Attachment A

PUBLIC UTILITY STAKEHOLDER SURVEY

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BACKGROUND

This report presents the findings of an electronic survey that was conducted on behalf of Analytica94. The survey was conducted primarily to determine if industry stakeholders believe that cash flow should be considered in rate case and merger proceedings.

The survey was completed in November, 2014 by Left Brain Concepts, Inc., (LBC) a Denver-area market research and consulting firm. LBC completed the survey directly for Analytica94, a non-profit organization that focuses on the economic regulation of U.S. industries, primarily, but not limited to, the public utility, water/wastewater, transportation and telecommunications industries. The findings presented in this report have been prepared completely independently from Analytica94.

By design, participants represented a range of stakeholders and consisted of advocates, public utility regulators and senior management at public utilities. LBC sent 149 postal service letters inviting people to participate. Recipients of the letters consisted of 52 senior officials at individual state public service commissions at the National Association of Regulatory Utility Commissioners (NARUC), 54 senior officials at individual state consumer advocate organizations at National Association of State Utility Consumer Advocates (NASUCA), senior staff at 40 public utilities and senior staff at the Edison Electric Institute, American Gas Association and a senior official at the Federal Energy Regulatory Commission. Respondents were offered to receive a copy of the results of the survey but did not receive any monetary compensation.

A total of 23 people completed the survey for a response rate of 15%. This is a very good response rate for an unsolicited survey. As reported by market research trade associations American Association for Public Opinion Research (AAPOR) and Council of American Survey Research Organizations (CASRO), most surveys of this nature realize about a 5% response.

As is always present in survey research, there is the potential for response bias; there is the risk that the views of people who responded to the survey differ from those who were invited to participate but not do so.

KEY FINDINGS

Relationship of cash flow to rates for service: Most respondents felt that rates for service should allow for an adequate cash flow – to service obligations, for capital expenditures and new investments, for financial integrity, to facilitate access to credit, to cover operating expenses, to service long term debt, and to avoid or at least reduce the need for financing. A few said that there is no relationship.

Relationship of cash flow to rate of return model: People gave similar responses. In fact, many replied - "see previous response."

Consideration of cash flow in mergers: More people feel that consideration should be given to a public utility's cash flow in mergers. Respondents cited that a positive cash flow allows a utility to invest in infrastructure, that it can and should provide value to customers, that it increases access to and lowers the cost of capital and that it represents the strength or weakness of a utility.

Consideration of cash flow in rate case proceedings: Fewer people believe that consideration should be given to a public utility's cash flow in rate case proceedings. But, comments included that a strong cash flow will allow a utility to make infrastructure investments, that it drives credit ratings and that it helps determine a utility's overall rate of return.

Consideration of free cash flow to rate case proceedings: People gave responses similar to the previous question - that free cash flow should be one but not the only variable that should be considered and that free cash flow is an aspect of the financial strength of a utility.

Determining cash value in mergers: Most replied that the cash value is the net present value of future cash flows which takes into account income, spending, debt, sale of assets and other investment options. A couple of people said that they follow best practices and advice from investment banking firms in determining the cash value of a utility.

Organization: Respondents consisted of two senior staff at public utilities, six consumer advocates and nine public utility regulators. Six people did not respond to the question.

Membership in trade organizations: One respondent works at the Edison Electric Institute, seven were from NARUC and five were from NASUCA. Ten people did not respond to the question.

RELATIONSHIP OF CASH FLOW TO RATES FOR SERVICE

Question: What relationship does/should a public utility's cash flow (CF) have to its rates for service?

Edison Electric Institute
There should be no formulaic relationship between a utilities rates and cash flows from operations. In general, rate increases should result in an increase in cash flows from operations.

NARUC
Cash flow from rates must provide enough free cash to service obligations as they become due especially debt service.

None. Rates are developed primarily from a return on rate base and reimbursement of expenses. In certain circumstances rates can be based on cash flow. Example: Large amounts of capital expenditures on large projects with no cash coming in to offset capital costs.

None.

Indirect, in the sense that free cash flow can influence capital costs, which in turn can influence rates.

The PUC considers cash flow as part of general rate proceedings with lead-lag studies. Additionally free cash flow might be considered in establishing the utility's cost of capital.

Cash flow should certainly be considered especially if a utility is proposing substantial new investments.

Should: An indirect but compatible relationship between cash flow and revenue requirement should be considered when setting rates. Does: Generally, cash flow is not considered and when it is considered it is not considered to be a critical component in setting rates.

NASUCA
Limited to none.

CF should be a factor in rate setting. Rates should provide adequate CF to cover O&M, Depreciation, taxes, amortizations, capital costs and a sizeable piece of capital expenditures.

Cash flow should be sufficient to maintain the utility's financial integrity and to allow it to have free access to credit sources.

It is important that a utility have adequate cash flow to cover prudently incurred operating expenses such as labor, materials and fuel, and service long term debt. These costs are appropriately included in customer rates.

Cash flows determine the accounting results which rates are based on.

Other
The revenue requirement formula does not explicitly take cash flow into consideration; however, it does directly affect cash flow since it determines the amount of revenue that utility tariffs are designed to produce.

It should be evaluated in the context of requested rate increases focused on the need for cash.

Company earnings on investment traditionally control rates. However it has caused overbuilding and inefficiency.

A utility's need for cash working capital is an element of its rates.

It should be related, but not dispositive.

Cash flow serves to reduce debt/equity financing to the extent it provides cash reserves.

RELATIONSHIP OF CASH FLOW TO RATE OF RETURN MODEL

Question: What relationship does/should a public utility's cash flow have to the rate base/rate of return model?

Edison Electric Institute
The greater the level of rate base and/or return as compared to the level of operations and maintenance expenses the greater the cash flows as a percentage of rates needs to be.

NARUC
Cash flow must be considered when deciding if CWIP should be allowed rate base treatment i.e., providing cash flow or just allowed to defer financing costs using AFUDC which does not provide for cash flow.

(Same as previous response). None. Rates are developed primarily from a return on rate base and reimbursement of expenses. In certain circumstances rates can be based on cash flow. Example: Large amounts of capital expenditures on large projects with no cash coming in to offset capital costs.

None.

Cash impacts bond rating; bond rating impacts ROE and cost of debt.

The PUC considers cash working capital when it establishes general rates.

Our Commission allows projected rate bases and the inclusion of CWIP projects that will be completed within one year. This helps improve cash flow and reduces regulatory lag.

Should: Cash flow should be considered as a component of and have an indirect but compatible relationship in the rate base/rate of return model. Does: Cash flow is not often considered in the rate base/rate of return model other than in the context of the 'working capital' component of the rate base.

NASUCA
Limited to none.

CF should cover all components of the ROR model and a normal level of capital expenditures.

To the extent that cash flow is reflected in the utility's working capital, such working capital should offset other rate base items, e.g., plant in service.

Cash must be available to cover operating expenses. To the extent that cash is not sufficient to cover operating expenses the safety and reliability of service is jeopardized. Earnings net of prudent expenses should be adequate to allow the utility to cover debt service obligations and to earn its authorized return. To the extent that they are not, then the utility is entitled to seek a revenue increase. However, the latter occurrence typically does not pose a threat to the safety and reliability of service.

Cash flows determine the accounting results that are the basis of rate of return models.

Other
(Same as previous response). The revenue requirement formula does not explicitly take cash flow into consideration; however, it does directly affect cash flow since it determines the amount of revenue that utility tariffs are designed to produce.

None.

(Same as previous response). A utility's need for cash working capital is an element of its rates.

CONSIDERATION OF CASH FLOW IN MERGERS

Question: What consideration should be given to a public utility's cash flow in mergers?

Edison Electric Institute
Cash flows should be given significant consideration in mergers. The level of positive cash flows indicates the ability of a utility to invest in needed infrastructure.

NARUC
There is always a concern that cash produced in one company will be "Swept" into the other company without cash leaving the first company with weak cash flow, increasing financial risk.

It should be analyzed the same as other aspects of a merger. For example: A public utility should not have cash flow difficulties if internal controls are in place around billing and collections. Utilities that do have cash flow problems are most likely in need of rate adjustments.

None.

Major changes up or down could have an impact on decision concerning value of merger (or lack of harm) to customers.

Nevada statute does not require consideration of the utility's cash flow.

A commission should certainly consider the probable financial structure and viability of the newly formed entity. Cash flow is an important consideration of credit rating agencies and these ratings can positively or negatively impact the utility's cost of capital.

Again, it should be a component to be considered.

NASUCA
Not relevant to rates.

CF of the combined entity must be sufficient to cover the ROR model for each utility.

This depends on the cash positions of the merging utilities and the details of the merger. Merger details should provide positive outcomes to customers as a whole as a result of the merger.

Cash flow must be sufficient to at least cover prudently incurred operating expenses. To the extent a merger diminishes a utility's ability to cover operating expenses and earn its allowed return, without raising rates, then it is not in the public interest. Alternatively, if a merger enhances a utility's ability to cover expenses and earn its return. Any net earnings generated in excess of the allowed return should be credited to customers in the form of lower rates.

Cash flows represent the financial strength or weakness of a company. The financial strength of the companies involved in a merger should be major area of consideration.

Other

Cash flow could be a determinant in a utility's access to capital, which is one of the aspects of a merger the law of our state requires the commission to assess.

It should be used in estimating the value of the target and the merged entities.

Same answer. A utility's need for cash working capital is an element of its rates.

CONSIDERATON OF CASH FLOW IN RATE CASE PROCEEDINGS

Question: What consideration should be given to a public utility's cash flow in rate case proceedings?

Edison Electric Institute
Rate case proceedings should be concerned with cash flows in the same manner that they are concerned with returns. Both of these are necessary to support future investment in the utility by investors so that the utility can make the needed infrastructure investments.

NARUC
If there is any question that cash flow can be weakened with a party's proposal or the end result does not provide sufficient cash flow the regulator must consider it.

(Same response as to the first question.) None. Rates are developed primarily from a return on rate base and reimbursement of expenses. In certain circumstances rates can be based on cash flow. Example: Large amounts of capital expenditures on large projects with no cash coming in to offset capital costs.

None.

Question cannot be answered in the abstract.

Cash working capital requirements and consideration in cost of capital of free cash flow.

Cash flow should certainly be considered in the context of lead lag studies to determine working capital to be included in rate base. Future investments and the utility's credit rating should also be considered. Typically, cash flow is addressed by reducing regulatory lag by allowing CWIP in rate base or use of projected rate base. A lead lag study should also be considered to determine proper balance for working capital in rate base.

Cash flow should be considered in rate case proceedings in the context of funds needed from operations to provide an appropriate credit rating and capital in the provisioning of least cost service and quality of service.

NASUCA
Limited to none.

CF should be considered when determining a utility's overall rate of return in a rate proceeding.

Cash flow (in the context of Working Capital) should provide an offset to plant in service in rate base.

(Same response as to previous question). Cash flow must be sufficient to at least cover prudently incurred operating expenses. To the extent a merger diminishes a utility's ability to cover operating expenses and earn its allowed return, without raising rates, then it is not in the public interest. Alternatively, if a merger enhances a utility's ability to cover expenses and earn its return. Any net earnings generated in excess of the allowed return should be credited to customers in the form of lower rates.

How the accounting results are driven by cash flows needs to be given considerations in rate case proceedings.

Other

(Same response as to first question). The revenue requirement formula does not explicitly take cash flow into consideration; however, it does directly affect cash flow since it determines the amount of revenue that utility tariffs are designed to produce.

It should be evaluated in the context of requested rate increases focused on the need for cash.

CONSIDERATION OF FREE CASH FLOW IN RATE CASE PROCEEDINGS

Question: What consideration should be given to a public utility's free cash flow (FCF) in rate case proceedings?

Edison Electric Institute
It should be given a similar weight to return on equity. Earnings without cash flow will not support capital investment.

NARUC
If there is a question that FCF is not sufficient it must be considered.

None.

Can be a factor among many. In the abstract the question cannot be answered.

FCF considerations are generally considered as part of the cost of capital portion of utility rate cases.

I would probably consider this in the context of the utility's credit rating and credit metrics.

Free cash flow (FCF) should be considered in rate case proceedings as one of and along with the many other components of the overall consideration of cash flow.

NASUCA
Limited to none.

If FCF is low or negative it may show abnormal CAPEX.

Free cash flow that provides insight into the investment quality of the utility may be one of the components used in the determination of an appropriate rate of return.

(Same response as consideration of cash flow in mergers). Cash flow must be sufficient to at least cover prudently incurred operating expenses. To the extent a merger diminishes a utility's ability to cover operating expenses and earn its allowed return, without raising rates, then it is not in the public interest. Alternatively, if a merger enhances a utility's ability to cover expenses and earn its return. Any net earnings generated in excess of the allowed return should be credited to customers in the form of lower rates.

FCF are an indication of financial strength and risk. That should be taken into consideration in selecting an authorized ROE in a rate case proceeding.

Other

(Same response as to relationship of cash flow to rates for service). The revenue requirement formula does not explicitly take cash flow into consideration; however, it does directly affect cash flow since it determines the amount of revenue that utility tariffs are designed to produce.

The sources and uses of a public utility's free cash flow should be determined.

DETERMINING CASH VALUE IN MERGERS

Question: How should a public utility's cash value be determined in proposed mergers? Please provide as much explanation as possible.

Edison Electric Institute
Utilities should be valued from a regulator based upon traditional rate base approaches.

NARUC
I'm not clear on what is meant by "cash value."

Not applicable.

NPV of future earnings, though because this commission does not allow recovery of excess of purchase price over book, the question is not terribly important.

The Commission is not required by statute to address cash value.

Utilities typically hire investment banking firms to prepare valuation reports and analysis which serve as the basis and justification for the merger. Copies of these reports should be obtained and analyzed. We recently reviewed a Reverse Morris Trust transaction that was rejected because shareholders gained at the expense of ratepayers. Utilities will typically provide front end benefits to ratepayers to make the transaction more attractive to commissions, but it is essential that the long term impact of the transaction be considered.

Generally, cash value is determined based on an entity's future cash flows that give consideration to all of the components of cash flow---that include but are not limited to income, rates, capital spending, new debt, retirement of debt, sale of assets, depreciation, other investment options and an expectation of a return of and on capital (hurdle rate, IRR).

NASUCA
Not relevant.

Net book value + value of other assets.

Statutory authority in this jurisdiction allows only for the determination of mergers consistent with the public interest and showing no abuse of market power. In that light, limited evaluation of the merger details is allowed. Reviews are conducted to ensure that accounting entries comply with GAAP.

Unsure about the definition of "cash value". For purposes of merger proceedings the utility value is net book value.

Use the same methods that investment bankers use in estimating value. Preparing a forecasted income statement, balance sheet, and cash flow statement to determine projected cash flows and then discounting those cash flows back to the present to derive a value for the firm. Rules of thumb such as revenue multiples or EBITDA multiples can also be used to determine if a value is reasonable when compared to other transactions in the marketplace.

Other
Not applicable. Cash value is not one of the conditions that the Commission must examine under the Law of our State.

Original cost as defined by the FERC USoA.

ORGANIZATION

Question: Please tell us if your organization is a:

- ❑ *Consumer Advocate*
- ❑ *Public Utility*
- ❑ *Public Utility Price Regulator*

2 - Public Utility
6 - Consumer Advocate
9 - Public Utility Price Regulator
6 – Did not report

MEMBERSHIP IN TRADE ORGANIZATIONS

Question: Please identify the trade organization to which you belong.

- ☐ *American Gas Association*
- ☐ *Edison Electric Institute*
- ☐ *National Association of Regulatory Utility Commissioners (NARUC)*
- ☐ *National Association of State Utility Consumer Advocates (NASUCA)*
- ☐ *None of the above*

American Gas Association
1 - Edison Electric Institute
7 - National Association of Regulatory Utility Commissioners (NARUC)
5 - National Association of State Utility Consumer Advocates (NASUCA)
10 - None of the above / Did not report