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 DENISE SULLIVAN
ON BEHALF OF
THE TOWN OF STOWE ELECTRIC DEPARTMENT

Summary of Testimony

Ms. Sullivan's testimony in support for the Town of Stowe Electric Department's 2018 Rate Case provides SED's Test Year cost of service, explains the adjustments made to certain income and expenses items to arrive at SED's Rate Year cost of service, and discusses the process of normalizing certain income and expense items that will change subsequent to 2018. Ms. Sullivan also discusses the impact of the proposed rate increase on SED's projected cash position over the next four years.

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PREFILED DIRECT TESTIMONY
OF DENISE SULLIVAN
ON BEHALF OF STOWE ELECTRIC DEPARTMENT

Q1. Please state your name and occupation and business address.

A1. My name is Denise Sullivan. I am the Controller of the Town of Stowe Electric Department ("SED"). I began working at Stowe Electric Department in December 2017. My business address is 56 Old Farm Road, Stowe, VT 05672.

Q2. Please describe your educational background and work experience.

A2. I earned a Bachelors degree in Accounting from the University of Georgia and a Masters in Management from Georgia Institute of Technology. I have held a license to practice as a Certified Public Accountant in the state of Vermont since 2005. I am a Certified Fraud Examiner and a Certified Internal Auditor. I have owned and operated a CPA firm in St. Johnsbury, Vermont since January 2015.

In my previous position, I served as Vice President of Finance for Equity Services, Inc., a National Life Group company, and as Assistant State Auditor for the State of Vermont. Resume provided as Exhibit SED–DS–1.

Q3. Have you ever testified before the Vermont Public Utility Commission?

A3. Yes. I previously testified in Case No. 18-0123-PET with respect to SED's request for approval under 30 V.S.A. § 108(c) to finance certain 2018 capital projects.

Q4. What is the purpose of your testimony?

A4. I will discuss SED's Test Year ("TY") 2017 operating results and cost of service and the adjustments made to various TY income and expense categories necessitated by non-recurring items during the 2018 calendar year to arrive at SED's Rate Year (aka "Adjusted TY") cost of service. I will also explain how and why certain income and expense items were normalized based on known and measurable changes that will occur beyond 2018. Lastly, I will discuss SED's cash position coming out of the TY and projections of its cash position in the ensuing three years with and without the rate relief requested.

Q5. Please discuss the features of the 2017 Test Year, and any extraordinary items that affected SED financial performance during the Test Year.

A5. As discussed in the testimony of Ellen Burt, there were several items that affected SED's financial performance during the 2017 Test Year. SED's audited 2017 financial statement show that SED experienced a 4.3% decrease in retail sales across all customer classes. It also tallied approximately $350,000 in damages from a single storm event in late October 2017. The event qualified for emergency relief and SED has applied for relief from the Federal Emergency Management Agency ("FEMA"). Though not yet known or measurable, SED accrued a receivable and offset (i.e. reduced) 2017 operating expenses by the amount of estimated relief. SED also made several capital acquisitions during 2017, including an approximately $900,000 purchase of an additional ownership interest in the Highgate Converter, and incurred new debt to fund the purchase of Membership Units in Vermont Transco, LLC ($825,000, as approved in Docket No. 8868). SED's financial performance during the 2017 Test Year and the factors influencing that performance are discussed more fully in SED's audited financial statements attached as Exhibit SED–DS–2.

Q6. Please identify and discuss the adjustments made by SED between the 2017 Test Year and the 2018 Rate Year, and explain what expenses were normalized based on known and measurable changes that will occur beyond 2018.

A6. Going forward into Stowe's 2018 Rate Year, there are certain non-recurring income and expenditures that are expected to further affect cash flows. Adjustments made in the Rate Case Model incorporate SED's power supply and transmission budget prepared by Energy New England, LLC's ("ENE") (see prefiled testimony of Timothy Hebert and Exhibit SED–TH–2) and all known and measurable increases from year to year. The specific adjustments are identified in the Rate Case Model attached to the testimony of the Daymark Panel Exhibit SED–Daymark–4 and I will describe them below.

A handful of items, based on known and measurable changes that will occur beyond 2018, were "normalized" in order to spread inter-period costs and levelize rates over the normalization period with the hope of averting an additional rate case within the next few years. Many of the normalized expenses relate to the unwinding of the Lamoille County Project ("LCP") Specific Facilities Settlement (discussed below), including Dividend revenues in Adjustment 3, Miscellaneous Non-Operating income in Adjustment 4, Significant Non-Recurring Income in Adjustment 5, Specific Facility Fixed Payments in Adjustment 7 and Specific Facilities contributions in Adjustment 17. A period of four years was selected for the normalization period for the reasons explained in the testimony of the Daymark Panel.

Below I describe each adjustment made between the Test Year and the Rate Year and explain, if applicable, whether the adjustment was normalized and how. The first five adjustments are to income, while the remainder are to expenses:

Adjustment 1: Residential Energy revenues are projected to increase by $18,358 due to new customer installations.

Adjustment 2: Commercial Energy and Demand revenues are projected to increase by $18,569 due to a new Stowe Cider cidery installation.

Adjustment 3: As discussed more completely below, Transco Dividends from SED's LCP Membership Units will end in 2018 after the LCP Membership Units are resold to Transco. 2018 dividend revenues will be $2,339,059 with none to follow in subsequent years. The revenue reduction is normalized over four years resulting in a reduction of $1,754,294 in the Adjusted Test Year down to $584,765.

Adjustment 4: Misc. Non-Operating Income in 2018 was $240,000. This income represents the amortization of a gain on hedging and amortization of the ten-year Spruce Peak/Stowe Mountain Resort contribution towards the LCP which will end in 2019. For the Adjusted TY, the two years of revenue were normalized over a four-year period and, therefore, include Adjusted TY income of $120,000. This represents a reduction of income in the Adjusted Test Year of $120,000.

Adjustment 5: Stowe received significant non-recurring income in April 2018 of $255,000. This income represents Vermont Transco, LLC's distributed earnings from the sale of its joint-venture interest in the Utopus analytics program. Transco plans to release currently escrowed funds during 2019 in the amount of $40,000. For the Adjusted TY, we normalized the two years of revenue over a four-year period and, therefore, include Adjusted TY income of $73,750.

The following adjustment were made to the Adjusted TY expenses:

Adjustment 6: ENE's power supply and transmission budget projections were used to populate the Power Costs section of the Normalized Profit and Loss statement. As shown in Exhibit SED–TH–2 to the testimony of Timothy Hebert, ENE's budget for the Rate Year shows energy costs are higher by $316,225, offset in part by higher REC Credits of $53,073 for a total Energy Cost increase of $263,152, Snowmaking costs are higher by $78,326, and transmission expense is higher in 2018 by $260,485. These adjustments have been included in the Adjusted Test Year.

Adjustment 7: LCP Specific Facility payments required under the Lamoille County Project (described more particularly below) are $1,100,000 in 2018 and 2019 when they end. To reflect the decreasing/elimination of that expense in future years, a four-year average of the expense was used, decreasing expenses in the Test Year by $550,000 to $550,000.

Adjustment 8: As discussed in Mr. Hebert's testimony, SED capacity costs are decreasing after 2018 through 2021. A four-year average was used to reflect these decreasing costs. Other Charges from ISO-NE and ENE's Consulting Fees increased in the 2018-2021 ENE budgets. Because these items are known and measurable, the Test Year includes the amounts budgeted by ENE.

Adjustment 9: Depreciation increases by $40,305 representing full-year depreciation for assets acquired during 2017 and incremental depreciation on the capital projects expected to be completed during the 2018 calendar year.

Adjustment 10: O&M Expense – Solar project operations and maintenance was increased by $6,815 due to negotiation of a solar maintenance contract with Namaste Solar.

Adjustment 11: Contract Services during 2017 were primarily related to Mutual Aid services provided by contractors during the October 2017 storm. Because they are expected to be non-recurring, these expenses were decreased by $71,018.

Adjustment 12: SED and its unionized employees negotiated and the IBEW ratified a three-year contract in late May 2018. This contract established wage increases of 4% in 2018 and additional increases in subsequent years. Only the 4% increase in 2018 was embedded in Rate Year expenses. The TY employment-related accounts include: Salaries, Wages, Payroll taxes, fringe benefits and Pension plan costs. Year to date payroll summaries through May 31, 2018 serve as the foundation for the TY. This summary was projected forward to current year end to estimate the year-end payroll expenses. The 2017 System Labor expenses benefitted from the accrual of payments due from mutual aid billings and a FEMA accrual. This offset is not anticipated for future years. As a result, Total Cost of Sales is $124,153 higher in the TY at $1,665,618.

Adjustment 13: A series of adjustments were made to transmission expenses related to Stowe's share of the Highgate Converter asset. SED plans a sale of its share of Highgate ownership to a merchant transmission owner in 2018, as described in the testimony of Ms. Burt. To reflect the fact that ownership-related expenses and use rights will cease following that sale, test year expenses (other than payroll taxes and benefits) were reduced by half and use rights end. Payroll taxes and benefits are a calculation based on actual year to date expense percentages as related to salaries and wages. Rate Year expenses drop by $181,561 from the 2017 Test Tear.

Adjustment 14: At the end of 2017, Finance & Administration operated with two open positions, resulting in lower Wage expense. These positions were filled in early 2018. In 2017, paid time off represented the payout of accumulated vacation for departing employees; this expenses is not anticipated in the Rate Year. Raises in varying amounts were given to non-union employees up to 4%. As a result of these two offsetting changes, the Test Year Wages and associated Fringe Benefits for Finance & Administration are lower by $8,468.

Adjustment 15: IT Costs in 2017 were higher than average due to the cost of running two systems in parallel during the implementation of a new billing system. IT Costs are budgeted to be lower in 2018 and years forward by $45,398.

Adjustment 16: Combined Professional Fees are projected to be $85,000 higher in the TY for rate case consulting.

Adjustment 17: The LCP settlement will end in 2019 after one more year of Interest Expense of $1,080,704 and two more years of Arbitrage payments of $1,258,354. As a result, the Adjusted TY has been normalized over a four-year period resulting in reduced interest expenses of $540,352 and reduced arbitrage payments of $629,177.

Adjustment 18: Interest expenses are $62,235 higher in the Adjusted TY due to new debt for the 2017 and 2018 Transco equity purchases as well as new debt for the 2018 Capital Projects.

Q7. You have listed several adjustments relating to the unwinding of the Lamoille County Project Settlement. Please explain those adjustments in more detail.

A7. The adjustments to income and expenditures associated with the Lamoille County Project ("LCP") are central to SED's need for a rate increase at this time. The LCP Uncontested Settlement Agreement[1] required Stowe Electric Department to purchase 1,870,000 LCP Member Units from Transco at $10 per unit. To facilitate the purchase, Stowe was approved in Docket No. 7458 to issue $18.7 million in indebtedness with a term of ten years. The LCP Member Units were to be held by Stowe for a period of ten years, then sold back to Transco at the original offering price, fully retiring the Member Unit Financing. The Settlement also required Stowe to pay its portion of the annual contribution of Specific Facilities[2] components of the Project but limited those payments to the margin between the return on equity ("dividend") and the cost of Member Unit financing. This agreement is vernacularly termed the "hedge" by parties involved.

In fulfillment of the Settlement, in December 2008, Stowe borrowed $18.7 million from Keybank, purchased the $18.7 million of Member Units, and began paying both interest payments to Keybank and Specific Facilities annual contribution payments to Transco.

[1] The Uncontested Settlement Agreement was approved by the Federal Energy Regulatory Commission ("FERC"), Docket No. EL07-11-000, *et al*, on August 22, 2008.

[2] The term "Specific Facilities" is defined in Article IV of the 1991 Transmission Agreement as "those high-voltage transmission lines, substations and other appurtenances constituting a direct physical interconnection to the VT Transco system and not constituting part of VT Transco's looped transmission facilities, that are requested, used, and installed to benefit a requesting Purchaser of transmission service . . ."

However, the LCP Specific Facilities were late going online. Transco could not charge for Specific Facility payments until the Specific Facility was placed in service at the end of 2009 making it "used and useful". The delay created a mismatch in the timing of the hedge. The Member Units will be resold back to Transco and dividends will cease in December 2018, a full year before the Specific Facilities payments end in December 2019. In addition, fixed Specific Facilities payments of $1.1 million are due annually through calendar year 2019. These expenses, which for the past nine years have been offset by the Transco dividend annual revenue of $2.34 million, are equivalent to 16% of SED's annual operating budget and are the largest contributor to SED's need for a rate increase at this time.

Q8. Please discuss SED's cash flow during the period 2018 to 2020.

A8. Exhibit SED–DS–3 contains cash flow projections with and without the requested rate increase; Exhibit SED–DS–4 contains SED's four-year debt service schedule; and Exhibit SED–DS–5 contains SED's four-year capital spending plan.

As, Exhibit SED–DS–3 demonstrates, even with the proposed rate increase, SED will be forced to operate in a cash-constrained manner during 2018 and 2019 until the increased transmission expenses abate and income and cash flow improve. In the analysis, net income has been adjusted for non-cash items, such as depreciation and the Spruce Peak contribution to the LCP, and for several items not included in the rate model because they are not known or measurable, such as the anticipated FEMA contribution to storm expenses. The resulting deficits in 2018 and 2019 and surplus in 2020 yield a three-year average net decrease to cash flow of ($188,107). Ellen Burt discusses in her testimony why SED has limited the amount of its rate increase in the manner it has and why SED is confident it can meet its financial obligations in the near term despite this average net decrease to cash flow.

The 7.9% rate increase is needed to ensure SED can meet its obligations as they come due and to fund operations in years 2019 through 2021, including the servicing of existing debt and continuing to make planned capital improvements. The rate increase will also help replenish the cash deficits that occur in 2018 and 2019 by creating a cash surplus in the latter years, 2020 and beyond.

Based on annual expenses of $14,808,311 in 2017, SED's 45-day operating expenses are approximately $1,825,682. SED does have the ability to borrow up to $1.5 million against its line of credit and plans to utilize this line of credit as necessary to mitigate its anticipated cash shortage and meet operating expenses in the near term— in particular, during 2018 and 2019. As discussed further in the testimony of Ellen Burt, so long as SED continues to be prudent and responsible, it can manage its cash flow and meet its financial obligations in the near term.

Q9. Does this conclude your testimony?

A9. Yes; thank you.

EXHIBIT LIST

Exhibit SED–DS–1	Resume
Exhibit SED–DS–2	2017 Audited Financial Statements
Exhibit SED–DS–3	Three-Year Projected Cash Flow (2018 to 2020)
Exhibit SED–DS–4	Four-Year Debt Service Schedule
Exhibit SED–DS–5	Four-Year Capital Spending Projections