



GREEN MOUNTAIN POWER

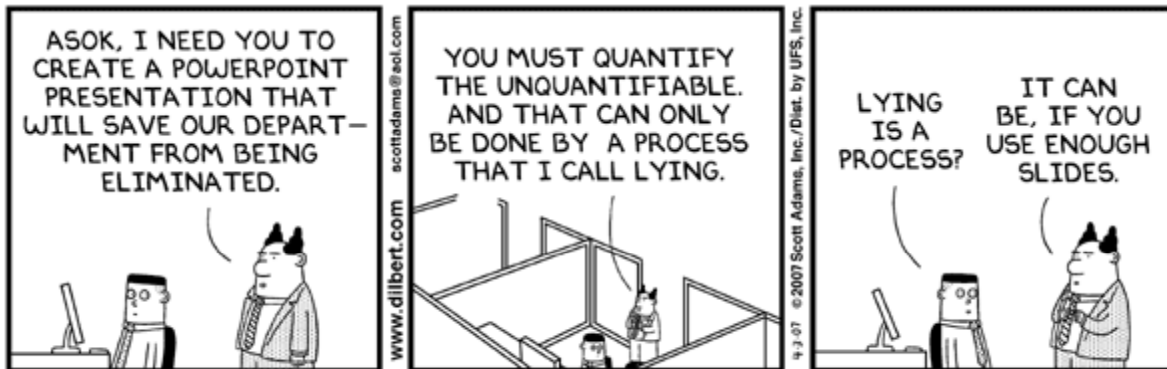
Panel # 3 - Revisiting Capital Structure Issues in Ratemaking

Tony Kvedar

SURFA

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Recovery of Cost of Capital

- *A key financial* concern of Utility companies is recovery of cost to service customers
- Identification of risk components that affect the cost of capital to quantify the appropriate cost of capital is the primary goal.
- Work product provided by credit rating agencies is extremely helpful.
- The identification of *net* risk that *PPAs transfer* as a substitute for owned generation is important.

Key Issues in New S&P Method

- 1. Change in Discount rate to calculate imputed debt.
- 2. *Value* of applied discount if utility has a fuel adjustment clause.
- 3. Ever greening PPAs of less than three years.
- 4. Change in calculating capacity costs when there is all in energy price.
- 5. Implied depreciation expense is added to calculate FFO.

Change discount from standard 10% to average costs of debt

- 1. *Could* lead to inconsistent and non comparable results.
- 2. Using strictly a debt rate is not best way to measure a stream of capacity payments
- 3. Average debt costs do not equate to marginal costs of capital. WACC makes more sense.
- 4. *Biases* utilities *with* outstanding tax-exempt debt issuances.

Ever greening Contracts of less than Three years

1. S&P revised approach in final draft. Utilities appreciate this response to the feed back provided.
2. Updated approach is more company specific.
3. Companies utilize short term contracts for different reasons.
 - a. Short term contracts employed for various reasons. Like short term debt is employed for different reasons. Could be a bridge to building a generating plant.
 - b. Contracts may be short term due too uncertainty concerning future load responsibilities.
 - c. Contracts may be short term to avoid locking into a long term contract with a high costs.

Capacity Adjustment

1. Was the One for One assumption reasonable?
2. Is prevailing capacity for the development of new generation always reflective of market capacity costs?
3. Does this method take into consideration the market price of purchase power?
4. If the intent is to factor in the low fuel costs such as wind or nuclear, what about the avoidance of O&M risk on the nuclear plant.
5. What if the contract is take and pay and the unit doesn't perform the utility has to substitute power purchased from the market, but avoids the operational costs

Depreciation Adjustment

1. Clarified more in recent letter.
2. Including a depreciation adjustment makes sense.

Different Business Needs

- 1. Decision to buy instead of build may be a function of business realities not strictly an economic decision.
- 2. Small Utilities can not build base load units and maintain a diversified portfolio.
- 3. Siting generation may be problematic.
- 4. Sell owned generation and take back a PPA to reduce operational risk and hedge fuel risk.