



Eric Stinneford - Vice President, Controller and Treasurer of Central Maine Power

LD 1708 An Act To Create the Pine Tree Power Company, a Nonprofit Utility, To Deliver Lower Rates, Reliability and Local Control for Maine Energy Independence

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Testifying: In Opposition

Senator Lawrence, Representative Berry and Members of the Energy, Utilities & Technology Committee, my name is Eric Stinneford. I am Vice President, Controller and Treasurer of Central Maine Power Company (CMP) and I am here today testifying in opposition to LD 1708 An Act To Create the Pine Tree Power Company, a Nonprofit Utility, To Deliver Lower Rates, Reliability and Local Control for Maine Energy Independence.

Like Mr. Flanagan who testified before me, I am lifetime resident of Maine, raised in the mountains of Franklin County, educated in Maine schools and I care deeply about our state and its people. For the past 40 years, I have had the privilege of working for CMP. That's roughly one-third of the Company's history.

The primary purpose of my testimony today is to provide accurate information about CMP's financial structure and the tax impact on Maine of a government takeover. In particular, I refute representations to the effect that Maine's investor owned utilities currently have a "guaranteed" cost of capital as high as 14% and that this represents several multiples of the attainable cost of capital for the proposed "Pine Tree Power Company." This is simply not accurate, and greatly exaggerates CMP's actual earnings.

**Rate of Return.** Utility rates are made up of many components. About half of what customers pay for electricity is made up of electric generation service which is not controlled by CMP, and a state takeover would not have any impact on these rates. Another portion of rates is made up of government fees such as the PUC assessment and contributions to Efficiency Maine Trust. These fees would not change with a government takeover.

The portion of rates impacted by a government takeover are CMP's transmission and distribution rates. The rates for transmission services are regulated at the federal level by the Federal Energy Regulatory Commission (FERC), and distribution rates are regulated at the state level by the Maine Public Utilities Commission (MPUC). Both agencies establish "just and reasonable" rates that allow utilities an **opportunity** to recover their prudently incurred costs of providing safe, reasonable and adequate service. The emphasis on opportunity is important for reasons that I will explain.

Drilling further into CMP's T&D rates, there are two basic components: operating expenses, and capital expenses. Operating expenses are the single largest component, and they cover employee salaries, fuel, supplies, and the like. These costs are paid for in rates at cost, with no markup. Shareholders do NOT earn a rate of return on operating expenses. If LD 1708 were to pass, and there was no change in salaries or operations, there would be no difference in rates before or after a government takeover. However, under LD 1708, the new power authority would be directed to hire a third-party private contractor to operate the

grid, which would actually raise operating costs since all of the employees would be private contractors rather than direct employees of the power authority.

The remaining portion of rates relates to capital, and this is where there is a difference between government ownership and private ownership. However, the difference is much smaller than government power proponents would have you believe. Not only is CMP’s “allowed” rate of return much smaller than proponents claim, but CMPs “actual” rate of return in recent years has actually been below the likely cost of capital of a state-run utility. Let me explain.

Electric utilities are very capital-intensive businesses and their costs of providing service necessarily include the utility’s cost of financing such capital investments. Regulatory agencies like the FERC and the MPUC conduct rigorous analysis to establish the utility’s cost of capital to be incorporated in setting rates. This analysis includes establishing an appropriate capital structure for the utility – the percentage mix of short-term debt, long-term debt and investor equity, as well as the reasonable cost of each component. The typical capital structure for most utilities includes roughly 45-55% equity with the balance comprised of a blend of short- and long-term debt. The cost of the equity component, or the allowed level of return on shareholder equity (“ROE”), is established using a variety of methods that are designed to establish a reasonable percentage return that is representative of the return required by other similarly situated companies in the industry with comparable degrees of investor risk. There is sound economic theory behind this principle, as investors will not invest equity in a business if the return on their investment is not commensurate with the risk they assume in making the investment. They will simply invest their funds elsewhere where either the returns are higher or the risks are lower. In the context of investor owned utilities, this means that if the allowed ROE established by the regulator is set too low relative to a peer group of utilities of comparable risk profile, they will be unable to attract investment capital on reasonable terms. This can result in either higher costs for customers or under-investment and a degradation of service.

For CMP, the Company’s currently authorized cost of capital for its distribution assets is **7.90%**, as set by the MPUC in its February 2020 rate case order. This includes an allowed ROE of 8.25% and a capital structure with a 50% equity layer. The table below illustrates CMP’s approved distribution cost of capital and structure.

**CMP Distribution Weighted Average Cost of Capital  
from MPUC Order in Docket No. 2018-00194**

<b>Component</b>	<b>Capitalization Percentage</b>	<b>Cost</b>	<b>After-Tax Weighted Cost</b>	<b>Pre-Tax Weighted Cost</b>
Common Equity	50.00%	8.25%	4.13%	5.73%
Preferred Stock	0.02%	6.00%	0.00%	0.00%
Long-Term Debt	47.16%	4.39%	2.07%	2.07%
Short-Term Debt	2.82%	3.50%	0.10%	0.10%
<b>Total</b>	<b>100.00%</b>		<b>6.30%</b>	<b>7.90%</b>

For its transmission assets, the FERC has established CMP’s currently allowed ROE at 11.30% and its total cost of capital at 10.70%. This ROE value has been the subject of multiple ongoing disputes before the FERC since 2010 and is still subject to retroactive revision. In the case of both distribution and transmission, these

authorized cost of capital values are far below the 14% that proponents of LD 1708 have portrayed as CMP's cost of capital.

Returning to the regulatory concept of an "allowed" equity return and an "opportunity" to achieve such returns, notwithstanding the bill proponent's statements to the contrary, there are no guaranties that investor owned utilities will actually achieve these values. In fact, a review of CMP's actual equity returns on its distribution assets over the past several years makes this point very clearly.

CMP Distribution Return on Equity

Year	Allowed ROE	Achieved ROE
2018	9.45%	4.18%
2019	9.45%	6.13%
2020	8.45%	6.22%

There simply is no guarantee that once such rates are established, the utility will actually achieve full recovery of all its costs and will earn its full authorized return on shareholder equity. In every regulatory structure, the utility assumes some degree of risk that it will incur costs that are not recoverable from customers or that its revenue will be insufficient to recoup all its operating expenses. For example, in the years summarized in the table above, CMP incurred millions of dollars of expense associated with storm recovery costs that were not recovered from customers. These costs were absorbed by CMP's shareholders, resulting in earnings that were well below the allowed ROE levels.

Because utility investors accept such risks, they must be compensated by having an *opportunity* to earn a return on their invested equity and this return must be commensurate with the accepted level of risk. In contrast to this feature of investor owned utilities, consumer owned utilities have no shareholders to accept such risks and absorb such unanticipated costs. 100% of the consumer owned utility's costs must either be immediately recovered in rates or financed with additional debt that will eventually be recovered from its customers.

I hope this helps clarify some of these basic principles of utility regulation and dispels some of the egregious misinformation that has been issued by the supporters of this bill.

**Tax implications to the State related to LD 1708.** As a private company, CMP pays taxes to state and local government. Even with these tax payments, CMP's rates are lower than comparable consumer-owned utilities in the region. If LD 1708 were to pass, these tax payments to state and local government would no longer occur because government entities are exempt from state and local taxes.

With regard to local property taxes, CMP is Maine's largest taxpayer, by a wide margin. In 2020, CMP paid approximately \$64 million in property taxes to hundreds of cities and towns within its service territory. Under LD 1708, these payments would disappear but for a provision calling for the new state-run utility to make "payments in lieu of taxes." These "PILOT" payments are intended to offset the loss of property tax revenues of local municipalities, but the payments would only last as long as the Legislature leaves this provision of law in place.

Turning to state taxes, CMP is also one of the state's largest taxpayers. CMP contributes corporate income taxes and sales tax payments to the State General Fund, payments that would disappear under a government-owned utility. In 2020, CMP contributed over \$15 million in corporate income and sales tax

payments to the State of Maine. Under LD 1708, there is no provision for these payments to continue, which would eventually translate into a significant budget hole for Maine's General Fund if a state takeover were to occur.

**Conclusion.** For these and many other reasons, I respectfully urge the Committee to vote ought not to pass on LD 1708. Thank you for considering this testimony.