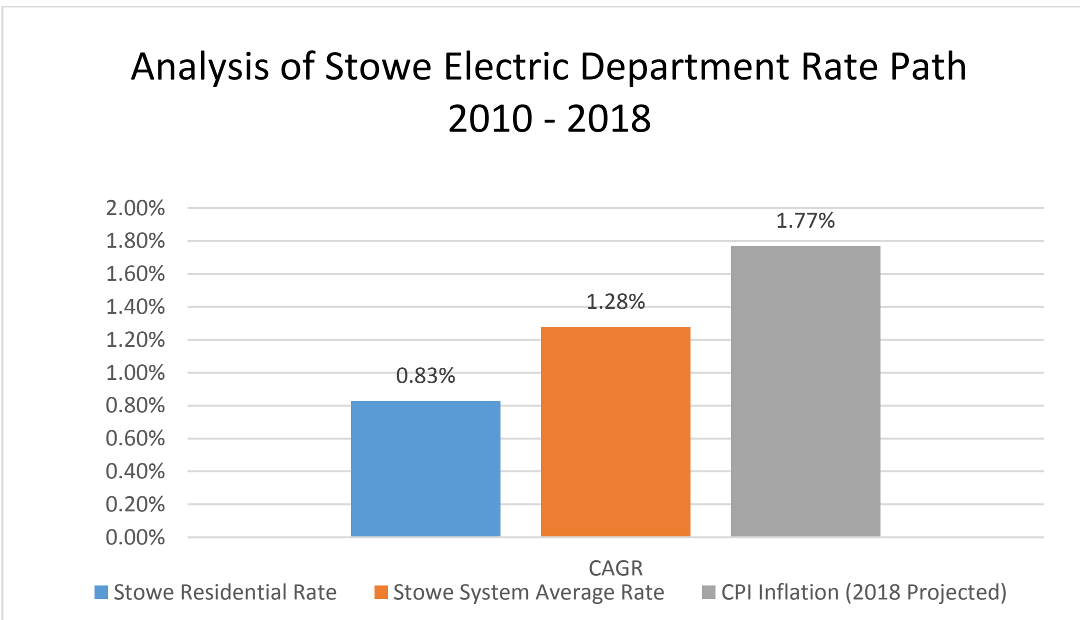
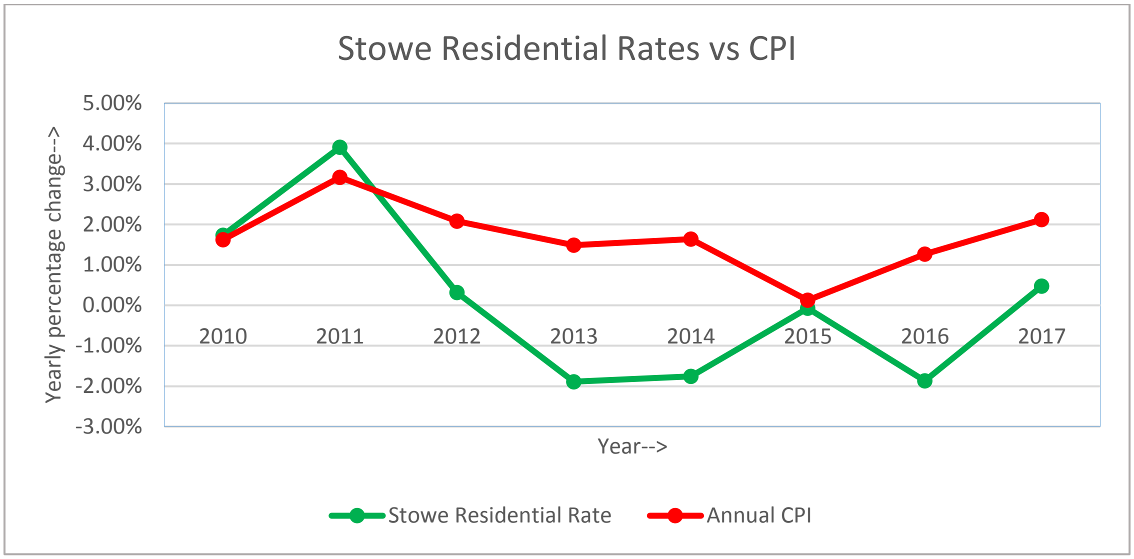


Figure 5 shows a comparison of year-to-year changes in the CPI vs Stowe's average residential rate, which has managed to stay below the rate of average inflation through 2017.

Figure 5



IV. FACTORS BEHIND THE CURRENT REQUEST FOR RATE RELIEF

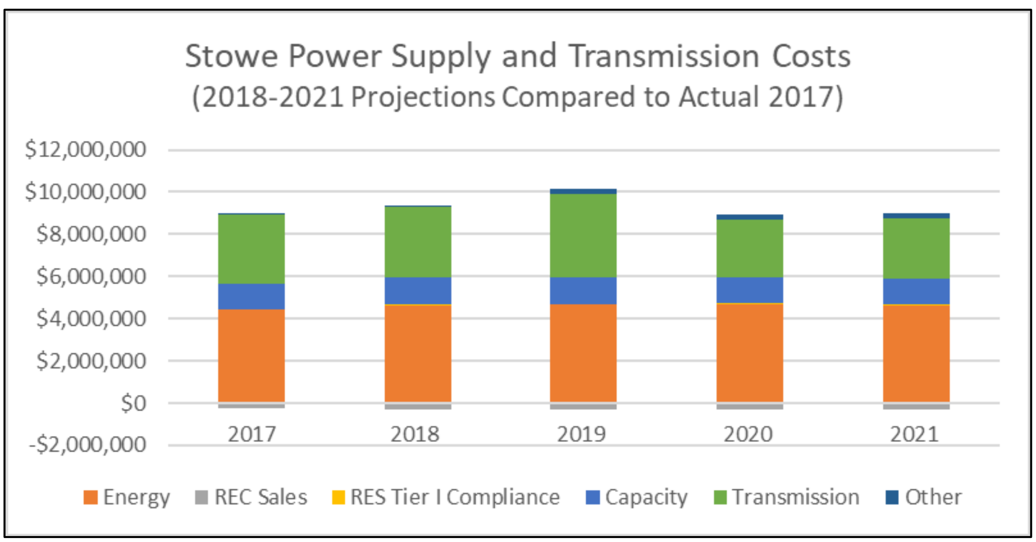
Q13. PLEASE BRIEFLY DESCRIBE THE FACTORS THAT LED STOWE TO SEEK A RATE INCREASE NOW.

A13. The primary reason for requesting rate relief now is that overall costs of service have increased beyond Stowe's revenue growth under current rates. These factors are discussed more fully in the testimony of Ms. Burt and Ms. Sullivan, but bear repeating here. In summary:

- Retail sales decreased about 4.3% in the 2017 Test Year, and are projected to increase only 0.3% in the 2018 Rate Year based on known and measurable adjustments.
- As noted in the testimony of Mr. Hebert, Stowe's power supply and transmission expenses, which comprise about 3/4^{ths} of projected 2018 cost of

service, have increased due to higher capacity charges starting in 2017 and higher transmission expenditures going forward through 2019. Much of the higher transmission costs are traced to the closeout of the Lamoille County Project ("LCP") financing settlement described in the testimony of Ms. Sullivan, under which Specific Facilities payments and the arbitrage payments related to purchases of Vermont Transco stock a decade ago extend into 2019, while offsetting Transco stock dividends expire a year earlier in 2018. As shown in Figure 6 below, SED expects to incur over $1 million in mostly higher transmission expenses by 2019 compared to the 2017 test year.

Figure 6



- New debt was taken on in 2017 of about $1.65 million to fund equipment replacement and to purchase Membership Units in Vermont Transco.

- Operating expenses and depreciation associated with some of the new plant increased by about 18% over 2017, and depreciation will increase again beginning in 2018 as a result of placing two capital projects[4] into service this year, as discussed in Ms. Burt's and Ms. Sullivan's testimony.
- A 4% increase in salaries and wages for unionized employees and an SED Board-approved 3.5% increase in same for non-unionized employees, as described in Ms. Sullivan's testimony, will occur starting in 2018.
- A substantial amount of storm expense, especially from the late October 2017 wind and rainstorm, resulted in approximately $350,000 in additional restoration costs incurred in 2017, for which reimbursement by the Federal Emergency Management Agency ("FEMA") is expected to be only about a third of that level, as described in the testimony of Ellen Burt and Denise Sullivan.

Q14. AFTER TAKING INTO ACCOUNT ALL OF THE FACTORS DESCRIBED ABOVE WHICH HAVE AFFECTED SED'S OVERALL COST OF SERVICE, WHAT IS THE RATE INCREASE STOWE REQUESTS OF THE PUC?

A14. As also discussed in the testimony of Ms. Burt and Ms. Sullivan, we project in our rate case model that Stowe will need an increase to current rates of 7.9%. It

[4] Replacement of the tie point between Circuits 6 & 7, and a rebuild of the 34.5 kV distribution line behind the cross-country ski center and metering pots at the Lodge substation.

would be a little more than half of that if the 2013 Docket 8074 rate decrease had not been implemented.

V. THE RATE CASE MODEL

Q15. DID YOU PREPARE A RATE CASE MODEL TO INDICATE CHANGES TO OVERALL COST TO SERVE BETWEEN THE 2017 TEST YEAR AND THE 2018 NORMALIZED RATE YEAR?

A15. Yes, the Rate Case Model is provided as Exhibit SED–Daymark–4. Associated schedules that support the model are provided in the testimony of Denise Sullivan, including Exhibit SED–DS–4 (Three-Year Projected Cash Flow (2018 to 2020)), Exhibit SED–DS–5 (Four-Year Debt Service Schedule), and Exhibit SED–DS–6 (Four-Year Capital Spending Forecast).

Q16. PLEASE DESCRIBE THIS MODEL.

A16. The model we developed to support the rate increase is the same one used in Docket 8074 which led to the 3.5% rate decrease then approved by the PUC.

Importantly, while the Test Year and Rate Year costs and revenues have changed, the model presents Stowe’s “Cost to Serve” as described in the Docket

8074 Direct Testimony of Stowe's then-rate case consultant Raymond Koliander. As Mr. Koliander noted, the model includes not only traditional utility cost of service components, but also non-operating expenses and income from unregulated operations. As Mr. Koliander explained at the time, for investor-owned utilities it is not common to include such items in the cost of service to set retail rates, though investments in affiliate operations are sometimes considered. However, as a municipal public power utility, SED has elected to include those non-operating items because costs and returns on investments such as SED has made in VELCO/Vermont Transco, for example, made with ratepayer funds, should be recognized in the retail rate revenue requirement.

Q17. HOW WAS THE TEST YEAR IN THE MODEL DEVELOPED?

A17. Calendar 2017 Test Year income and expenditures are based on SED's actual audited financial statements for 2017,[5] and costs are categorized similarly to the way they are portrayed in the SED 2017 Annual Report to the DPS, without any adjustments.

[5] Provided in the testimony of Ms. Sullivan as Exhibit SED–DS–2.

Q18. PLEASE DESCRIBE THE RATE YEAR AS COMPOSED IN THE MODEL.

A18. The Rate Year (aka "Adjusted Test Year") in the model is based largely on projected 2018 income and expenses, which themselves are based on known and measurable changes since the 2017 test year. However, in some cases where costs track higher or lower beyond 2018, we *normalized* (adjusted) Rate Year known and measurable costs for these different tracks.

Q19. PLEASE DESCRIBE HOW YOU NORMALIZED CERTAIN INCOME AND EXPENDITURES IN YOUR RATE CASE MODEL.

A19. The Rate Case Model provides detail on the Rate Year changes over Test Year cost of service and totals up Stowe's Cost to Serve (Revenue Requirement) in the Rate Year. It also presents in the *bottom line*, a comparison of SED's Rate Year revenue requirement to its revenue under current rates plus other non-operating income and expenses.

That comparison indicates that Stowe will need another $1,035,932 in retail rate revenue in the Rate Year, or 7.9% over current retail rates, once several new residential accounts and one commercial account that are known and measurable since the Test Tear have been accounted for. This process of adjusting rate year income (in this case) or expenditures is known as normalization. If an income or expense item changes in a known and measurable way beyond the adjustments made for the next calendar year (in this case 2018), we have chosen to normalize such changes by averaging the income or expense item over a period of time beyond the rate year.

Q20. OVER WHAT PERIOD OF TIME WERE NORMALIZATION ADJUSTMENTS MADE?

A20. In most cases, we propose a normalization over four (4) years, when various extraordinary and/or non-recurring income or expenditures occur beyond 2018. In those cases, expected costs or income are averaged over the period from 2018 to 2021 to the extent they are known and measurable.

Q21. WHY DID YOU CHOOSE A PERIOD OF FOUR YEARS FOR SOME OF THE NORMALIZATION ADJUSTMENTS?

A21. There were two reasons. First, particularly in the case of large non-recurring income (such as the Vermont Transco LCP Member Unit dividends ending in 2018 as described in Ms. Sullivan's testimony) or cost items (such as the interest expense on the loan to purchase those Member Units and the related Specific Facilities payments which end in 2019), a four-year amortization blunts the rate year retail rate impact that would otherwise result from cessation of these non-recurring items.

Secondly, insofar as these normalization adjustments are based on known and measurable changes, a four-year period of normalization was chosen because Stowe believes that it is in the interests of the utility, customers, and regulators to try to craft a rate and revenue requirement now that is intended to be stable and sustainable for several years in order to avoid the requirement for another rate case and the rate dislocation that comes with it.

Importantly, as shown in Figure 6 and Exhibit SED–Daymark–4, SED's power supply and transmission expenses, and certain other costs like salary and wages, increase through 2019. After that, however, they either level off or start to come down, particularly due to the closeout of the LCP-related transmission expenditures. A rate case based only on known and measurable Rate Year adjustments through 2018 would yield insufficient revenue starting in 2019. If normalizations were only for two years through 2019, because overall costs decrease considerably thereafter, the rate case revenue requirements would end up being more than is needed to cover costs in the 2020 to 2021 timeframe. So, a four-year normalization was chosen to strike a reasonable balance given the cost and revenue trajectory SED faces. We believe this approach promotes rate stability and has the potential to avoid any rate adjustments until the next decade.

Q22. WHERE ARE THE NORMALIZATION ADJUSTMENTS FOR INCOME AND EXPENSE ITEMS BEYOND CALENDAR YEAR 2018 DESCRIBED?

A22. The adjustments between the 2017 Test Year and the Rate Year are discussed below, as well as in the testimony of witnesses Sullivan and Hebert, and are identified numerically in the Rate Case Model (Exhibit SED–Daymark–4). Generally:

Retail Rate Revenue

With regard to retail rate revenues, please see Adjustments 1 & 2 as described in Ms. Sullivan's testimony, which adjust rate year revenues up by about $37,000 over test year revenues as a consequence of new accounts being added.

Miscellaneous Non-Operating and Significant Non-Recurring Income

Refer to adjustments 3 & 4 in Ms. Sullivan's testimony. These items extend into 2019 but then cease, so were normalized over a four-year period from 2018-2021.

Lamoille County Project (LCP) Related Transmission Expense

These adjustments are described in the testimony of witnesses Hebert, Sullivan, and Burt. Significantly higher transmission expenses related to the LCP in 2018 and especially in 2019 give way to substantial reductions in 2020 and 2021 following the end of the hedge described in Ms. Sullivan's testimony. Therefore, these expenses were normalized over a four-year period. This normalization, while appropriate, will put cash flow pressure on Stowe in the first couple of years as the amounts embedded in retail rates will be insufficient by over $1 million during the first two years of the four-year amortization. This is one factor supporting Stowe's TIER request discussed in section VI of our testimony.

LCP Specific Facilities Payments

This is another significant expenditure associated with the Lamoille County Project, $1.1 million per year for 2018 and ending in 2019. Therefore, a four-year amortization was built into rates of $550,000.[6] Again, like the LCP transmission expense discussed above, this normalized value will be insufficient to cover the costs in 2018 and 2019, which will affect SED cash flow. This is another key factor supporting SED's TIER request discussed below.

[6] (1.1 million X 2 years)/4 years of amortization = $550,000.

Planned Sale of SED Share of Highgate Converter

As discussed in Ms. Burt's testimony, the planned sale of its Highgate Converter entitlement will affect transmission expense associated with this asset. To reflect the fact that ownership-related expenses and use rights will cease following that sale, test year expenses were reduced by half and use rights end. The rate year assumption is that these costs are incurred for 2018 only and use rights end completely by the end of the year.

SED Capacity Costs

As noted by witnesses Hebert and Sullivan, the trajectory for SED capacity costs is down over the coming years, reflecting known and measurable declining ISO-NE forward capacity market ("FCM") prices. See Exhibit SED–TH–2. We therefore amortized these known and measurable declines in ISO-NE interchange capacity costs over four years. Like with the foregoing two adjustments, the embedded rate year expense will lead to under-recovery of these costs and reduced cash flows over 2018 and 2019, and is another factor supporting Stowe's TIER request in the next section.

Depreciation Expense

While depreciation expense built into rates increases by a little over $40,000 in 2018 as known and measurable system projects are placed into service, depreciation expense is expected to increase further in the years after 2018 when other projects, not yet approved (and therefore not precisely known and measurable) are expected to be added to rate base. Like with a number of previous adjustments described above, it is anticipated that the $586,562 built into rates, based on a 2018 adjustment only, will be insufficient to cover this non-cash expense after 2018. So again, Stowe's TIER request discussed in the next section is based in part on these under-recoveries in 2018 and 2019.

Solar Project Operations and Maintenance

Solar O&M costs are increased based on a known and measurable new contract as described in the testimony of Denise Sullivan.

Contract Services & Information Technology (IT) Expenses

These expenses are, it is hoped, non-recurring in 2018 and beyond, so an adjustment was made to reduce Rate Year expense by the costs that occurred in 2017 and that will not be required going forward.

Rate Case Professional Fees

An adjustment for higher professional fees for rate case consulting and legal fees in the rate year of about $150,000 was embedded in rates. It is hoped that rate case external professional fees are unneeded after this rate case for several years, so a four-year amortization was proposed for these expenses.

Labor & Staff Salaries and Wages

As explained more fully in the testimony of Denise Sullivan, a new labor agreement was negotiated with SED's unionized employees calling for wage and benefit increases in the coming years, and non-union staff have been approved by SED's Board of Commissioners to receive a 3.5% increase next year. Only the increases in salaries and wages for 2018 were built into Rate Year rates, not the subsequent increases for 2019 & 2020 negotiated with the IBEW. This potential under-recovery beyond 2018 is another reason in support of Stowe's TIER request discussed in the next section.

Interest Expense Associated with New Capital Borrowing

Like with depreciation expense, interest expense associated with the capital borrowing for the two capital projects to be undertaken in 2018 as discussed in Ms. Burt's testimony and recently approved by the PUC earlier this year, is also built into the rate year cost to serve. This too represents a four-year average of interest expense for the Union Bank debt.

VI. TIER REQUEST

Q23. WHAT IS TIER?

A23. Unlike with investor-owned utilities that are approved to establish rates that afford them the opportunity to earn a return on rate base reflective of their weighted average cost of capital (i.e. a weighted blend of outstanding debt interest rates plus a return on equity for their common and preferred stock held by shareholders), public power utilities are allowed to build into rates a differently-calculated net profit or "return." For public power utilities, this return is calculated as a function of their rate year interest expense .

The calculation is known as the times interest earned ratio (TIER). The surplus built into rates is set to equal some multiple of rate year interest expense minus that amount of interest expense. So, for example, a TIER of 2.0 on a rate year interest expense of $500,000, would represent a TIER return of $500,000.[7]

Q24. WHAT IS SED REQUESTING FOR ITS TIER RETURN?

A24. SED respectfully requests a TIER of 1.25, which would result in a return or surplus to Stowe of 25% of its rate year interest expense.

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[7] [(Rate year interest expense of $500,000 X 2.0 = $1,000,000) - $500,000]

Q25. ON WHAT GROUNDS HAS STOWE BASED THIS REQUEST?

A25. This was the last PUC-approved TIER level in Docket 8074.

It is notable that, based on pre-filing discussions with the DPS, Stowe has learned that the two rural electric cooperatives in Vermont, Washington Electric Cooperative ("WEC") and Vermont Electric Cooperative ("VEC") have either requested in a recent rate filing or have been approved for TIER of at least 1.9. These are public power utilities that have been managed well, and SED ardently believes that it too has been well-managed and has secured for ratepayers the benefits that attend good management. Please refer to the testimony of Ellen Burt for a summary of SED's recent accomplishments and the benefits it provides ratepayers, including stable or decreasing rates since 2010, system improvements ranging from an economic utility-owned solar project, installation of smart meters, SED streetlights, and electric vehicle charging installations, timely storm restorations, and plans for construction of a new office building and garage, to name several.

Q26. ARE THERE ANY BOND COVENANTS OR OTHER LENDER REQUIREMENTS MANDATING A CERTAIN STOWE TIER OR DEBT SERVICE COVERAGE RATIO?

A26. SED is not aware of any such lender requirements.

Q27. DO STOWE CASH REQUIREMENTS SUGGEST IT WILL NEED A TIER OF AT LEAST 1.25?

A27. Yes. Denise Sullivan has testified as to the 45-day cash flow requirement of SED and has conducted analysis indicated that a TIER of at least 1.25 is needed to satisfy SED's cash requirements. Also, as described in the previous section, even though SED has proposed normalization adjustments to test year expenses that are based in some cases on as much as a four-year amortization, in virtually all of these cases the expenses SED will see in the coming years are escalating upwards. So, for the next two years, the total proposed expense reflected in SED's Rate Year revenue requirement will likely be less than the actual expense it incurs. This is true for some important items such as the LCP hedge transaction and associated transmission and specific facilities payments, SED capacity charges, depreciation and interest expense as new projects (which do not technically meet the known and measurable test) are eventually placed into service, and as labor and other salaries and wages increase beyond 2018.

Q28. WHAT IS THE REQUESTED TIER RETURN IN DOLLAR TERMS?

A28. SED is requesting $227,123 in authorized TIER return.

Q29. IF GRANTED THE REQUESTED RATE RELIEF, INCLUDING THE 1.25 TIER, WOULD THE RESULTING REVENUE REQUIREMENTS PUT STOWE ON A SUSTAINABLE RATE PATH?

A29. While there are no guarantees that SED will not need any subsequent rate relief sometime in the coming 2 to 4 years, SED's General Manager, Ellen Burt, and Controller, Denise Sullivan, are satisfied that the requested 7.9% rate increase would, together with other initiatives aimed at controlling costs, provide an opportunity for SED to avoid filing for another rate increase during that timeframe. Furthermore, the efforts made in this rate case to identify and amortize revenue and costs for items that decrease following the Rate Year, should likewise reduce the likelihood of SED requiring a rate reduction during that period. While nothing is certain, the requested rate increase and TIER request were designed to meet SED's minimum projected financial requirements.

Q30. PLEASE EXPLAIN THE PROOF OF REVENUE COMPLETED TO SUPPORT THE RATE INCREASE.

A30. A Proof of Revenue was completed to detail from a bottom up approach the rate revenue needed by SED. Our proof of revenue analysis, which is provided in Exhibit SED–Daymark–5, shows that we came within 0.5% of the Stowe's 2017 revenue.

VII. TARIFF CHANGES

Q32. WHAT CHANGES ARE PROPOSED TO THE EXISTING TARIFFS?

A32. In SED–Daymark–3, we provide redline and clean tariff sheets for all current tariffs. The proposed tariff changes are based on current labor and other costs of service. All the redlined tariff sheets show the resulting rate increases resulting from the proposed 7.9% rate increase and changes to the Effective Dates for service and billing. The list of tariff sheets contained in SED–Daymark–3 is as follows: Residential Rate 01, Residential Rate 03 – Time of Use & Critical Peak Pricing, Residential Storage Heating Rate 11, Small Commercial Rate 20, Large Commercial Rate 25, Interruptible Load Tariff, Street Light Rate 30, LED Street Light Rate 31, and Electric Vehicle Charging Station Rate 35. Additionally, tariff language was adjusted for the following rate classes:

- Rate 25 – The transformer discount is being corrected. It had been reduced by 3.5% to $0.457 in 2014 as the result of a scrivener's error, and now is being revised to $0.474 in this case to be consistent with the tariff prior to 2014. The transformer ownership discount is meant to credit customers who receive service under this rate and elect to purchase their own transformer at a primary or secondary voltage level thereby reducing SED's cost to serve that customer. There is no correlation between the utility's cost of service and the avoided cost that comes from the customer taking responsibility for the transformer so it should not have been changed in 2014.
- Rate 03 – The peak and off-peak descriptors were updated so that all periods started at the beginning of an hour and ended at the close of an hour (e.g. 4:00 pm to 7:59 pm). Previously, some of the periods started one minute after the start of the hour and ended at the close of the hour. For example, the Summer Off-Peak Hours were from 8:01 pm through 11:59 am of the next day. Although the summer peak period lasts sixteen hours each day in June through September, in effect the wording in the tariff would lead the reader to believe the period was fifteen hours and fifty-nine minutes.
- Interruptible Load – The language in the Effective Date section has been changed to be consistent with all of the other tariff sheets.

Q33. IS STOWE REQUESTING ANY CHANGES TO ITS MISCELLANEOUS (I.E. NON-RETAIL RATE) FEES?

A33. Not at this time. We are aware that Stowe is considering changes to the miscellaneous fees, but since these changes will not impact the revenue requirement they will be addressed at a later date.

VIII. CONCLUSION

Q34. COULD YOU PLEASE SUMMARIZE YOUR TESTIMONY?

A34. As discussed herein and in the testimony of SED's other witnesses, SED faces a generally increasing cost to serve over the coming years, over and above that embedded in its 2017 Test Year. Those costs and the corresponding adjustments to the Test Year cost to serve are described above and the testimony of Denise Sullivan; of particular note is the unwinding of the LCP hedge with various associated costs extending into 2019, while the Vermont Transco dividend income used to offset those costs over the last decade ends in 2018. Other factors include a generally higher transmission cost outlook, initially higher capacity costs that then begin to decline, higher depreciation expense and interest costs as new capital equipment gets placed into service, and higher salaries and wages. Importantly, SED implemented a 3.5% rate decrease in the 2013-2014 timeframe, which has also factored into the requirement for relief now.

SED has proposed a limited 7.9% rate increase, which will likely be sufficient to meet its needs over the coming several years, but will require SED to carefully monitor and contain costs over 2018 and 2019 to ensure it breaks even or earns some return during those years until it experiences lower costs to serve in 2020 and 2021.

Q35. ARE THE RATES PROPOSED BY SED HEREIN CONSISTENT WITH PUC RATEMAKING PRECEDENT AND ARE THEY JUST AND REASONABLE?

A35. In our opinion, yes. The costs and income adjustments contained in this filing are based on known and measurable changes from the 2017 Test Year. Costs and investments made in prior years received regulatory approval in most cases and met other key tests including that they were *prudent* and have been *used and useful* in serving SED ratepayers. To that extent, we believe the rate increase request is consistent with PUC ratemaking precedent for public power utilities in Vermont, and as shown herein, consistent with the model used in Docket 8045 to justify SED's last 3.5% reduction in rates. Therefore, the rates established using the Rate Case Model contained in Exhibit SED–Daymark–4, as reflected in the revised tariffs contained in Exhibit SED–Daymark–3, serve the public interest and we believe they are just and reasonable.

Q36. DOES THIS CONCLUDE YOUR TESTIMONY?

A36. At this time, yes.

<u>EXHIBIT LIST</u>

Exhibit SED–Daymark–1	Resume of Stan Faryniarz
Exhibit SED– Daymark–2	Resume of Matthew Loiacono
Exhibit SED– Daymark–3	Marked and Clean Revised Tariff Sheets
Exhibit SED– Daymark–4	Rate Case Model
Exhibit SED– Daymark–5	Proof of Revenue