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May 20, 2008

BY FEDERAL EXPRESS PRIORITY OVERNIGHT
Luly Massaro
Commission Clerk
Rhode Island Public Utilities Commission
89 Jefferson Blvd.
Warwick, RI 02888

Re: Block Island Power Company General Rate Filing
Docket No. 3900

Dear Luly:

Enclosed please find for filing in the above matter an original and nine (9) copies of the Brief of the Town of New Shoreham. A copy of this filing is being emailed to you and to the Service List.

Thank you for your assistance in this matter.

Very truly yours,

Alan D. Mandl, Bar No. 6590

Enclosures
cc: Service List
Katherine A. Merolla, Esq.
Nancy Dodge

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: BLOCK ISLAND POWER	:	
COMPANY: GENERAL RATE	:	**DOCKET NO. 3900**
FILING	:	

BRIEF OF THE TOWN OF NEW SHOREHAM

By its attorney,

Alan D. Mandl, Bar No. 6590
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Dated: May 20, 2008

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I. INTRODUCTION AND STATEMENT OF PROCEEDINGS

A. TRAVEL OF CASE

On November 9, 2007, Block Island Power Company ("BIPCo" or the "Company") filed an application seeking to increase its base rates by $400,027, or 17.46% (Schedule WEE-1). In rebuttal testimony, the Company reduced its request to $361,978 (Schedule WEE-1 Rebuttal), a 15.80% increase in base rates. The Company proposed to collect these additional base revenues through an across the board rate increase.

The Commission suspended the Company's proposed base rate increase for investigation. The Division of Public Utilities and Carriers (the "Division") presented direct and surrebuttal testimony from its consultant, David Effron. Mr. Effron recommended a base rate increase of $181,948 (Schedule DJE-1S). The Town of New Shoreham (the "Town") moved to intervene in this matter on December 5, 2007. The Town submitted direct and surrebuttal testimony from its consultant, Richard La Capra on five (5) major issues of concern to the Town.

Evidentiary hearings were held on May 8 and May 9, 2008. Through cross-examination of Company witnesses, the Town identified additional management prudence and cost of service issues that must be addressed by the Commission. In accordance with the procedural schedule adopted in this matter, the Town of New Shoreham files its Brief.

B. BACKDROP OF THESE PROCEEDINGS

The Town of New Shoreham represents the entire service area of the Company.

Historically the cost of electric service has been very high, with increasing fuel costs representing a larger part of consumer bills. In order to address these increased fuel costs and mitigate their impact upon ratepayers, the Town has stressed the need for a demand side management program and supported the recommendations of HDR Engineering, which prepared the Integrated Resource Plan submitted to the Commission for review and approval. Other communities in Rhode Island benefit from DSM programs, and the type of program recommended by HDR is a critical step in reducing the impact of rising fuel costs on ratepayers. Conservation reduces the fuel costs that the Company passes through to ratepayers. HDR found conservation to be the most cost effective way to create ratepayer savings.

The Town also has recommended that the Commission direct the upgrading of the Company distribution system and the addition of engine regulators. The distribution system upgrade will reduce historically high line losses, over 24% in 2003, to a more acceptable 8%, producing substantial ratepayer savings in excess of $160,000 per year. The upgrade and addition of engine regulators will address the service quality problems brought to the Commission's attention in this case. Moreover, the reduction in voltage losses will result in higher kwh sales for the Company and improve its revenues. HDR and Town consultant Mr. La Capra concur that these system improvements are critical for ratepayers and needed by the Company to meet its public service obligations.

The Town also has stressed the need to assure the reasonableness of base rate expenses, over which the Commission has greater control. The Town urged the Commission apply its ratemaking precedents and enforce affiliate transaction requirements in order to reduce the base rate increase sought by the Company.

The Town has shown its desire to promote constructive action by the Company for the long-term benefit of ratepayers. In Docket No. 3655, the Town supported a summer surcharge to fund the HDR Integrated Resource Plan. In the present case, the Town has proposed to defer recognition of the credit to ratepayers arising out of the Company's sale of land and buildings that have been included in utility plant in service and rate base for many years, in order to facilitate systems improvements.

The history of the Company shows that it does not take necessary and timely actions to improve its system unless directed to do so by regulators, be they environmental regulators or public utility regulators. The current owners have placed their personal gain ahead of the financial health of the public utility and the provision of adequate and reliable service at a reasonable cost. The Town has invested substantial resources of its own to bring these issues before the Commission and respectfully requests that the Commission address the legitimate concerns of the Town and its residents.

II. SUMMARY OF ARGUMENT

A. SUMMARY OF TOWN RECOMMENDATIONS

The Town recommends a base rate increase of $77,342. Schedules supporting the Town's recommendation, in relation to the positions of the Company and the Division, are attached to the Town's Brief.

The Town has raised five major issues for Commission resolution through the testimony of its consultant, Richard La Capra. It also has raised additional management performance and revenue requirements issues:

1. Ratemaking Treatment of Net Gain on the Sale of Utility Property Reflected in Cost of Service

In accordance with well-settled Commission precedent and Rhode Island Supreme Court decisions, the net gain of $828,196 derived from the Company's sale of real property should be credited entirely to ratepayers because this real property was supported by ratepayers.[1]

In the alternative, giving ratepayers credit for assets included in utility plant in service and supported by them in rate base, but excluding a garage built by a tenant as a leasehold improvement on rate-based land, would result in crediting ratepayers with eighty percent (80%) of the net gain, or $662,557.

2. Method for Crediting Ratepayers With Their Share of the Net Gain

The Town supports either (a) an immediate rate base deduction in this case or (b) the creation of a construction reserve account funded from an annual amount collected through rates equal to ten percent (10%) of the net gain to be credited to ratepayers. Under the second option, the net gain amount credited to ratepayers annually would be used to fund a segregated construction reserve account to help pay for a badly needed and long overdue distribution system upgrade and the installation of regulators at Company engines, rather than used to reduce rates currently. When the Company seeks rate recognition for new debt used to fund any part of this construction or for any portion of these capital improvements, the portion funded by the ratepayers' share of the net gain should be treated as customer-contributed funds, with a zero rate base impact. If these needed improvements have not been made within 24 months of the beginning of the rate year, an immediate reduction in rate base should be directed in order to credit ratepayers with their share of the net gain.

If the construction reserve option is adopted by the Commission, it would be unnecessary to impose a $0.01/kwh summer surcharge to pay for the Company's RUS loan application costs.[2]

3. The Amount of Net Gain

Net gain should not be reduced by post-sale costs of $27,908.04. The Company was not obligated to pay any of these zoning and planning board expenses under the terms of its purchase and sales agreement. Planning

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[1] The Town has used the same net gain amount used by the Division (Effron Direct, Schedule DJE-8). The Company has elsewhere referred to the net gain amount as $814,000 (e.g., Tr. 5/8/08 at 52).

[2] Any fees collected through this surcharge, if adopted, also would result in a deduction in future plant in service because it would have been prepaid with ratepayer-supplied funds.

Board expenses were the express responsibility of the buyer and the transaction was made without any zoning contingencies, leaving all zoning a matter for the buyer's due diligence.

4. Interim Reduction in Payments and Benefits Given by the Owners to Themselves as Unsupported and Unreasonable Affiliate Transactions

The Company failed to comply with affiliate transaction requirements under Rhode Island General Laws. It has not met its burden of proving the reasonableness of approximately $267,000 in rate year payments and benefits for the owners of the Company under affiliate transaction and general ratemaking standards. These payments and benefits should be reduced to $135,000, the equivalent of one full-time executive position plus one set of benefits, based on Company compensation consultant Bodah's study. This allowed amount is in addition to compensation and benefits for the Company's General Manager, Mr. Milner, and is more than adequate for a small utility. It would not prevent the Company from paying dividends out of its earnings. In the alternative, the Town has proposed a $113,322 reduction in owner payments and benefits, tied to specific adjustments, as described by Mr. La Capra.

5. Remedial Actions Concerning Payments and Benefits Given to the Company's Owners

The owners must comply with Rhode Island's affiliate transaction statutes. Written agreements between the Company and any owner receiving payments over $500 should be filed with the Division. Commencing with the rate year, the owner/officers should be directed to maintain and submit certified time records indicating, per month, the amount of time spent on specific company matters and the nature of the work performed each month on these matters. Because the owners consider themselves independent contractors and appear to require unaffiliated independent contractors to submit these types of records, this requirement is reasonable and necessary. The owners also should be required to maintain records of their personal use of Company vehicles and the Company should be fully reimbursed for their personal use.

6. Adoption of the HDR Integrated Resource Plan Report, Including the Energy Advisor Component, for Implementation

The Commission should approve the HDR IRP Report, including its establishment of an Energy Advisor position, funded through a continuation of a $0.01/kwh surcharge applicable to consumption during the summer surcharge period. The Energy Advisor's functions are outlined in the HDR IRP Report. HDR found, after extensive work, that the Company does not have the capability to carry out and pay for a

legitimate conservation and load management program of the type recommended by HDR. The track record of ownership regarding conservation and DSM is dismal. They would cause a critical part of the Integrated Resource Plan to fail. The Company's "Green Officer" alternative is inadequate to carry out the most cost effective measures for ratepayers found by HDR.

7. Cost Allocation and Rate Design Study to be Conducted by an Independent Consultant Under IRP Work Group Direction

The Commission should direct the performance of a cost allocation and rate design study by an independent consultant selected by a majority of the IRP Working Group, to be paid for by the Company and made available for review and consideration at the time of the Company's next rate case.

8. Compliance With Division Meter Testing and Reporting Requirements

The Company has not complied with Division meter testing and reporting requirements. The Commission should direct the owners to comply with these requirements.

9. Additional Revenue Requirements Issues

The Town has raised additional cost of service issues in this case, apart from its acceptance of certain cost of service adjustments proposed by the Division:

1. Removal of BIPCo Rental Payment to Affiliate Island Services, Inc. for Use of Property Owned by BIPCO - ($5,000)

2. Amortization of Meter Reading Methods Study Expense - ($8,000)

3. Disallowance of Non-Recurring Expenses Associated With a Completed Hazardous Waste Clean-Up Project - ($13,999)

4. Normalization of Board of Directors Meeting Expenses - ($3,184)

5. Crediting of Revenues From Backbilling of Verizon and Block Island Cable Through 6 Year Amortization - ($9,961)

6. Normalization of Tree Trimming Expenses - ($2,335)

7. Crediting of Gain From Sale of Time Share Units - ($4,800)

8. Imputed Revenues for Owner Storage of a Boat on Utility Land included in Rate Base - ($1,200)

9. Disallowance of One Third of Amortized Rate Case Expenses as Imprudent - ($18,333)

These adjustments should be accepted by the Commission.

B. REMEDIAL ACTIONS BY THE COMMISSION ARE NEEDED

The Commission must take remedial action in this case to (1) cure chronic failures of ownership to perform basic public service obligations and (2) curb unreasonable affiliate transactions. The owners have shown that they will continue to shirk their duty to provide adequate service and place their personal financial gain ahead of the financial needs of the Company and the interests of its ratepayers, unless they are brought in line by the Commission.

The Commission has the opportunity in this rate case to go to the root of these problems. It can: (1) direct that net gain from the real estate sale be properly credited to ratepayers in accordance with precedent; (2) jump start the distribution system upgrade and installation of engine regulators by directing that the net gain credited to ratepayers initially fund these improvements, followed by a deduction in rate base; (3) eliminate non-compliant and unreasonable affiliate transactions and require time records from the owners going forward; (4) approve the HDR IRP Report for implementation in full; (5) move the Company toward cost-based rates; and (6) direct compliance with Division meter testing and reporting requirements.

Maintaining the status quo would result in continuing financial harm to the public utility and its ratepayers, inadequate service and undue enrichment of the owners.

III. ARGUMENT

A. THE NET GAIN OF THE SALE OF REAL PROPERTY BOOKED AS UTILITY PLANT IN SERVICE AND INCLUDED IN RATE BASE FOR RATEMAKING PURPOSES MUST BE CREDITED TO RATEPAYERS IN ACCORDANCE WITH THE COMMISSION'S DECISIONS APPROVED BY THE RHODE ISLAND SUPREME COURT

1. The Commission Has Consistently Credited Ratepayers With Net Gain on the Sale of Utility Assets to the Extent that Ratepayers Have Supported the Asset Through its Inclusion in Utility Plant in Service and Rate Base

The Commission has consistently ruled that ratepayers should benefit from any gain realized on the sale of utility property that has been supported by ratepayers through the rate-setting process. This approach has been referred to by the Rhode Island Supreme Court as a "support approach" whereby a gain on the disposition of utility real estate is divided on the basis of the percentage of the financial burden of the property that each party [ratepayers and shareholders] bore. Ratepayers should receive recognition to the extent that they contributed to the asset (*Newport Electric Corp. v. Public Utilities Commission*, 624 A.2d 1098, 1103 (R.I. 1993). *South County Gas Company v. Burke,* 551 A.2d 22 (R.I. 1988). (La Capra Direct at 2)).

The Commission has applied the support standard to utility sales of real estate as well as equipment. The same standard has been applied to depreciable and non-depreciable assets supported by ratepayers (*Providence Gas Company,* Docket No. 1189 (Order No. 9120)(1976) (requiring amortization of gain on the sale of real estate to reduce rates). *Block Island Power Company,* Docket No. 1709 (March 30, 1984)(Order No. 11202)(requiring that gain from the sale of office trailers be amortized as revenues to reduce the level of rate increase sought by BIPCo)).

The support standard has been applied by the Commission irrespective of the amount of the net gain to be credited to ratepayers or the degree by which base rates are reduced by the crediting adjustment. Nor do the support standard decisions of the Commission take into account in determining the amount of net gain to be credited to ratepayers whether the Company would be better off financially if it retained the entire gain-an issue that exists in the case of every cost of service adjustment dictated by established ratemaking standards.

Under current Rhode Island law, therefore, ratepayers should be credited with the gain realized from the BIPCo real estate transaction to the extent that they supported the underlying property as a rate base asset.[3]

2. The Real Property Sold by the Company was Recorded as Utility Plant in Service-Not as Non-Utility Property-and has Been Included in Rate Base

There is no dispute that the land sold by the Company has been recorded by the Company in its regulated utility plant in service land account and included in rate base. The property sold was acquired in 1958 (Lot 37) and 1961 (Lot 38, including land and house) and included in rate base (Response to Division-16) (La Capra Direct at 8-10; Responses to TOWN-46,49,52; Edge Rebuttal at 25-27). The house was never booked to a separate asset account. Since it was acquired as part of the 1961 purchase of land, it was not a leasehold improvement made by a tenant.

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[3] There have been rate case settlements where gain on the sale of rate-based assets has been credited either to ratepayers or shareholders[*See, e.g., Interstate Navigation* Co, Docket No. 2484 (Order 15300 issued May 23, 1997); *Interstate Navigation Co.,* Docket No. 1935 (amended stipulation dated December 21, 1989], but these settlements do not constitute Commission precedent and a afford no basis for a ruling in the present case. The Division has properly taken the same position as the Town on the applicable ratemaking standard to be applied to gain from the sale of utility plant in service (including land). The case mentioned by BIPCo counsel during hearings (Tr. 5/9/08 at 119) was based on a settlement and is of no precedential value. It is inconsistent with the Commission's longstanding application of the support standard.

The Company does not claim that this real property was ever booked to the Account 121 non-utility property account, and excluded in setting rates. Mr. Edge admitted that both parcels of land and the house have been included in rate base ((Edge Rebuttal at 25-27) (La Capra Direct at 8, 9; Response to TOWN-55)).

The garage was built by a tenant as a leasehold improvement. Ratepayers supported the arrangement as a result of the Company crediting rental revenues against all costs associated with the property, which were included in utility operating and maintenance expense accounts and cost of service. The tenant improvement merely reflects a reduction in rental revenues previously credited to ratepayers. The garage reverted to BIPCo prior to the sale of the land on which it was located. For these reasons, the entire gain on the sale of real estate by BIPCo should be credited to ratepayers because they supported the entire property (La Capra Direct at 14).

Should the Commission disagree with the Town's position regarding the treatment of the garage leasehold improvement, the Town recommends, in the alternative, that eighty percent (80%) of the net gain should be credited to ratepayers. This percentage is derived by adding together the appraised value of the 2 parcels of land and the house ($380,000 (land and house) + $310,000(land) = $690,000), dividing that appraised value by the total appraised value ($855,000), and multiplying the resulting fraction (80%) by the net gain from the sale ($828,196). The resulting net gain to be credited to ratepayers would be $662,557 (Exh. WEE-3 Rebuttal, Appraisal Report dated February 23, 2006, at 4, 5, 49, 61, 63, 64).

3. No Basis Exists for Varying From the Commission's Ratemaking Treatment of Net Gain on Utility Assets Included in Rate Base

a. The Company's Theories for Shareholder Retention of 100% of the Net Gain are Without Merit

Mr. Edge's self-styled theories why the owners should retain the entire net gain from the real estate transaction conflict squarely with longstanding Commission precedent recognized by the Rhode Island Supreme Court. The Division agrees with the Town on this point (Effron Surrebuttal at 7-10; La Capra Surrebuttal at 4-10). Mr. Edge never acknowledged, and made no effort to comply with Commission precedent.

Mr. Edge is wrong in claiming that net gain on the sale of real estate should be treated differently than the net gain on the sale of plant equipment. The Commission has made no distinction between the sale of utility plant and the sale of land recorded in a regulated land account and included in rate base (*Providence Gas Company,* Docket No. 1189 (Order No. 9120)(1976) (requiring amortization of gain on the sale of real estate to reduce rates)(La Capra Surrebuttal at 9-10)).

Under these circumstances, and given its longstanding practices, it would be arbitrary and capricious for the Commission to suddenly depart from decades of its own precedent and accept Mr. Edge's erroneous positions.

The Commission should disregard the owners' *post hoc* attempt to escape the historic accounting and ratemaking treatment given to its real property. It is disingenuous for the Company to have recorded this asset as a regulated asset and included it in rate base, but claim that the asset, now that it has been sold, should be treated as non-utility property (Edge Rebuttal at 20, 21, 25, 26). As Mr. Effron and Mr. La Capra have testified, any self-serving statements by the Company and any statements by the RUS

(based upon the Company's self-serving statements) have no bearing on and do not alter the facts that the real property has been treated as a regulated asset for accounting and ratemaking purposes (Effron Surrebuttal at 7-10; La Capra Surrebuttal at 4-7).

b. There is No Rational Basis for Abandoning the Settled Support Standard and Determining the Net Gain to be Credited to Ratepayers Based Upon the Benefit That Would Flow to Ratepayers and the Effect of Stockholder Retention of the Net Gain

During the hearings in this matter, the Commission questioned whether the amount of net gain to be credited to ratepayers should be based upon the relative financial impacts upon ratepayers and the Company. The implication was that if ratepayers received a small amount of rate relief (compared to the Company's total fuel and non-fuel expenses) and the Company would benefit financially if it retained the net gain, then the scale tipped in favor of Company retention of the net gain (Tr. 5/9/08 at 92-97).

There is no rational basis for the application of such a standard. In effect, it would be no better than ruling that if a robber were more needy than a robbery victim, the robber would be permitted to keep stolen property.

The Town agrees with Division witness Effron that determining the amount of net gain to be credited to ratepayers does not and should not depend upon the relative impact upon ratepayers and a public utility (Tr. 5/9/08 at 96, 97). When BIPCo was required to amortize the proceeds from the sale of a trailer, for example, the amount involved was a small reduction in cost of service. The amount of benefit to ratepayers was never a factor in determining the amount to be credited to ratepayers (*Block Island Power Company,* Docket No. 1709 (March 30, 1984)(Order No. 11202)). Nor in any other case known to the Town has the Commission taken such an approach as a basis for determining the

ratepayer share of net gain on the sale of utility property booked to regulated utility accounts and supported through rates.

The Town further agrees with Mr. Effron that under Commission ratemaking standards, the amount of the net gain to be credited to ratepayers is not based on a public utility's financial condition-that is true of all adjustments to Company revenues and expenses during a rate case (Tr. 5/9/08 at 96, 97).

In no instance in which the Commission's support approach has applied did it ever determine the amount of net gain to be credited to ratepayers based upon a public utility's financial condition. In past cases, the Commission has taken into account whether the property had been excluded from regulated plant accounts and rate base for any periods of time prior to its sale, and based its apportionment of net gain on that basis in applying its support standard (*Newport Electric Corp. v. Public Utilities Commission*, 624 A.2d 1098, 1103 (R.I. 1993). *South County Gas Company v. Burke,* 551 A.2d 22 (R.I. 1988)).

If all that mattered was how a public utility would be affected by a cost of service adjustment, there would be no reason to have any other ratemaking standard applicable to any other cost of service issue. Speculative and non-recurring expenses would be built into rates on the grounds that they mattered only little to ratepayers, but would improve the Company's profits or balance sheet. Plainly stated, adoption of this approach would turn the exercise of public utility ratemaking on its head. It would be arbitrary and capricious action that this Commission should not take (Tr. 5/9/08 at 96, 97).

c. The Commission Has Other Tools to Address the Financial Condition of the Company

While it is legitimate for the Commission to be concerned about the financial health of a public utility, the cure is not to abandon established Commission precedent for determining the amount of net gain to be credited to ratepayers. The Commission has other tools to address the financial condition of the Company. First, putting a stop to unreasonable affiliate transactions and self-dealing by the owners would curtail the financial damage that the owners are causing the Company. As shown in the discussion below, the paring back of these types of transactions to a reasonable level would have enabled the corporation to satisfy its 2007 RUS OTIER coverage requirements.

Second, the Commission is authorized to grant interim rate relief if a public utility demonstrates the need for such extraordinary relief. BIPCo has received emergency rate relief from the Commission in the past. Docket No. 1998 (Order 13601, issued April 29, 1991). Third, the Commission has taken a number of steps in the past to help BIPCo meet extraordinary expenses, such as environmental remediation expenses, through the implementation of surcharges (*Report and Order*, Docket No. 1998 (Order 13769, effective November 1, 1991)). Fourth, the Commission and Division can take steps to encourage an infusion of new equity capital from investors.[4]

In sum, the Commission should not take legally indefensible actions to aid BIPCo where it has several tools to address any legitimate need of BIPCo for rate relief. The

[4] The owners have done nothing to increase the Company's capital stock limitation of $200,000, which has been in effect since 1959. In the past, the Division has had to exercise its extraordinary statutory power to amend the Company's charter to enable the issuance of more stock (*Report and Order*, Docket No. D-91-3 (Order 13663 dated May 1991) (authorizing issuance of preferred stock pursuant to Division authority to amend BIPCo's charter under R.I.G.L. §39-3-23 and noting, "The long term solution requires a legislatively approved amendment to the existing charter in order to bring BIPCo up to date.")).

financial impact upon the Company, as a result of crediting ratepayers with net gain from the sale of rate base assets, is not a proper factor for determining the amount of net gain to be credited to ratepayers.

4. The Highest and Best Use of the Ratepayer Share of Net Gain is the Funding of Generation Plant Regulators and the Distribution System Upgrade, With Rate Base Deductions Equal to the Amount of the Ratepayer Share of Net Gain Used to Fund These Badly Needed System Improvements

The Town has proposed a method for using the ratepayer share of net gain from the Company's sale of land that would result in the highest level of benefit for ratepayers. While typically net gain credited to ratepayers is flowed through as a current reduction in base rates by spreading the net gain as a credit against cost of service over a period of years,[5] the Town has suggested other methods, at least one of which would defer the credit to ratepayers to facilitate the system upgrade. As the upgrades are completed, the ratepayer share of the net gain would be subtracted from plant in service (La Capra Direct at 14-16; La Capra Surrebuttal at 11-13).

For example, assuming a net gain of $828,196 and the crediting of ratepayers with 80% of the net gain, ratepayers would be credited with approximately $662,557. If that gain were "kept" by the Company in the form of higher current rates rather than reduced annually by $66,256 annually (as would occur with a 10 year amortization), the annual amount to be credited to ratepayers could be used to fund a restricted construction reserve account. Funds could be drawn from that account to pay for loan application or startup expenses (other funds available to the Company also could be applied). A loan or other source of capital would be used to fund the cost of the distribution system upgrade and the installation of regulators. At such time as any portion of these capital additions and

[5] *See, e.g., Providence Gas Co.*, Docket No. 1189 (Order No. 9120) (1976).

improvements and/or any source of external capital are recognized in rates, plant in service would be reduced by the amount of the net gain credited to ratepayers (e.g., $3 million of capital investment would be reduced by $662,557, using the above net gain and ratepayer share values).[6] If, after a reasonable time[7], the Company failed to carry out these system improvements, the Commission could order an immediate rate base reduction. A safety net of this type is needed to assure that the Company moves quickly to implement these long overdue, badly needed capital improvements.

The Town's approach also does not result in any immediate reduction in the Company's rates-it defers the rate reduction to enable badly needed system improvements to be made as soon as possible.

5. The Net Gain Should be Calculated Without Subtraction of Post Sale Expenses Due to Zoning and Planning Board Expenses That Should be the Responsibility of the Buyer, an Entity in Which One Owner has an Indirect Financial Interest

The net gain should be determined to be $828,196 and not reduced by post sale expenses for zoning and planning board issues arising after the sale. Under the terms of the purchase and sale agreement, all planning board expenses were the express responsibility of the buyer (Edge Rebuttal, Exh. WEE-3 Rebuttal, Purchase and Sale Agreement, paragraph 11; Tr. 5/8/08 at 55, 56). Also, nothing in the purchase and sale

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[6] The Company's hearing proposal presented through counsel, that a 1 cent per kwh summer surcharge be imposed to finance upfront costs of applying for a RUS loan (Tr. 5/8/08 at 171-19), is unnecessary. In effect, allowing the Company to continue to collect through annual rates a portion of the net gain to be credited to ratepayers serves the same function, without causing a further increase in rates through a separate surcharge.

[7] Based on the record, 2 years would be a reasonable time. Mr. La Capra testified that the outside limit for preparing and submitting a RUS loan application would be 12 months. HDR estimates a 24 week construction period for the proposed distribution system upgrade. Allowing time for the RUS to issue the loan and for some additional construction time would be covered by an additional 6 months (Tr. 5/9/08 at 178, 179; Town Exh. 7 (December 2004 HDR Distribution System Report, included with the Company's original RUS grant application). Less time might be needed depending on the availability of other sources of capital.

agreement obligates the Company to pay for zoning expenses incurred after the sale (Tr. 5/8/08 at 57). The purchase and sale agreement does not include any zoning contingency and the buyer agreed to purchase the property as is (Edge Rebuttal, Exh. WEE-3 Rebuttal, Purchase and Sale Agreement-the only contingency was title).[8] The buyer was under an obligation to conduct its own due diligence regarding the zoning applicable to the purchased property.[9]

6. The Company's Accounts Payable Were Largely Supported by Revenues from Rates Approved by the Commission in Docket No. 3655, are Annual Recurring Expenses of the Type that the Company has Paid Prior to and Since the Sale of Rate Based Property, and Have No Bearing on the Ratemaking Treatment of the Net Gain on the Sale of the Property

The Commission should treat as irrelevant and inaccurate the Company's contentions that it applied the net gain on the sale of real property to pay off accounts payable and that its owners have derived no benefit from its proposed retention of the entire net gain (La Capra Direct at 13, 14). All that the Company has done is pay its ordinary, recurring expenses of operation. These expenses were covered by the increased rates approved by the Commission in Docket No. 3655. The rate year in that case was the year ending May 31, 2006. Rate increases went into effect as of June 1, 2005. *Report and Order, Block Island Power Co.,* Docket No. 3655 (Written Order issued September

[8] The buyer also received substantial tax benefits as a result of this purchase under Internal Revenue Code Section 1031 for a like kind exchange of property within a period of time after it had sold other property. (Tr. 5/8/08 at 49).

[9] The buyer is an estate being administered by Mr. McGinnes, one of BIPCo's owners, and family members are beneficiaries under Rhode Island intestacy laws. Despite the alleged post sale agreement that BIPCo pay fifty percent (50%) of these post-sale expenses (which it was not obligated to pay), BIPCo has been paying one hundred percent (100%) of these post-sale expenses (Tr. 5/8/08 at 57-60), which further harms the public utility.

13, 2005). Many of the expenses listed in Exh. PUC-5 were invoiced during the rate year.

The Company ignores the fact that it also derives cash from other sources, including its charges to ratepayers. Any cash from the real estate sale is indistinguishable from other sources of cash. [10] To the extent that the receipt of more cash enabled the Company to pay its routine expenses earlier than usual, it is simply a function of the levels of sales and revenues of the Company during the winter, spring, summer and fall. Typically, the Company has deferred making some payments until it was more flush with cash. The extra cash from the property sale led to increases in the retained earnings and book value of the Company. As Mr. La Capra stated, the Company has effectively borrowed funds from ratepayers pending a rate case in which the ratemaking treatment of the net gain would be addressed (La Capra Direct at 13, 14).

Contrary to Mr. Edge's claims, the owners benefit from their retention of the entire net gain, while ratepayers are being harmed as a result. The proposed overall cost of capital has been inflated, the return requirement increased and the tax component of cost of service increased. An increase in book value also benefits the owners. Ratepayers already have covered the Company's rate year revenue requirements and routine recurring expenses through rates approved in Docket No. 3655 and should not forced to pay higher rates based upon the Company's retention of the entire net gain.

[10] In one instance, the Company claims to have paid from net gain fuel transportation charges. These charges are recovered directly from ratepayers through the Company's fuel adjustment tariff, filed as part of its rate filing. This illustrates that the Company received two sources of cash (ratepayers and net gain) to cover one set of routine expenses largely covered by the rates approved in Docket No. 3655 (payment of rate case expenses built into rates, payment of gross receipts taxes, property taxes, payment of outside contractors, for example)(Tr. 5/9/08 at 28-38; Commission Exh. 5).

B. THE COMPANY SHOULD BE ORDERED TO SUBMIT, AFTER INPUT FROM THE IRP WORKING GROUP, A TIMETABLE FOR THE INSTALLATION OF GENERATING PLANT REGULATORS AND THE UPGRADE OF ITS SUBSTANDARD DISTRIBUTION SYSTEM

1. There is no Dispute That the Company has Operated a Substandard Generation and Distribution System That Has Inflicted Continuing Harm on Ratepayers as Well as the Financial Health of the Company

HDR Engineering reported to the Company in December 2004 that its distribution system was plagued by high voltage losses and high line losses. Line losses were reported as 24.17% in 2003 (Response to TOWN-96, Financial Forecast, Determination of Load, Item 4c) and ranged from 13.15% during FY 2005 to 15.46% in FY 2007, the test year (La Capra Direct at 16-20). Based on FY 2007 fuel costs, each reduction of 1% in line losses would save ratepayers $21,400 annually in fuel costs; with an upgrade projected to reduce line losses to about 8% (as provided in the Company's most recent 10 year financial forecast)(Response to TOWN-96, Financial Forecast, Determination of Load, projected Item 4c), ratepayers would save about $160,000 annually, even more given increases in fuel costs since the end of FY 2007 (La Capra Direct at 17). The owners have been indifferent to this long-term, unnecessary cost because fuel costs are passed through to consumers under its fuel charge.

High voltage losses are responsible for fluctuations that have caused damage to the property of ratepayers.[11] In a quality of service investigation by the Division in 1990,

[11] Dr. Casazza's claim that a ratepayer's electronic equipment was "fried" as a result of a tree falling on the drop line on her property (Tr. 5/9/08 at 171) demonstrates his lack of knowledge of the causes of the problems due to a substandard distribution system and the lack of engine regulators. Had a tree fallen on the ratepayer's service drop, she would have experienced an outage, not the "frying" of electronic equipment caused by voltage fluctuations. Moreover, the problem cited by a ratepayer at the April 24, 2008 public hearing was also cited by other ratepayers, including the Town school. There is no evidence of a falling tree epidemic on Block Island.

a Division Electrical Engineering Specialist explained that more voltage regulators were needed in order to reduce surge problems (*Report and Order,* Docket No. D-90-7 (Order 13477 issued November 27, 1990)). In a subsequent rate case, the Commission found "...that a study of the Company's distribution system is appropriate" and allocated funds to a restricted account to provide for the costs of the necessary study (*Report and Order*, Docket No. 1998 (Order 13769, effective November 1, 1991)).

More recently, HDR Engineering advised the Company in 2004 that high voltage losses also result in the Company billing lower kwh sales than it could bill if its system had voltage losses within industry standards (La Capra Direct at 19, 20, HDR December 2004 Distribution System Study at 10-16). The Company recognizes this fact (Tr. 5/9/08 at 156). Mr. La Capra further explained that the service problems experienced by ratepayers due to voltage losses (including the Town school, which had brand new equipment damaged as a result of voltage losses)[12] are due to the Company's substandard distribution system and its lack of regulators on all of its engines. The lack of a cable to the mainland is not the cause of the Company's inadequate service (Tr. 5/9/08 at 178, 179).

2. The Commission Should Direct the Company to Seek Funding For These Improvements, if Necessary, Based Upon the Timetable Described by Mr. La Capra

The Commission should direct the Company to proceed immediately to seek financing of the distribution system upgrade and installation of regulators for its engines. The RUS is one possible source of funding. Mr. La Capra has had extensive experience with preparing and obtaining RUS loans for distribution system upgrades and described a reasonable time line for submitting a loan RUS application and work plan and obtaining

[12] Transcript, April 24, 2008 public hearing.

funds from the RUS. At the outside limit, this part of the process may take 12 months (Tr. 5/9/08 at 179, 180). Less time might be required if other sources of capital are obtained.

The time frame provided by Mr. La Capra is further supported by the fact that Company consultant HDR Engineering already has prepared an extensive engineering analysis of distribution system upgrade work and updated the cost of the distribution system upgrade for a Company grant application filed with the RUS as recently as March 28, 2008. Also, the Company is well aware of the need to install regulators on all of its engines (Tr. 5/9/08 at 156), so it is unlikely that it will be starting from scratch in developing a loan application and work plan for these capital improvements.

C. PAYMENTS AND BENEFITS GIVEN BY THE OWNERS TO THEMSELVES ARE UNSUBSTANTIATED AFFILIATE TRANSACTIONS AND EXCESSIVE IN AMOUNT IN LIGHT OF THE COMPANY'S FAILURE TO PROVIDE ADEQUATE SERVICE AT A REASONABLE COST

1. Payments and Benefits Given to the Owners by Themselves Constitute Affiliate Transactions That Require Close Scrutiny by the Commission

The Company's four owners, Messrs. Casazza, Edwards, McGinnes and Pezzimenti, each own more than 10% of the Company's voting stock (Tr. 5/8/08 at 94,95; FERC Form 1 filing for FY 2007 at 104,106). As a result, each owner constitutes an affiliate of Block Island Power Company. Under R.I.G.L. Section 39-3-27, an "affiliate" is defined as including "(1) [e]very person owning or holding, directly or indirectly, ten percent (10%) or more of the voting capital stock of a public utility."

As affiliates, the owners were required to file written contracts with the Company or verified summaries of any unwritten contract or arrangement with the Company within

10 days after the date of contract execution or the entering into of the arrangement (R.I.G.L. Section 39-3-28). In the present case, the owners have not complied with applicable affiliate transaction requirements. There are no written contracts or verified summaries of oral arrangements between the Company and its affiliate owners, although they each receive far more than $500 worth of payments and benefits charged to Company operating expenses (FY 2007 FERC Form 1 at 104,106; Responses to TOWN-24, TOWN-71, TOWN-72). Payments under these non-compliant arrangements are subject to disallowance (R.I.G.L. Section 39-3-29).

Further, under R.I.G.L. §39-3-32, payments to affiliates may be disallowed in any rate proceeding unless the public utility has established the reasonableness of such payments (*Town of New Shoreham v. Rhode Island Public Utilities Commission,* 464 A.2d 730, 732-733 (R.I. 1983)). Because the payments and benefits given to the owners by themselves constitute affiliate transactions, and given the lack of any independent Board of Directors' oversight, the Commission "...has the right and duty to scrutinize closely such transactions" (*Town of New Shoreham v. Rhode Island Public Utilities Commission,* 464 A.2d 730, 733,736 (R.I. 1983)).

Ordinary treatment of executive compensation as within the discretion of management, absent evidence tending to prove that the expenditures unreasonably and unjustly affect the fare-paying public, do not apply in a rate proceeding involving affiliate transactions (*Town of New Shoreham v. Rhode Island Public Utilities Commission,* 464 A.2d 730, 736 (R.I. 1983)).

2. The Company Has Not Met its Burden of Proving the Reasonableness of these Payment and Benefits Under Affiliate Transaction Standards and Otherwise Had Failed to Comply With Affiliate Transaction Requirements

The Company has not met its burden of establishing the reasonableness of the total payments and benefits given to its owners. During the test year, the Company gave or supported over $260,385 in payments and benefits to the owners, all of which were charged to operating expenses (Commission Exh. 5; La Capra Direct at 30-32).[13] These payments and benefits are projected to exceed $266,000 in the rate year, per Mr. Edge's projected increases in health benefit expenses (Schedule WEERY-5b, showing benefit expense increases of $5,826.28).

a. Increases in Direct Payments

Since Docket No. 3655 rates were put into effect, the owners have increased direct payments to themselves by $59,000 from $133,000 to $192,000, a 44% increase in direct payments alone relative to FY 2006.[14] Because these additional $59,000 payments were not reflected in the Company's rates, they eroded the Company's earnings during the test year.

b. Increased and Improper Benefits

In addition to the above payments, the Company also incurred for the owners substantial test year expenses for health and dental care ($36,270)(Schedule WEERY-5a)($41,338.69 in the rate year, per Schedule WEERY-5b). The payment of $13,497.87 test year health insurance benefits provided to an owner who is not an officer was

[13] There is a discrepancy of $757.27 in the medical expense for the President. Schedule WEER-5a lists $8005.00, while Commission Exh. 5 lists $7,247.73.

[14] The Company represented to the Commission that $33,000 in payments to officer/owners above $135,000 would be in the form of dividends. Order, Docket No. 3655 (issued April 17, 2006) at 5. However, they increased these payments by $59,000 and charged them entirely to operating expenses, exacerbating the Company's financial condition.

contrary to Commission precedent (*Block Island Power Company, Report and Order*, Docket No. 1998 (Order 13769, effective November 1, 1991)(benefits disallowed in case of owner who was not an officer and who claimed to be a consultant)).

c. Free Electric Service, Free Use of Company Vehicles and Free Boat Storage

The Company provided free electric service to Dr. Casazza and Mr. McGinnes, which amounted to $7,626 in the test year (Commission Exh. 5).[15] Mr. McGinnes and Dr. Casazza also receive Company-leased vehicles for their own personal use and do not keep track of the personal portion of their use of these vehicles-the Company absorbed $20,348 during the test year for these arrangements and did not provide Form 1099s to these owners, although the owners maintain that their undocumented amount of personal use of Company vehicles should be treated as compensation.

During discovery by the Town, the Company disclosed that it allows Mr. McGinnes to store a boat on rate-based land at no charge, while collecting $1,200 per year apiece from an unrelated party and a relative of Mr. McGinnes (Response to TOWN-58).

d. Lack of Support for Payments and Benefits Given to Affiliates

The owner/officers of the Company do not keep time records to indicate how much time they have spent on particular Company matters (Response to TOWN-5). In the case of Dr. Pezzimenti, the Company admitted that he works 4 days per week as a

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[15] The Town is concerned that the Company's providing free electric service may be inconsistent with its RUS mortgage covenant, Section 3.19, shown in RUS regulations, 7 CFR Part 1718, subpart B, App. A ("The Mortgagor will not furnish or supply or cause to be furnished or supplied any electric power, energy or capacity free of charge to any person, firm or corporation, public or private...."). This is a matter for the Company to address with the RUS which, according to Mr. Edge, might waive any covenant restriction that may be applicable to the Company.

physician in Danbury, Connecticut (Response to TOWN-99), and provided no information on the amount of time that he spends on specific Company matters.[16] The $48,000 payment to Dr. Pezzimenti equates to an annual payment of $240,000 per year, giving Dr. Pezzimenti the benefit of the doubt that he works 1 day per week on Company matters. This situation calls into question the entire payment scheme used by the owners. There is no objective way for the Commission to determine how much time the owners spend on Company matters.[17]

The facts presented in this matter are nearly identical to those in a BIPCo rate proceeding involving the same owners. In its *Report and Order* in Docket No. 1998 (Order 13769 dated November 1, 1991), the Commission scrutinized payments to the Company's owners and found that "...there was no evidence that the fourth owner, Dr. Pezzimenti, had done any meaningful work for BIPCo during the test year." It further found that there was no record support for payments to other director-owners- "...the scope and productive effect of Dr. Casazza's and Mr. McGinnes' efforts in BIPCo's behalf remains hazy." Under these circumstances, the Commission reduced the $95,000 in claimed "compensation" to $60,000 to cover both management and directors' fees.

Health insurance benefits paid to Mr. Edwards, which the Company is not required to pay and does not pay to others, are of the same type that were disallowed in the case of Mr. McGinnes during a period of time when he was an owner and consultant,

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[16] Because of the extensive reliance of the Company on Mr. Edge's firm and other accounting firms, it is highly unlikely that Dr. Pezzimenti spends 1 day per week on Company matters, or that his time is worth the equivalent of $240,000 per year or more, depending on how much time he actually dedicates to Company work and the benefit to ratepayers derived.

[17] The delayed Company response to a March 28, 2008 letter from the RUS, calling for a Company responses within 30 days, is indicative of the lack of management presence or attention to important Company matters. The RUS letter was addressed to Dr. Casazza and copied to Mr. McGinnes, but neither took or directed a timely response to the RUS.

but not an officer (*Report and Order*, Docket No. 1998 (Order 13769, effective November 1, 1991)). The $24,000 payment to Mr. Edwards is exactly the same as an affiliate transaction made by BIPCo and ruled improper by the Rhode Island Supreme Court (*Town of New Shoreham v. Rhode Island Public Utilities Commission,* 464 A.2d 736 (RI 1983)).

The Commission cannot take for granted anecdotal statements about the amount of time spent by the owners acting as officers. They keep no time records and do not pretend to work full-time. Two owners reside off-island in another state. In Order 13601 in Docket No. 1998 (April 29, 1991), the Commission found that Dr. Casazza spent up to one and one half days per month in some years and one day per week in other years on involvement in Company management. At that time (1991), he had received back $135,000 on a $200,000 investment made in 1987, according to Commission findings. He had claimed that these payments represented a return on his investment, not earned compensation. He clearly recognized that these payments could not be justified as compensation, given the amount of time spent on Company affairs.

In the present case, the owners have not provided any objective, reviewable evidence of the amount of time that they spent on Company matters. Nor have the demonstrated whether they have benefited ratepayers. It should be evident to the Commission that the owners essentially regard the payments and benefits that they receive as if they were a return on their investment-only charged as operating expenses.

The Commission should take note that the Company has 9 employees, including General Manager Milner. Paying four independent contractor owners and picking up their benefits is unreasonable on its face for a public utility of this size, and given the

very high percentage of total Company compensation and benefits that these payments represent. [18] Another indicator of the unreasonableness of these payments during the test year was their impact on the ability of the Company to meet its RUS OTIER coverage ratio.

3. Payments and Benefits to the Owner/Officers Should be Reduced as Recommended by Mr. La Capra

The Commission should adopt the recommendation of Mr. La Capra that the payments and benefits given to the three owner/officers be capped at $135,000, or the equivalent of one full-time executive position and one set of benefits, based upon the compensation study performed by Dr. Bodah (La Capra Direct at 29-38; La Capra Surrebuttal at 19-28).[19] Included in this adjustment is the disallowance of the $24,000 payment given to Mr. Edwards, which the Company was under no obligation to make and should not have made in light of its financial condition (La Capra Direct at 31). This payment to a fellow owner is mislabeled a pension, although it falls outside the Company's pension plan for employees and the Company was under no obligation to give this payment. This type of disguising of a payment to an affiliate as a pension has been denounced by the Rhode Island Supreme Court as improper [*Town of New*

[18] The overall amount of payments and benefits given to the owners during FY 2007 is nearly 38% greater than the amount of payments and benefits given to the owners during FY 2006. In order to put these amounts in perspective, the rate year benefits to be given to the owners equal 26% of the total rate year benefits for the entire Company ($41,338.69/$160,205.81, per Schedule WEERY-5b, dealing with health benefits). The $192,000 in annual payments to the owners during the test year equals nearly 30% of test year compensation for all Company employees (Schedule WEE-4a, plus consideration of the $24,000 payment to Mr. Edwards as part of total compensation, $192,000/$652,279= 29.435%).

[19] Mr. La Capra provided an alternative recommendation that payments and benefits to the owners be reduced by $113,322, based on test year expense levels. (La Capra Direct at 36-38). The basis for this alternative recommendation should be adjusted in two respects. First, it should be reduced by $15,121.87, since Dr. Pezzimenti did not receive benefits during the test year. Second, it should be increased by the same amount to remove the benefits given to Mr. Edwards, which were disallowed in the case of another owner who, like Mr. Edwards, was not an officer. No change in the amount of this alternative adjustment is necessary.

Shoreham v. Rhode Island Public Utilities Commission, 464 A.2d 730, 736 (R.I. 1983)] and should not be tolerated by the Commission.

In addition, the benefits paid to Mr. Edwards were of the same type disallowed in *Report and Order*, Docket No. 1998 (Order 13769, effective November 1, 1991). The lack of work performed by Dr. Pezzimenti on behalf of the Company is just as evident in this case as it was 17 years ago.

4. The Pascoag Approach, Used for Purposes of a Settlement, Does Not Adequately Remediate the Excessive Level of Payments and Benefits Taken Out of the Company by its Four Owners

The so-called "Pascoag" approach, used in the rate case settlement in Docket No.3655, has no precedential value because it was part of a total package of settlement terms. Also, it does not afford a reasonable basis for addressing the unreasonable amount of payments and benefits given to the owners through affiliate transactions.

First, the Pascoag approach does not take into account that payments are being made by the Company to affiliates who themselves determine what they are paid and what other benefits they receive. Second, the Pascoag settlement model did not take into account the payment of 3 sets of benefits to 3 of 4 owners-it completely ignored the issue of a reasonable level of benefits, including health and dental insurance, free electricity and free personal use of Company-leased vehicles. Third, the Pascoag model assumes that the individuals being compensated perform full-time work-clearly not applicable to BIPCo's owner/officers - a situation that does not apply in the case of BIPCo's owner/officers-most notably, Dr. Pezzimenti.

Finally, the Pascoag model does not justify the payment and benefits given to Mr. Edwards. Mr. Effron, who employed the Pascoag model in his testimony, eliminated this

improper payment to Mr. Edwards through a separate adjustment. The benefits paid to Mr. Edwards are inconsistent with the Commission's prior order in Docket No.1998, another factor that makes the Pascoag approach inappropriate for this situation.

5. The Company's Owners Should be Directed to Comply With Affiliate Transaction Statutes and Maintain and Submit Certified Time Records Starting With the Rate Year

Going forward, the Commission should require the Company's owners to comply with affiliate transaction statutes. They should file written contracts (summaries or oral arrangements should be discouraged). In addition, the Commission should adopt Mr. La Capra's recommendation that the owner/officers be required to maintain and submit certified time records starting with the rate year (La Capra Direct at 41-46). Certified time records, with descriptions of work performed each month and the amount of time spent, would provide a starting point for assessing the reasonableness of payments that the owners award themselves. Division witness Mr. Effron also testified in support of a time records requirement (Tr. 5/9/08 at 87, 88).

Maintenance of detailed time records is especially appropriate where, as here, the owners are affiliates who claim to be independent contractors (La Capra Direct at 45).[20] Other independent contractors who perform services for the Company, including Mr. Edge, Mr. McElroy and LFR, bill the Company monthly on the basis of time spent on particular work during each month (Tr. 5/8/08 at 91, 92; Response to TOWN-20,

[20] The Town questions the classification of BIPCo's owners as independent contractors, but leaves this issue for the Commission to address. Under the Internal Revenue Code, the definition of employee expressly includes "(1) the officer of a corporation..." (dealing with employment taxes) (26 U.S.C. §3121). The State of Rhode Island defers to federal law to distinguish between employees and independent contractors (R.I.G.L. §28-42-7). Mr. Edge did not address the Internal Revenue Code definition of "employee" in Docket No. 3655 and states that he is not conversant with the Internal Revenue Code (Response to TOWN-97). The Town raises its concern in order to avoid the Company's later claiming that the Town "implicitly approved" what the owners are doing. Ratepayers should not be responsible for any penalties or interest incurred if the owners have misclassified themselves.

showing LFR invoices with personnel involved, rates, time spent and services rendered by month).

6. The Abusive Practices of the Owners Have Jeopardized the Financial Condition of the Company and Must be Halted by the Commission and Division

The practices of the owners have jeopardized the financial condition of the Company and must be halted by the Commission and Division. The easiest example of the effects of these practices is the Company's failure to meet the RUS OTIER coverage ratio during calendar year 2007. The OTIER coverage ratio is defined in RUS regulations, 7 CFR §1710.2. OTIER means "Operating Times Interest Earned Ratio." It is calculated as interest expense on long term debt plus operating margin, divided by interest expense on long term debt during a calendar year period reported in RUS Form 7 (Tr. 5/9/08 at 55). In order to attain the required coverage ratio of 1.1, the Company needed to attain a positive operating margin equal to 10% of its interest expenses in 2007, or $20,206.37 (BIPCo Exh. 5; Town Exh. 8; Tr. 5/9/08 at 56, 57).

Mr. Bebyn acknowledged that the Company would have met the 2007 OTIER coverage ratio requirement if it had an operating margin of about $20,206.37 in place of the actual operating margin of about ($129,000), or a change in operating margin of about $149,000 (Tr. 5/9/08 at 57). The Company's operating margin could have been increased to over $20,206.37 during calendar year 2007 through the following actions, all of which were within the control of the owners:

1. reduction in payments and benefits to owner/officers to $135,000, the equivalent of one full-time position with benefits- ($260,000-$135,000= $125,000)[21]

[21] The bulk of this adjustment reflects test payments and benefits given to Dr. Pezzimenti ($48,000) and Mr. Edwards ($37,498), or $85,497.87.

2. not paying zoning and planning board expenses after the sale of its real property to the McGinnes Estate, which BIPCo was not obligated to pay under the purchase and sale agreement- $27,908 (Edge Rebuttal, Schedule WEE-14b (rebuttal) and Effron Surrebuttal at 12).

3. elimination of the BIPCo rental payment to Island Services, Inc. for use of property owned by BIPCo - $5,000

4. charging Mr. McGinnes for boat storage - $1,200

The above items total up to $159,108. Had the owners not charged excessive costs to the Company, the Company would have achieved a positive operating margin of $30,108 and an OTIER coverage ratio greater than the required 1.1.

The Commission also must take into account the adverse impacts on the Company's condition due to the long-standing practices of the owners.[22] The owners have continuously given themselves substantial payments and benefits out of operating expenses. Nearly 17 years ago, the Commission observed in Order 13769 in Docket No. 1998 "the exceptionally generous returns to the owners since their leveraged 1986 purchase of the Company...." Matters have only gotten worse over time as more money has been taken out of the Company in the form of higher operating expenses.

It is time for the Commission to remedy the abusive affiliate transactions that continue to unreasonably burden the Company as well as its ratepayers. The public

[22] As the Commission stated in the *Kent County Water Authority* Report and Order, Docket No. 3660 (Order 18316 issued August 4, 2005), three decades of unnecessary and unreasonable affiliate transaction charges by the owners to the Company "does not make that expense necessary to run a utility; it merely shows that an expense has gone unnoticed or unquestioned for far too long. An operating expense cannot be justified simply by citing past practices. There must be a valid business rationale demonstrating the necessity of the expense for the continuing operations of the utility, which would benefit ratepayers. Three decades of an unjustified...[expense for affiliates]...paid by ratepayers is enough."

utility does not benefit from these affiliate transactions and would be better off if they were curtailed by the Division or Commission.[23]

7. The Owners Have Ignored Commission Concerns

BIPCo's owners also have failed to adopt formal policies regarding personal use of Company vehicles or the making of payments and giving of benefits to some individuals but not others, as the Commission encouraged the Company to adopt in Docket No. 3655.

D. A COST ALLOCATION AND RATE DESIGN FILING SHOULD BE REQUIRED IN THE COMPANY'S NEXT RATE CASE, PERFORMED BY AN INDEPENDENT CONSULTANT, AND DESIGNATED FOR DISCUSSION BY THE IRPO WORKING GROUP

The Town has recommended that BIPCo undertake a comprehensive review of the cost allocation and rate design now in place. This review would be conducted through the IRP Working Group at the Company's expense, and a new allocation of costs and rate design should be filed as part of the Company's next rate case. The need for this study is evident from the Division's own statements in the Company's last rate case that the Company's rates are not cost-based and need to move in that direction.

Although the Commission noted that energy conservation could result in decreased sales for BIPCo, BIPCo would not be affected, as it can spread its revenue requirements across the level of sales that exist from time to time and also can utilize a cost study to determine the level of costs that are not usage sensitive. These costs include

[23] R.I.G.L. §39-3-32 authorizes the disallowance in rate cases payments to affiliates not shown to be reasonable. R.I.G.L. §39-3-31 authorizes the Division, after investigation, to take action to stop the making of any payment or the taking of any action "which substantially threatens or impairs the ability of the public utility to render adequate service, at reasonable rates, or otherwise to discharge its duty to the public..." by applying to the courts for an order directing the public utility to cease and desist making any payment or doing any other thing...." In the Town's view, the Division should take action to halt these destructive affiliate transactions, which have substantially impaired the ability of BIPCo to render adequate service, at reasonable rates.

customer costs, like metering investments, and may also include demand-related costs in the case of larger customers. Moreover, conservation saves ratepayers significant fuel costs that are a pass-through for BIPCo under its fuel charge and do not affect its bottom line. A cost and rate design study is the appropriate vehicle for assuring that the Company's revenue requirements are collected from ratepayers in an equitable fashion, while helping customers benefit from their own conservation.

Mr. La Capra explained that while the Division has tried to move the Company's rates toward a cost-based levels, much work remains to be done (La Capra Direct at 47-49). He explained that the cost involved in performing a cost allocation and rate design study is well within the Company's means and should not exceed $24,000 (La Capra Direct at 50, lines 17-21).

For these reasons, the Commission should direct that the Working Group take steps to have developed by an independent third party a cost allocation and rate design study for filing with the Company's next rate case, at an expense not to exceed $24,000 to be paid by the Company (La Capra Surrebuttal at 32-33).

E. THE COMMISSION SHOULD ADOPT THE HDR INTEGRATED RESOURCES PLANNING REPORT, INCLUDING ITS RECOMMENDATION FOR ESTABLISHMENT OF AN ENERGY OFFICER POSITION TO ENABLE ALTERNATIVE ENERGY SUPPLY SIDE, LOAD MANAGEMENT AND CONSERVATION MEASURES

1. The Commission Should Adopt the HDR IRP Report and Direct its Implementation

The Commission should adopt the HDR Integrated Resources Planning Report which was performed pursuant to the Settlement Agreement in Docket No. 3655.[24] The

[24] The HDR IRP Report was filed by the Division on February 4, 2008 and is before the Commission as Division Exhibit 5.

Division, the Town and the Company are in agreement with regard to the IRP report, with the sole exception being the Company's opposition to the implementation of HDR's recommendation that an Energy Advisor position be established to carry out detailed responsibilities described in Section 4 of the IRP Report.

HDR recommended the creation of the Energy Advisor position because of: (1) the lack of any demand side management leadership on the part of BIPCo, given its "organizational make-up", (2) the fact that there is currently only one full-time BIPCo staff person dedicated to administrative functions of the Company and (3) the lack of adequate office technology and record keeping needed to track the success of energy efficiency measures. HDR acknowledged that the Company could not bear the burden alone of implementing and financing a demand side management program. It therefore recommended the funding of the Energy Advisor position as a first step to be taken to implement demand side management recommendations in the IRP Report.

Funding for this crucial first step would come from a 1 cent per kilowatt-hour surcharge during the 4 month summer surcharge period, as suggested by HDR (Division Exh. 5 at Section 4; La Capra Direct at 23-26). According to HDR, demand side management represents the least cost option for ratepayers, based upon its supply side cost assumptions (La Capra Direct at 27, lines 14-16).

Mr. La Capra testified that the Energy Advisor should be an independent party who is neither an employee of the Company or the Town. He suggested that the IRP Working Group could be tasked to select the Energy Advisor as part of its ongoing role during the implementation of the HDR Report recommendations approved by the Commission for implementation. Further, the Working Group would help ensure that

demand side options pursued for BIPCo would be "manageable, meet specific objectives and be cost-effective investments" as recommended by HDR (Division Exhibit 5 at 4-19; La Capra Direct at 26, lines 12-14).

2. The Company's "Green Officer" Alternative is Disingenuous and Inadequate, and it Should be Rejected by the Commission

Given HDR's conclusion that DSM measures represent the most cost effective option for ratepayers, it is disturbing that the Company is trying to derail the implementation of this portion of the HDR IRP Report. The high electric rates of BIPCo make more DSM measures cost-effective (La Capra Surrebuttal at 28, lines 10-17). The Company's claim, that high rates alone should cause DSM measures to be implemented, is at odds with public policy in Rhode Island that has led other electric utilities to fund and support DSM programs. Further, as Mr. La Capra explained, awareness of the need for conservation is "quite different from the conservation effects which can be realized from a professional delivery program of current products and services, a removal of many institutional barriers to conservation and the assistance in distribution of conservation enhancing products" (La Capra Surrebuttal at 29, lines 4-17).[25]

The "Green Officer" alternative suggested by the Company is inadequate to carry out HDR recommendations for the promotion and implementation of cost-effective DSM measures (BIPCo Response to TOWN-129). As Mr. La Capra testified, the "Green Officer" alternative is disingenuous[26] (La Capra Surrebuttal at 28-30). HDR found that

[25] Dr. Casazza's remarks about the ready accessibility of conservation products from Walmart and Home Depot (Tr. 5/9/08 at 150) ignore the fact that there is no Walmart or Home Depot on Block Island. He also ignores the fact that other electric utilities in Rhode Island, including Pascoag Electric, have implemented DSM programs.

[26] Mr. McGinnes' receiving thousands of dollars per year worth of free electric service makes him unsuitable for any position promoting DSM. Dr. Casazza's receipt of thousands of dollars annually in free

the Company (including Mr. McGinnes) did not have the internal capability and expertise to perform the Energy Advisor functions that HDR recommended. The Company has not claimed that the "Green Officer" would perform the functions recommended by HDR as the first step in implementing DSM measures. Having the "fox guard the chicken coop" approach in the case of this Company, with its lack of expertise, resources and motivation, would be a poor decision for the Commission to make and put the Company's ratepayers at a disadvantage relative to other Rhode Island ratepayers.

The Commission should be mindful of other evidence demonstrating BIPCo ownership's lack of commitment to promoting implementation of DSM measures. BIPCo has no current DSM program, and the track record of the owners has been dismal. The Commission found that current ownership failed to comply with Commission directives regarding conservation and load management when they were given a chance to administer a program. Report and Order, *Block Island Power Co.,* Docket No. 2017 (Order 14234 issued July 15, 1993)(citing Order 13987 in 1992, in which the Company was directed to file reports on conservation and load management expenditures and on the implementation of a conservation and load management program in 1993): "The Commission takes seriously any violations of its orders...BIPCO has evaded reporting requirements, and the extent of its 1992-1993 surplus as well as the complaints about rebate refusal suggest that the Company has not adequately engaged in the dissemination of C&LM program resources."

It would be unconscionable for the Commission to place the administration of the Energy Advisor function, as described by HDR, in the hands of the same unqualified and

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electric service hardly qualifies him to opine of the lack of need for a professionally constituted DSM program recommended by HDR and endorsed by Mr. La Capra.

disinterested owners who previously failed to comply with Commission directives. Instead, the Commission should accept HDR's carefully developed recommendation, which is an integral part of the IRP implementation effort, regarding the implementation of DSM measures, which start with the creation of an Energy Advisor to manage the effort in an independent, cost effective manner.

A three year period is recommended to enable start-up, delivery times for various services and time needed to accurately assess effectiveness (La Capra Surrebuttal at 30, lines 17-21). Given that one function of the Energy Advisor is the pursuit of funding sources for a DSM program, the Energy Advisor could approach other area electric utilities (as suggested by the Commission) to determine the potential for cost sharing and, as HDR described, seek other funding sources to supplement or replace an initial surcharge.

F. OTHER REVENUE REQUIREMENTS ISSUES

As the proponent of the proposed rate increase, BIPCo has the statutory burden of proof with respect to the component elements of its request (R.I.G.L. §39-3-12; *Valley Gas Company v. Burke,* 406 A.2d 366, 379 (RI 1979)). The Company has not met its burden with regard to multiple elements of its request. The Town addresses here additional cost of service issues brought to light through discovery and its review of the Company's and Division's filings.

1. The Island Services, Inc. Affiliate Transaction Rental Expenses Should be Removed From Cost of Service and the Rented Space, Owned by the Company, Should be Returned to Utility Plant in Service

Discovery by the Town uncovered a $5,000 rental expense charged to the BIPCo by an affiliate (owned by the owners of the BIPCo) for office space owned by BIPCo and carried on BIPCo's books as Account 121 non-utility property.[27] In FY 2006, the rental expense was $12,000. BIPCo's paying rent to a separate company owned and controlled by its owners for space owned by BIPCo is imprudent and constitutes and unreasonable affiliate transaction (Tr. 5/8/08 at 65; Town Exhs. 10, 11).

Now that the portion of office space previously excluded as not used for utility purposes has been and is being used for utility purposes (Response to TOWN-23; Tr. 5/8/08 at 83-85)[28], 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 accumulated depreciation, and remove the test year rental expense of $5,000. The Company has not demonstrated that it has had a separate depreciation reserve account for this space or that it excluded from cost of service depreciation, property taxes or other expenses associated with this portion of the office building. No further adjustments appear necessary.

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[27] This portion of the Company's office building was excluded from utility plant in service in Order No. 11202 in Docket No. 1709 (March 30, 1984(Exh. Town-11) and recorded on BIPCo's books as Account 121 non-utility property [Tr. 5/8/08 at 76 ; FY 2006 FERC Form 1 at page 221 and FY 2007 FERC Form 1 at page 221) (Exh. Town-10)].

[28] It is noteworthy that the owners considered rate base recognition for this space, according to Board of Directors' meeting minutes dated June 2, 2005 (Item 5) (Response to TOWN-2). The minutes serve as further confirmation of Company ownership of this space. The Commission should infer that the owners preferred to charge the Company and put into their own pockets (through their ownership of an affiliate, Island Services, Inc.) $12,000 per year for space owned by the Company ($12,000 was charged to the Company in FY 2006).

2. The Cost of the Proposed Study Regarding Alternative Methods for Meter Reading Should be Disallowed and Amortized Over Five Years

The Company's proposed $10,000 increase in cost of service for a study of alternative methods for reading its meters should be disallowed. This item is a one-time, non-recurring expense that should not be built into the Company's annual revenue requirement (*Rhode Island Consumers' Council v. Smith,* 322 A.2d 17, 24 (RI 1974)).

If this expense is recognized in rates, it should be amortized over a five year period because it is not an annual recurring expense and nothing of its type appears to have ever been conducted by or for the Company. If this alternative is adopted, cost of service would be reduced by $8,000 and $2,000 recognized in the rate year.

3. Costs of a Completed, Multi-Year Hazardous Waste Clean-up Should be Removed From Cost of Service as a Non-Recurring Expenditure

During the test year, the Company completed a hazardous waste clean-up project that had fallen behind schedule. Work was accelerated during the test year and the project was completed during the test year (Response to TOWN- 98). Because this $13,999 expense is non-recurring, it should be removed from cost of service ((Response to TOWN-98; Tr. 5/9/08 at 59, 60) *Rhode Island Consumers' Council v. Smith,* 322 A.2d 17, 24 (RI 1974)).

4. Board of Directors Expenses Should be Normalized

The Company has included test year expenses of $7,950 for Board of Directors meeting expenses (Schedule DGB-2 at 3; Tr. 5/9/08 at 65, 66). This amount is far in excess of the $2,500 amount spent in FY 2005 and FY 2006 and well above the five year average of $4,766 (Bebyn Schedule DGB-2 at 3; $23,832 divided by 5). Cost of service

should be reduced by $3,184 to reflect no more than the five year average expense of $4,766, which is more representative.[29]

5. Verizon and Block Island Cable Back Payments of Unbilled Pole Attachment Charges Should be Amortized Rather Than Completely Removed From Rate Year Revenues

The Company removed test year revenues of $37,518 for a payment made by Verizon to cover a period of years during which the Company had failed to bill Verizon (Schedule DGB-4; Tr. 5/9/08 at 62-65). It also removed test year revenues of $22,249 payments made by affiliate Block Island Cable, which has neglected to pay the Company pole attachment fees and still is not completely caught up (Schedule DGB-4; Tr. 5/9/08 at 62-65).

Because ratepayers paid higher rates as a result of the Company failing to bill Verizon and collect pole attachment fees from an affiliate(no revenues were built into rates that have been in effect since June 1, 2005), it would be improper to allow the Company to completely remove these revenues from the rate year. In past cases, the Commission has required that one-time revenues that cover expenses previously paid by ratepayers be credited to ratepayers over a period of years (*Report and Order, Valley Gas Company,* Docket No. 1378 (Order 9727)(1978)(requiring that a gas supplier refund be applied to reduce operating expenses over a 3 year period)).

The Town recommends that both of these revenue sources be amortized over a six year period to assure that ratepayers that supported higher rates receive the benefits of revenue credits that they would have received but for the Company's imprudent neglect.

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[29] The Commission should note that cost of service also includes $6,437 in board meeting-related expenses charged by Mr. Edge, which are separate from the Board of Directors expenses discussed above (Edge Direct at 17, lines 9-16).

Accordingly, rate year revenues should be increased by $9,961 ($37, 518 + $22,249 = $59,767/6= $9,961).

6. Tree Trimming Expenses Must be Normalized

The Company incurred $6,591in tree trimming expenses during the test year and included that expense in its rate year revenue requirements (Schedule DGB-2 at 4; Tr. 5/9/08 at 65). However, during the past two fiscal years the Company incurred no tree trimming expenses and its five year average expenses for tree trimming was $4,356(Schedule DGB-2 at 4). Given that tree trimming expenses are not an annual recurring expense and that the test year level was much higher than the five year average, tree trimming expenses for the rate year should be no greater than the five year average of $4,356 and cost of service should be reduced by $2,335.

7. Gain from the Sale of Time Share Units Should be Credited to Ratepayers Through a Revenue Credit or Reduction in Bad Debt Expenses

The Company included in its rate year expenses $1,330 relating to time share units that the Company had acquired as partial payment for unpaid electric bills owed by the former time share owner. Time share expenses have been included in past rate case filings by the Company. Because the time share units have been sold, the Company admitted that this $1,330 expense should be removed from cost of service and did so in its rebuttal filing.

However, the Company has not credited ratepayers with gain on the sale of these time share units. This gain of $14,400 should be credited to ratepayers because ratepayers supported a bad debt expense allowance of the Company and also bore the additional burden of time share expenses incurred by the Company pending its sale of

these units (Schedule DGB-2 at 5; Tr. 5/9/08 at 68). The Town recommends that this gain be flowed through as a revenue adjustment over a three year period. Revenues would be increased by $4,800 ($14,400 divided by 3).

8. Revenues of $1,200 Should be Imputed For Boat Storage Charges that are Paid by other Parties, but not by an Owner of the Company

Mr. McGinnes has stored a boat on Company property at no charge, while two other parties are each charged $1,200 per year to store their boats on Company property (Response to TOWN-58). This affiliate transaction is unreasonable. Mr. McGinnes should be required to pay the same storage fees paid by other parties. $1,200 in revenue should be imputed to the Company.

9. The Town Supports Other Division Cost of Service Adjustments Where in Addition to, and not Inconsistent with, the Town's Cost of Service Adjustments

The Town supports cost of service adjustments recommended by the Division where they are in addition to adjustments discussed above and not inconsistent with the Town's positions. These adjustments include, but are not limited to, the elimination of any recovery of past rate case expenses and lobbying expenses.

10. A Portion of the Company's Current Rate Case Expenses Should be Disallowed as Imprudent

a. The Town's Proposed Adjustment

The Company is entitled to rate case expenses only if those expenses are reasonable (R.I.G.L. §39-3-12; *Valley Gas Company v. Burke,* 406 A.2d 366, 379 (RI 1979)). The Commission should disallow a portion of the Company's rate case expenses as imprudent. The Town recommends that at least one third of the Company's rate case expenses be disallowed. Based upon Mr. Edge's revised estimate of $165,000, this

adjustment would equal $55,000. Assuming a 3 year amortization period, $110,000 would be amortized over 3 years, at $36,667 per year, and cost of service would be reduced by $18,333.

b. The Company's Imprudence Has Caused Unreasonable Rate Case Expenses

i. Failure to Follow Commission Precedent on Treatment of Gain on Sale of Utility Plant and Real Property

The Company increased rate case expenses by claiming 100 percent entitlement to the net gain on the sale of assets that have been recorded as utility plant in service and maintained in its rate base. This position was patently inconsistent with Commission precedent, supported by the Rhode Island Supreme Court, that ratepayers are entitled to the gain on the sale of utility assets (including real estate) to the extent that they supported those assets through their inclusion in rate base.

There was no factual controversy that 2 parcels of land and a house situated on one parcel and acquired with the land were recorded on the Company's books as utility plant in service in the land account and supported by ratepayers through their inclusion in rate base and through the inclusion of all related expenses in utility operating accounts (property taxes, for example).

Under these circumstances, it was incumbent on the Company to present a direct case that was based upon precedent of the Commission. Instead, Mr. Edge has admitted that both lots and a house that were part of the sale were all "debited to the land account" (Edge Rebuttal at 25) and included in rate base, allegedly due to unsophisticated management (Edge Rebuttal at 26). He does not dispute that current management treated these assets as rate base assets for the 20 years prior to their sale. Instead, he concocted a

theory that has no support under Commission precedent, which he chose to ignore. The Company made no effort to dispute the essential facts that the real property in question had been booked to the utility plant account for land and included in rate base. By taking such an extreme and unsupported position, the Company drove up its rate case expenses.

ii. Affiliate Transactions

The Company increased its rate case expenses by continuing to ignore its fundamental obligations under Rhode Island's affiliate transaction requirements, legal precedents, and concerns expressed by the Commission. As discussed previously, in violation of law, the Company has no written contracts with its officers, who also are affiliates by virtue of owning more than ten percent (10%) of Company voting stock. It has not filed verified written summaries of any oral agreements between the Company and its officer/owners, as required under R.I.G.L. §§39-3- 28, 39-3-29, 39-3-32. Despite the part-time nature of work performed by its officer/owners, the Company maintains no records of the amount of time spent by any officer/owner during each month and with regard to specific work. This behavior is part of a habitual pattern of concealing the lack of work done by absentee owners who either work other jobs or have other business interests.

Contrary to Rhode Island Supreme Court decisions, the owners awarded a payment to an owner that was outside the pension plan applicable to employees and labeled it a pension. This $24,000 annual payment did not arise from any contractual obligation of the Company and caused a further erosion of its RUS coverage ratio.

The Rhode Island Supreme Court ruled in the case of BIPCo that a payment to a former officer and owner outside of a public utility's employee pension plan was nothing

more than a gift in disguise and should not be included in cost of service charged to ratepayers (*Town of New Shoreham v. Rhode Island Public Utilities Commission,* 464 A.2d 730, 733,736 (R.I. 1983)). The Court stated that "...it is apparent that gifts to executives and employees disguised as pension payments are not recognized as proper operating expenses (citation omitted). Similarly, when a company has no established policy governing pension payments and payments are made within the discretion of the board of directors, the commission should not recognize the payment as an operating expense" (*Id.* at 737).

Similarly, the Company has paid benefits to Mr. Edwards that were the same as benefits disallowed in the Company's 1991 rate case, involving another owner who, like Mr. Edwards, was not an officer. The Company also ignored this precedent.

The giving away of electric service, while permitted under Rhode Island law relating to rate discrimination, should be considered imprudent in this case. The financial straits claimed by the Company make such a give away imprudent, as it contributes to the Company's failure to meet the 2007 OTIER RUS coverage ratio. Even if giving away electric service is permitted with regard to the issue of rate discrimination, such a give away should be disallowed as an imprudent affiliate transaction that causes financial harm to the utility.

The Island Services, Inc., affiliate transaction, discussed above, is another example of an abuse of the Company and its ratepayers by the owners for their personal financial gain. It is unreasonable for a public utility to pay rent to an affiliate corporation for office building space owned and recorded on the books of the public utility. The fact

that this transaction generated discovery and hearing time is a function of ownership self-dealing and imprudence.

iii. Disregard for Commission Concerns

The Company also ignored Commission expressions of concern regarding its practices. In its Report and Order, Docket No. 3655 (issued September 13, 2005) at 17, the Commission expressed its concern about that "...there were no policies in place for various situations or that the policies have not been applied equally to all company officials/employee, for example, with regard to vehicle usage and pensions. This is a concern to the Commission which should be addressed in the future." The Company took no steps to address these concerns. The disregard of pension considerations is discussed above. It was determined that the Company has treated personal use of Company vehicles as additional compensation to the owners, without any documentation of the amount of personal use involved and without any Form 1099s being provided to these owner/officer-independent contractors.

In sum, the Company's rate case expenses are a function of its own imprudence. It was disingenuous for the company to blame its rate case expenses on the Town.[30] The Town has raised legitimate issues, some of which could have been avoided if the Company had made a good faith rate filing that tracked Commission precedent. In order to mitigate the impact of the Company's imprudent actions on ratepayers, the Commission should disallow one-third of its rate case expenses and require a 3 year amortization period for recoverable rate case expenses.

[30] Dr. Casazza also encouraged the Town to ask questions about the Company's operations in the context of this rate case (TOWN Exh. 12; Tr. 5/9/08 at 135).

G. BIPCO SHOULD BE DIRECTED TO COMPLY WITH DIVISION REGULATIONS REGARDING METER TESTING AND REPORTING

The Company has stated that its current policy for meter testing is to test new meters at the time of installation (Tr. 5/9/08 at 147, 148). Division regulations relating to meter testing require the testing of all meters periodically after they are installed (TOWN Exh. 14 at 8-10). The Company does not comply with the Division's meter testing regulations. In addition, the Company admitted that it does not file annual reports with the Division (the Periodic Meter Test Report or Selective Meter Test Report) as required under Division rules (TOWN Exh. 14 at 15; Tr. 5/9/08 at 148). The Commission should direct the owners to bring the Company's meter testing and reporting practices into compliance with the Division's rules.

IV. CONCLUSION

For these reasons stated above, the Commission should disallow the proposed rates of Block Island Power Company. Based upon its recommendations and several recommendations of the Division supported by the Town, the Town recommends that the Company be allowed a rate increase of no more than $77,342. The Town has appended to its Brief schedules that compare the positions of the Company, the Division (per its testimony) and the Town. The Commission should adopt the Town other recommendations contained herein for the reasons stated.

Respectfully submitted,

TOWN OF NEW SHOREHAM

By its attorneys,

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Dated: May 20, 2008

BLOCK ISLAND POWER COMPANY
RATE YEAR REVENUE REQUIREMENT

	Company Position (A)	Division Position (B)	Town Position
Cost of Service	$2,653,670	$2,473,639	$2,384,994 (C)
Miscellaneous Revenues	$185,439	$185,439	$201,400 (D)
Net Revenue Requirement	$2,468,231	$2,288,200	$2,183,594
Tariff Revenues, Present Rates	$2,106,252	$2,106,252	$2,106,252
Revenue Deficiency	$361,979	$181,948	$77,342
Percentage Rate Increase	17.19%	8.64%	3.67%

(A) WEE- 2, Rebuttal
(B) DJE- 1S
(C) Town Schedule 2
(D) Town Schedule 5

Town Schedule 2

BLOCK ISLAND POWER COMPANY
COST OF SERVICE

	Company Position	(A)	Division Position	(B)	Town Position	
Operation and Maintenance	$1,843,592		$1,719,719		$1,584,402	(C)
Depreciation	$344,493		$344,493		$344,493	(D)
Taxes Other Than Income Taxes	$164,919		$157,718		$162,228	(E)
Income Taxes	$30,129		$21,092		$29,741	(F)
Return on Rate Base	$270,537		$230,618		$264,130	(G)
Total Cost of Service	$2,653,670		$2,473,640		$2,384,994	

Sources:
(A) WEE-3, Rebuttal
(B) DJE-2S
(C) Town Schedule 3
(D) Town Schedule 4
(E) Town Schedule 5
(F) Town Schedule 6
(G) Town Schedule 7

Town Schedule 3

BLOCK ISLAND POWER COMPANY
OPERATION AND MAINTENANCE EXPENSES

	TOWN ADJUSTMENTS TO COMPANY POSITION	EXPENSES	REVENUES
1	Payments to Owners (1)	$68,000	
2	Pension Expense	$24,000	
3	Adjustments to Owners' Benefits (3)	$33,425	
4	Imputed Revenue for Free Boat Storage by Owner (4)		$1,200
5	Elimination of Island Services Rental Expense (5)	$5,000	
6	Amortization of Meter Reading Methods Study (6)	$8,000	
7	Non-Recurring Clean-Up Expenses (7)	$13,999	
8	Normalization of Board Meeting Expenses (8)	$3,184	
9	Revenue Credits From Verizon and Block Island Cable (9)		$9,961
10	Normalization of Tree Trimming Expenses (10)	$2,335	
11	Credit for Gain on Sale of Time Shares (11)		$4,800
12	Disallowance-Imprudent Rate Case Expense (12)	$18,333	
13	Production Maintenance-Per Division (13)	$58,917	
14	Prior Rate Case Expense-Per Division (14)	$15,169	
15	Lobbying-Per Division (15)	$3,825	
	TOTAL RATE CASE ADJUSTMENTS	$254,187	$15,961
16	BLOCK ISLAND POWER COMPANY OPERATION AND MAINTENANCE EXPENSES	$1,584,402	

NOTES:

(1) RLC Surrebuttal at 24, line 11 [adjusted for rate year level]
(2) Per Division and La Capra Direct at 29
(3) RLC Rebuttal at 24, line 11 [adjusted for rate year level]
(4) Town Brief
(5) Town Brief
(6) Town Brief
(7) Town Brief
(8) Town Brief
(9) Town Brief
(10) Town Brief
(11) DJE-3S
(12) Town Brief
(13) DJE-3S
(14) DJE-S
(15) DJE3-S
(16) WEE-1 less Town Adjustments

BLOCK ISLAND POWER COMPANY
ADJUSTMENTS TO DEPRECIATION EXPENSE

Adjustments	Depreciation Expense Adjustment
Engine 24 Overhaul	$28,735
2008 Bucket Truck	$12,900
Total Adjustments	$41,635
Adjusted Depreciation Expense	$344,493

Town Schedule 5

BLOCK ISLAND POWER COMPANY
ADJUSTMENTS TO TAXES OTHER THAN INCOME TAXES

Operation and Maintenance Expenses (A)	$1,584,402
Depreciation (B)	$344,493
Taxes Other Than Gross Receipts and Income Taxes (C)	$58,772
Income Taxes (D)	$29,741
Return on Rate Base (E)	$264,130
Miscellaneous Revenues (F)	$201,400
Net Revenue Requirement Excluding Gross Receipts Tax	$2,482,938
Gross Receipts Tax Gross-up Rate 0.04/(1-0.04)	4.167%
Pro Forma Gross Receipts Tax	$103,456
Company Pro Forma Gross Receipts Tax	$106,147
Adjustment to Company Expenses	$2,691

Sources:

(A) Per Town Schedule 3
(B) Per Town-Schedule 4
(C) Per Division- Schedule DJE-5S
(D) Per Town Schedule 6
(E) Per Town Schedule
(F) WEE-2 Rebuttal plus Other Revenue Adjustments From Town Schedule 3 (= $15,961)

BLOCK ISLAND POWER COMPANY
INCOME TAX EXPENSE

Rate Base	**$3,981,104**
Weighted Return on Equity	**2.72%**
Taxable Income Base	**$108,475**
Taxable Income (A)	**$138,977**
Effective Income Tax Rate-(B)	**21.4%**
Net Income Tax Expense	**$29,741**

NOTES:

(A) Methodology Per Schedule DJE-6S
(B) Methodology Per Schedule DJE-6S

Town Schedule 7

BLOCK ISLAND POWER COMPANY
RETURN ON RATE BASE

	COMPANY (A)	DIVISION (B)	TOWN
Net Utility Plant	$4,344,550	$4,344,550	$4,365,216 (C)
Working Capital	$165,382	$165,382	$158,683 (D)
Inventory	$116,517	$116,517	$116,517
Prepaid Expenses	$27,284	$27,284	$27,284
Accrued Maintenance Reserve	($146,878)	($257,917)	($257,917)
Deferred Credits	($160,478)	($160,478)	($160,478)
Deferred Taxes	($268,201)	($268,201)	($268,201)
Net Rate Base	$4,078,176	$3,967,137	$3,981,104
Rate of Return	6.63%	5.81%	6.63%
Return on Rate Base	$270,383	$230,491	$264,130

Sources:
(A) Schedule WEE-13, Rebuttal
(B) Schedule DJE-7S
(C) Plant Increased by $20,666 for inclusion of Second Floor of Office in Rate Base
(D) Working Capital Adjusted for $255,517 O&M Decrease with 9.62 Net Lag Days

Town Schedule 8

BLOCK ISLAND POWER COMPANY
RATE OF RETURN

Company Position (1)	Percent	Cost	Weighted Cost
Long Term Debt	74.05%	5.28%	3.91%
Common Equity	25.95%	10.50%	2.72%
Total Capital	100%		6.63%
Division Position (2)			
Long Term Debt	74.05%	5.28%	3.91%
Zero Cost Capital	7.82%	0.00%	0.00%
Common Equity	18.13%	10.50%	1.90%
Total Capital	100%		5.81%
Town Position (3)			
Long Term Debt	74.05%	5.28%	3.91%
Paid in Capital	16.20%	10.50%	1.70%
Common Equity	9.75%	10.50%	1.02%
Rate Base Offset (1)	*		*
Total Capital	100%		6.63%

(1) Schedule WEE-14, Rebuttal
(2) Schedule DJE-8S
(3) Town credits 100% of Net Gain Ratepayers ($828,196) in Form of an Offset to Rate Base (credit) beginning on the sooner of the completion of the proposed Distribution System Upgrades or 24 Months from the Order in 3900.

BLOCK ISLAND POWER COMPANY
PROPOSED CAPITAL STRUCTURE

	$	%	
Long Term Debt (A)	3,787,060	74.05%	
Shared Gain on Sale of Property (B)	828,196	16.20%	
BIPCo Common Equity	498,652	9.75%	
Average Common Equity-Total (A)	1,326,848	25.95%	
Total Capital	5,113,908	100%	
Sources:			
(A) Schedule WEE-14			
(B) Gain on Sale of Assets	$927,213		Schedule DGB-2
Expenses on Sale	$99,017		Schedule DGB-2
Net Gain	$828,196		