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June 17, 2008

Luly Massaro, Clerk
Public Utilities Commission
89 Jefferson Boulevard
Warwick, RI 02889

Re: Block Island Power Company General Rate Filing – Docket 3900
Response to Letter from Alan Mandl, Esq. dated June 10, 2008

Dear Luly:

As requested by the Commission, as legal counsel to Block Island Power Company (BIPCo), I am writing to respond to the June 10, 2008 letter to you from Alan Mandl, Esq., legal counsel to the Town of New Shoreham (Town).

1. The June 10 letter cannot be considered as part of the record in this proceeding and should be stricken from the record.

Commission Rule 1.20 (m) provides in pertinent part as follows:

> "The record in a proceeding shall close after the briefs, if any, have been filed, or otherwise after the dispositive open meeting, and thereafter there shall not be received in evidence or considered as part of the record any document, letter or other evidence submitted except as provided in Rule 1.20(i) [further evidence requested by the Commission at the hearing], changes in the transcript as provided in Rule 1.23(b) [hearing transcript corrections], or as otherwise stipulated by the parties with the agreement of the Commission." (Emphasis added.)

Because (1) the briefs were filed before June 10, and (2) the dispositive open meeting at which the issues were ruled on was concluded before June 10, the June 10 letter filed on behalf of the Town may not be either received in evidence or "considered as part of the record" in this proceeding. It is therefore a nullity and should be stricken from the record.

2. The Commission's power to substantively act has ended.

Under R.I.G.L. § 39-3-11, the Commission has the authority "to suspend the taking effect of the change or changes" proposed by BIPCo, pending the Commission's decision, but not for longer than seven (7) months from the date of the rate change filing (automatic 30 days plus an additional six months). At the end of this 7-month period of time, the Commission no longer has any statutory power to prevent the taking effect of any changes proposed by BIPCo if the Commission has not formally acted on those proposed changes at an open meeting within the 7-month period. This rate case was filed by BIPCo on November 9, 2007. Accordingly, the Commission's power to alter the filing by making adjustments thereto ended no later than on June 9, 2008. The Commission's substantive open meeting in this matter was held on May 29, 2008. The Town's letter was not sent to the Commission until June 10, 2008, and this was after the 7-month statutory period expired. Therefore, the Commission is without jurisdiction to take any of the actions requested by the Town in its June 10 letter.

It is for this reason that Rule 1.26(a)(3) provides:

> "The Commission will not consider any motion to reopen the record filed within ten (10) days before the expiration of a final suspension order in a proceeding initiated by a general rate change filing."

In other words, if a party wishes to file a motion to reopen the record, it must do so more than 10 days before the expiration of the suspension period or the motion cannot be considered by the Commission because the Commission has no authority to substantively act after the suspension period ends.

3. The June 10 letter is not a proper Motion requesting relief.

The Town's June 10 letter is also a nullity because it was not properly filed as a Motion as required by the Commission Rules. The letter does not meet the filing requirements of Rule 1.5 (Formal Requirements as to Filings) or Rule 1.15 (Motions). In fact, in footnote 1 of the June 10 letter, the Town states that "by submitting this letter, the Town does not waive any right it may have to submit a motion following a written order or to petition for a writ of certiorari." In making this statement, the Town concedes that the letter is not a Motion. However, under Commission Rule 1.15, "any application to the Commission to take any action or to enter any order" must be made by filing a motion which complies with the requirements of Rule 1.15 and Rule 1.5. The June 10 letter does not meet any of those requirements. Therefore, the letter cannot be considered as an appropriate request for Commission action. Such a request can only be made by way of a Motion.[1]

[1] BIPCo feels that this letter is simply a second attempt, not sanctioned by any Commission Rule or the procedural schedule in this docket, to reargue the same points the Town made in its post-hearing brief. If the Town is aggrieved by any of the Commission rulings made at the May 29 open meeting, then any remedy would be to file an appeal with the Supreme Court; the suspension period was over by the time the June 10 letter was filed and the Commission is not in a position to take any further substantive action as requested by the Town in its letter. In BIPCo's opinion, the only thing left for the Commission to do at this point is to rule on BIPCo's compliance filing and then issue the appropriate Report and Order.

4. The Commission did not act "contrary to law" when it ruled that BIPCo was not required to file written employment contracts with its owners/officers.

Nothing in Title 39 requires the filing of employment contracts. It is true that, because BIPCo's owners/officers are the holders of 10% or more of the voting capital stock of BIPCo, they must file either a copy of such contracts (if such contracts exist) or, if no such contracts exist, then BIPCo must simply file a "summary of any unwritten contract or arrangement" as set forth in R.I.G.L. § 39-3-28. No such written contracts exist.

The filing of a "summary of any unwritten contract or arrangement" is a far cry from having the Commission mandate that BIPCo must enter into employment contracts with its owners/officers. BIPCo has, on repeated occasions, filed a "summary" of the "unwritten contract or arrangement" between BIPCo and its owners/officers. In each rate case filed by BIPCo in recent years, BIPCo has set forth the exact sums paid to the owners/officers and has described in each recent case the duties and responsibilities of each of the owners/officers. Such filings clearly comply with R.I.G.L. § 39-3-28.

These filings include a filing made pursuant to a Commission Order dealing specifically with management compensation. In Docket 3655, the Commission issued an Order stating that "within ninety (90) days following the issuance of the Commission's written order in this docket":

> "BIPCo will justify, how it pays its owners and/or management (management fees, management salaries, dividends, director's [sic] fees, use of Company-owned or leased vehicles by owners and/or management, benefits provided to owners and/or management, etc., or some combination, and any other management-related transactions with affiliates) and show that its approach and the resulting payments are reasonable and in the best interest of ratepayers."

BIPCo complied with this Order, and as stated in the Compliance Order No. 18570 issued by the Commission on April 17, 2006:

> "Accordingly, on December 12 2005, ninety days following the issuance of Commission Order No. 18364, BIPCo filed four documents ("Compliance Filing"): (1) Prefiled compensation compliance testimony of Walter E. Edge, Jr., MBA, CPA; (2) An analysis of executive compensation at the Block Island Power Company performed by Matthew M. Bodah, Ph.D., dated November 30, 2005; (3) Resume of Matthew M. Bodah; and (4) Block Island Power Company position descriptions for President, Chief Operating Officer, Secretary-Treasurer, and General Manager dated December 1, 2005."

The Commission reviewed BIPCo's filing, and the Town's opposition thereto, and ruled as follows:

> "1. The Town of New Shoreham's Motion for Summary Rejection of Block Island Power Company's Management Compensation Compliance Filing or in the Alternative, for an Investigation of Block Island Power Company's Management Compensation Payments and Practices is hereby denied.
>
> 2. Block Island Power Company's Compliance Filing dated December 13, 2006, [sic] is hereby accepted for filing.
>
> 3. Nothing herein precludes the Commission from further investigation into the executive compensation of BIPCo at a future date."

Again, in the subject docket 3900, the amount of compensation paid to BIPCo's owners/officers was set forth in detail in the cost of service schedules and testimony provided by BIPCo's witnesses David Bebyn, CPA (test year) and Walter E. Edge, MBA, CPA (rate year). In addition, Mr. Edge's rebuttal testimony included an updated management compensation report prepared by Dr. Bodah, once again setting forth in detail the job duties of each of the owners/officers and concluding that their compensation was reasonable.

Accordingly, it is beyond dispute that BIPCo has complied with R.I.G.L. § 39-3-28 by filing summaries of the unwritten contracts or arrangements between BIPCo and its owners/officers.

5. The Commission closely scrutinized the $1,000 per month pension payment to Mr. Edwards, its retired president, and therefore complied with the law.

The Town incorrectly argues that the case of Town of New Shoreham v. Rhode Island Public Utilities Commission, 464 A.2d 730 (RI 1983) requires the Commission to reject the $1,000 per month pension payment to Mr. Edwards "as an improper affiliate transaction." In fact, the Town's letter specifically (and incorrectly) claims that the Supreme Court "rejected this very type of payment." The Town is wrong.

The Town of New Shoreham case did not reject the $12,000 per year payment to Mr. Hutchinson. The Court simply ruled that the payment to Mr. Hutchinson, which was made pursuant to a consulting fee agreement, needed to be remanded back to the Commission, to "closely scrutinize the consulting-fee payment and determine whether or not it is properly includable as an operating expense." (at 737). Therefore, the Court did not "reject this very type of payment as an improper affiliate transaction" as the Town incorrectly argues in its letter. The Court simply said that the Commission must "closely scrutinize" the payment. This Commission, at its May 29 open meeting, did exactly that. In its first vote, the Commission denied BIPCo's request for a $24,000 pension to Mr. Edwards. In a second vote, the Commission approved a $1,000 per month pension to Mr. Edwards, which was in accordance with BIPCo's pension policy under which Mr. Edwards qualified.

In addition to having misstated the Supreme Court holding, the Town has failed to point out in its letter that there are significant distinctions between the $12,000 per year consulting fee payment to Mr. Hutchinson and the $1,000 per month pension to Mr. Edwards that was approved by the Commission. The distinctions include the following:

1. This Commission "closely scrutinized" the pension payment to Mr. Edwards before it was approved.

2. The $1,000 per month payment to Mr. Edwards that was allowed by the Commission was pursuant to an existing pension policy for BIPCo's long-time employees, whereas there was no such pension policy agreement in existence at the time of the 1983 Town of New Shoreham case.

3. The payment for Mr. Hutchinson was a consulting fee payment and was not a pension payment; whereas the payment to Mr. Edwards was a pension payment.

4. As the Supreme Court stated in the Town of New Shoreham case (but which the Town failed to point out):

> "As a general rule, employee pension plans are properly includable as an operating expense. 1 Priest, Principles of Public Utility Regulation, 108-109 (1969); Welch, Preparing for the Utility Rate 225 (1954). It cannot be gainsaid that social and economic advantages of pensions for superannuated employees exist. The commission should treat these expenditures as proper operating expenses because 'the benefits which the company obtains from a pension plan in freeing the lines of promotion, and improving the morale and efficiency of employees, necessarily result in definite though indirect economic benefit to the company's subscribers.' Re: Southern Bell Telephone & Telegraph Co., 92 P.U.R.N.S. 335, 346 (Fla. 1952). See generally Re: Utility Employee Pension Costs, 93 P.U.R.N.S. 159, 160 (N.Y. 1952)."

Accordingly, the $12,000 pension approved by the Commission, after "closely scrutinizing" the request and taking into account BIPCo's pension policy, was lawful and reasonable and did not in any way violate the Town of New Shoreham case.

STANDARD OF REVIEW

With regard to the other issues raised in the Town's June 10 letter, it is important to consider that the legal standard of review of a Commission Report and Order is that the Commission's ruling will not be set aside unless they are "unlawful or unreasonable" (R.I.G.L. § 39-5-1). Great deference is paid by the Supreme Court to Commission decisions when the Commission acts in its ratemaking-regulatory capacity. Blackstone Valley Electric Co. v. Commission, 543 A.2d 253 (RI 1988), cert. denied, 488 U.S. 995 (1988). Many cases have held that the role of the Supreme Court in reviewing a Commission decision is limited to determining whether the

Commission's findings are lawful and reasonable, fairly and substantially supported by legal evidence, and sufficiently specific to enable the Court to ascertain if the evidence upon which the Commission based its findings reasonably supports the result. See for example, Roberts v. New England Tel. & Tel. Co., 487 A.2d 136 (RI 1985); Valley Gas Co. v. Burke, 518 A.2d 1363 (RI 1986); Interstate Navigation Co. v. Burke, 465 A.2d 750 (RI 1983); New England Tel & Tel Co. v. Commission, 446 A.2d 1376 (RI 1982); United Transit Co. v. Public Utilities Hearing Board, 192 A.2d 423 (RI 1963).

In this regard, it is important to note that the Town did not support the alleged "material issues raised by the Town" (as itemized in its June 10 letter) in the Town's direct or surrebuttal testimony of its witness. By the Town's own admission in its June 10 letter, the Town addressed these the six (6) issues only "during cross-examination of Company witnesses and on brief." (at 2). This is simply insufficient as a matter of law to establish an evidentiary record in support of the Town's arguments set forth in its June 10 letter, especially when the cross examination of BIPCo's witnesses referred to by the Town did not support the positions taken by the Town in either its post-hearing brief or in its June 10 letter. The failure of the Town to put on supporting testimony with its witness dooms the Town's arguments due to lack of proof.

The following comments relate to the Town's incorrect allegation that the Commission failed to deliberate regarding several material issues raised by the Town during cross-examination of BIPCo's witnesses and on brief.

Initial Observations:

- The six items specifically listed in the June 10th Town letter were never raised by the Town's expert witness. Therefore, the Town's affirmative position on these issues was never set forth in the record.
- The Town attempted to put these items on the record through cross-examination of BIPCo's witnesses and failed.
- Most of the items listed are not material in nature despite of the Town's characterization that they are material.
- The Town's brief is not evidence. The Town tried to make its position on these issues through a few questions and answers that did not draw a conclusion contrary to the evidence already on the record. The Town's attempt is simply too little, too late.

1. **The Town continues its incorrect representation that the Company can not pay rent for the use of the second floor of the office building despite being told by Mr. Edge on cross-examination that the second floor was never included in BIPCo's rate base and therefore is a non-utility asset owned by the stockholders (tr. 5/8/08, at 65).**

   Mr. Edge was asked "And I believe we can recap one of your discovery answers. You had originally included $5,000 as annual expense for the transaction but upon review realized that it should have been $12,000, correct?" To which Mr. Edge responded "That's correct. It is the rent for the second floor of the office building which is not

included in our rate base, and therefore, we pay rent to use the second floor at $1,000 per month."

During subsequent cross-examination on this issue, the Town tried to establish that BIPCo could simply move the asset from non-utility plant to utility plant and stop paying the rent. This questioning shows that the Town understood that a step would have to be taken (moving the asset to a utility asset) before the Town's suggested treatment could make any sense. (Of course, this position is 100% opposite the Town's position on the proper use of the proceeds of the land transfer.)

BIPCo's stockholders paid for the second floor of the office building and therefore it is owned by the stockholders. From the beginning, the Commission did not allow the second floor in rate base. Therefore, it is fundamentally incorrect to think that BIPCo's stockholders should now, after many years of supporting this asset, simply transfer the second floor to a utility asset to save the ratepayers $1,000 per month in rent.

The Town's position that "the Commission should direct the reclassification of this portion of the office building to utility plant in service at its original cost of $20,666, less any accumulative depreciation, and remove the test year rental expense of $5,000" is not only too little, too late, it is also unreasonable in the extreme. The Town failed to address the legality of the transaction or answer 1) why would the accumulated depreciation (not paid by the ratepayers) be deducted from the original cost, and 2) why wouldn't the asset be transferred at its fair market value? The Town did not sufficiently develop this issue on the record. As a result, the Commission cannot take the action suggested by the Town in its brief.

2. **The Town has failed to understand the status on the record of the "amortization of the cost of studying alternative methods for reading meters" issue. The Town's proposal to make either a $10,000 elimination adjustment or an $8,000 amortization adjustment fails to recognize that the balance in this account on the record is only $3,333.**

In its prefiled testimony BIPCo filed for a $10,000 allowance to study the alternative new meter reading options available to the Company (See Schedule WEE-3, page 2 of 4). The Division filed pre-filed testimony that reduced BIPCo's request by $6,667 ($10,000 amortized over three years-see Schedule DJE-3), resulting in a recommended allowance for the rate year of $3,333. BIPCo accepted the Division's adjustment (See Schedule WEE-3, page 2 of 4 in BIPCo's rebuttal testimony).

The Town should have been aware of these facts. In fact, the Town even cross-examined Mr. Edge on this issue as follows:

> "Q. All right. You're aware that the Division has questioned the proposed $10,000 adjustment for the cost to study the best way for the company to read its meters, correct?

A. I'm sorry. I don't know what the beginning of that sentence was. Did you say they opposed it?
Q. Well, they questioned it.
A. Questioned it. I believe the correct statement would be that the Division accepted it, however, felt that it should be amortized over three years." (tr. 5/8/08, at 97).

Clearly the Commission could not accept either of the Town's two adjustments because you can not subtract either $8,000 or $10,000 from the record amount of $3,333.

3. **The Town recommends the elimination of the hazardous waste clean-up costs included in the test year ($13,999) by stating that the cost are non-recurring and references the response to data request Town #98. The response to Town #98 does not say that this expense is non-recurring.**

BIPCo incurred hazardous waste clean-up costs in the test year and the two preceding years. Even if the specific hazardous clean-up cost of the test year is non-recurring, one can not conclude that there will be no hazardous waste clean-up cost in the rate year. The fact that the Town never presented this issue through its own expert witness and further did not establish that there would be no hazardous waste clean-up costs in the rate year is once again too little, too late to be considered by the Commission.

4. **The Town is incorrect in its facts and its conclusion relating to the normalization of directors' expense.**

The Town stated in its brief that BIPCo spent $2,500 per year in FY 2005 and FY 2006. In fact, BIPCo spent $2,500 in FY 2006 but actually spent $4,355 in 2005 (See Schedule DGB-2, page 3 of 5). In addition, the concept of normalizing this account was never raised on the record. The only probative cross examination question on this issue was as follows:

"Q. Would you agree that over the five year period shown, that number [the test year expense] is the highest number.
A. I would agree." (tr. 5/9/08, at 66.)

The Town does not explain why it is appropriate for this account to be normalized. Further, the Town never explained in their proposal that the increase in the test year was the result of BIPCo's new finance committee meetings implemented by the President to better control costs. BIPCo has no intention of eliminating these budget meetings because they have provided better control over expenditures. The Town is wrong in suggesting that this account should be normalized.

5. **The Town is incorrect in its proposal to amortize the test year revenue from Verizon and Block Island Cable for back payments "paid by the ratepayers". The ratepayers have not paid for Verizon and Block Island Cable back payments**

because this is a revenue collection account not an expense account paid by the ratepayers.

In fact, in the last docket, the rates were calculated using an annual allowance for the Block Island Cable pole rentals, giving the benefit of this activity to the ratepayers as a reduction of revenue requirement. The Verizon revenue recovery is for pole replacement. Neither of these two activities should be amortized back to the ratepayers.

The test year activity in this account is a cash flow item and not a test year earned revenue item. BIPCo did not accrue the revenue for this activity until it was identified in the test year but it was earned in previous years. The fact that the Block Island Cable revenues were addressed in the last rate filing and the Verizon revenue is the recovery of capital costs shows that the Town's proposal is incorrect.

Once again this issue was not fully presented on the record by the Town. The Town's expert witness did not opine on the record relating to this issue, and BIPCo never agreed that the cash received for prior years should be amortized back to the ratepayers (in fact that concept was never raised except in the Town's brief, which is not evidence). In addition to the above listed points, BIPCo believes that the amortization of these past amounts into the future would be retroactive ratemaking and therefore not appropriate for this docket.[2]

The calculations in the Town's brief on these issues were never presented on the record. There is therefore no evidence to support the assumptions made in the Town's calculations. The Town's witness never supported these adjustments on the record and they must fail for lack of proof.

6. **The Division's meter rules can only be enforced by the Division, not the Commission.**

The Town states that the Commission failed to address alleged BIPCo non-compliance with the Division's meter testing and reporting requirements. The short answer to this allegation is that the meter provisions, which are set forth in the "Rules Prescribing Standards for Electric Utilities," were enacted by the Division, not the Commission. The Commission has no regulatory authority over Division Rules. If the Town wants to file a complaint regarding the meter standards established by the Division, a complaint would need to be filed with the Division, not the Commission. Relief would presumably need to be requested from the Division under R.I.G.L. § 39-4-10 "Orders as to unreasonable practices or inadequate services" and/or R.I.G.L. § 39-4-11 "Orders as to unsafe or improper conditions." Both of these statutes give jurisdiction to the Division, not the Commission. Only the Division can enforce its Rules.

[2] In a footnote on page 2 of the Town's June 10 letter four more issues are listed that the Town apparently did not feel rose to the level of the six points listed above. These footnote items are: 1. tree-trimming, 2. amortization of the gain on the sale of time shares, 3. imputation of revenue for an owner's storage of a boat on utility property, and 4. disallowance of a portion of Company rate case expense as imprudent. With the exception of tree-trimming, the first time the Town suggested these adjustments was in the Town's brief, which is clearly not evidence.

For the foregoing reasons, BIPCo respectfully submits that the Town's letter dated June 10, 2008 should be rejected.[3]

Respectfully submitted,

Michael R. McElroy

MRMc:tmg
07 Rate-Massaro20
cc: Service list

[3] The Commission previously denied BIPCo's request to increase its rate case expense allowance to the amount actually expended by BIPCo. However, BIPCo's preparation of this letter response, which was once again driven solely by the Town's actions, has further increased BIPCo's actual rate case expense.