

STATE OF VERMONT  
PUBLIC SERVICE BOARD

In Re: Joint Petition of Central Vermont Public Service Corporation ("CVPS"), Danaus Vermont Corp., Northern New England Energy Corporation ("NNEEC") for itself and as agent for Gaz Metro Limited Partnership and its parents, Green Mountain Power Corporation ("GMP") and Vermont Low Income Trust for Electricity, Inc. ("VLITE"), for approval of: PSB Docket No. 7770  
(1) the merger of Danaus into and with CVPS;  
(2) the acquisition by NNEEC of CVPS and certain other Vermont companies; (3) the amendment to CVPS 's Articles of Association;  
(4) the merger of CVPS into and with GMP; and (5) the acquisition by VLITE of a controlling interest in Vermont Electric Power Company, Inc.)

BRIEF OF THE VERMONT ELECTRIC POWER COMPANY, INC.

In this proceeding, the Public Service Board has been asked to approve a series of transactions that will consolidate Vermont's two investor-owned public utilities: Green Mountain Power Corporation (GMP) and the Central Vermont Public Service Corporation (CVPS). Together these utilities own a majority interest in the Vermont Electric Power Company, Inc. (VELCO), manager of the state's high-voltage electric transmission network.<sup>1</sup> VELCO and its sister companies, Vermont Transco LLC and Vermont Electric Transmission Company, Inc., appeared in this proceeding to ensure that any changes to VELCO's governance necessitated by the proposed merger will not impair the Company's ability to provide efficient and cost-effective electric transmission service consistent with the Company's duties to shareholders,

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<sup>1</sup> Exh. VELCO NMB-4 at 3.

customers, regulators and other stakeholders.<sup>2</sup> VELCO submits this brief on the governance issues presently before the Public Service Board to assist the Board in its consideration of these issues.

VELCO was founded in 1956 to own and operate the state's high-voltage electric transmission network.<sup>3</sup> In 2006, VELCO's owners, who are the state's electric distribution companies, reorganized the company for tax efficiency reasons.<sup>4</sup> Vermont Transco LLC, a limited liability company, was created to own the transmission assets that VELCO now manages and operates.<sup>5</sup> The reorganization did not change the role of VELCO's board of directors to make the big-picture decisions related to financing and major capital investments in the high-voltage transmission system VT Transco now owns.<sup>6</sup> Since its founding in 1956, the VELCO board has been comprised of the chief executives of the investor-owned distribution utilities and the larger municipal and cooperative utilities.<sup>7</sup> In more recent years, VELCO's board has included independent directors who were recruited for a particular expertise needed by VELCO at the time.<sup>8</sup> For example, the board recruited two of its three current independent directors from the construction industry as a result of the Company's major capital construction program underway

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<sup>2</sup> Docket No. 7770, Order of 11/1/2011 at 5.

<sup>3</sup> Dutton pf. at 3-4.

<sup>4</sup> Dutton pf. at 4.

<sup>5</sup> Dutton pf. at 4.

<sup>6</sup> Dutton pf. at 7.

<sup>7</sup> Dutton pf. at 6.

<sup>8</sup> Dutton pf. at 6-7.

since 2004.<sup>9</sup> These independent directors do not have any affiliation with the retail electric distribution utilities that own VELCO.<sup>10</sup>

VELCO has performed well under its existing governance structure.<sup>11</sup> The Company's board of directors is properly focused on its oversight role and serving the best interests of all of VELCO's shareholders.<sup>12</sup> Change in VELCO's governance is required in the context of this proceeding only to address the single VELCO-related issue arising from the merger: the concentration of power in one shareholder, otherwise referred to as "tyranny of the majority."<sup>13</sup> The solution to address the risk of "tyranny of the majority" should recognize VELCO's proven successes in meeting its public service obligations and in attracting low-cost third-party capital to help finance critical transmission system upgrades.<sup>14</sup> The solution need not include radical changes to VELCO's governance as some parties have suggested.<sup>15</sup>

Changes that have been proposed by parties in the proceeding range from one-utility/one-vote representation on the VELCO board of directors irrespective of ownership stake or utility size<sup>16</sup>, to the possible public or cooperative ownership of VELCO.<sup>17</sup> All of these proposals are based on a faulty premise — that an inherent

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<sup>9</sup> Tr. 3/28/2012 at 69 (Dutton); tr. 4/4/2012 at 37 (Powell).

<sup>10</sup> Dutton pf. at 7.

<sup>11</sup> Dutton pf. at 24; Brownell pf. at 31; Dutton reb. pf. at 2; tr. 3/28/2012 at 41 (Dutton).

<sup>12</sup> Dutton pf. at 22.

<sup>13</sup> Brownell pf. at 32; Dutton pf. at 23.

<sup>14</sup> Dutton pf. at 18-19, 24, 32, 33, 34; Exh. NMB-4 at 3; Dutton reb. pf. at 2-3; Brownell reb. pf. at 10.

<sup>15</sup> *See, e.g.*, Dworkin pf. at 32-38; Kandel pf. at 4, 9-11; Burt pf. at 20.

<sup>16</sup> Burt pf. at 20.

<sup>17</sup> Kandel pf. at 4, 9-11; Patt pf. at 11-12.

conflict exists between VELCO's public service obligation and its directors' and executive management's fiduciary duties — and the mistaken belief that the VELCO boardroom is an appropriate forum to resolve operational disputes between and among the state's distribution utilities and VELCO.<sup>18</sup> There is no inherent conflict, however, because VELCO's board and management cannot fulfill their fiduciary duties to VELCO and its shareholders without ensuring that VELCO fulfills its core public service mission.<sup>19</sup> As to the board of directors serving as a place to resolve operational disputes, the VELCO Operating Committee serves that purpose.<sup>20</sup> The suggestion by some parties that VELCO's utility executive directors participate in board meetings to advance their own distribution utility's interest reflects a fundamental misunderstanding of the role of the board, its directors' fiduciary duties, and how VELCO's board has operated in practice.<sup>21</sup>

On March 27, 2012 the Joint Petitioners and the Department of Public Service (collectively the "Settling Parties") filed a Memorandum of Understanding with the Board that incorporates a governance proposal for VELCO that, while lacking certain specifics that would be desirable in ensuring an appropriate governance structure for VELCO, offers a solid foundation for agreement among VELCO's shareholders.<sup>22</sup> The MOU calls for CVPS to transfer 38% of its voting shares in VELCO to a non-profit

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<sup>18</sup> Dutton reb. pf. at 3, 10, 11-12; Brownell reb. pf. at 11-13.

<sup>19</sup> Dutton pf. at 7, 26.

<sup>20</sup> Dutton pf. at 17-18; Dutton reb. pf. at 3, 9-10, 12; Exh. VELCO-CLD-5; Exh. VELCO-CLD-3a.

<sup>21</sup> Dutton reb. pf. at 9; Burt pf. at 15-18.

<sup>22</sup> Memorandum of Understanding between the Petitioners and the Vermont Department of Public Service (3/26/2012) ("MOU").

entity established for that purpose: the Vermont Low Income Trust for Electricity, Inc. or “VLITE.”<sup>23</sup> VLITE’s directors will be first appointed by GMP at the direction of the Department of Public Service, then subject to the bylaws established by the VLITE board consistent with Title 11B.<sup>24</sup> Under the MOU, VLITE will nominate three directors to VELCO’s board and must support the nomination of two independent directors nominated by VELCO’s public power and cooperative utility owners.<sup>25</sup> VPPSA, Burlington Electric Department, and Vermont Electric Cooperative would each nominate a director, and VELCO’s President would continue to serve on the board.<sup>26</sup> Thus, the MOU would retain the existing 13-member board of directors with two of the thirteen being independent from VELCO’s shareholders.<sup>27</sup> The MOU does not provide guidance on the meaning of “independence” for the two independent directors nominated by VELCO’s public power owners.

The Settling Parties themselves have recognized the desirability of working with VELCO’s other owners to address certain questions not answered in the MOU, and since the close of hearings, the MOU has provided the basis for discussions among VELCO’s owners and with the Department of Public Service.<sup>28</sup> We believe that certain issues of importance for VELCO’s governance — in particular, criteria for independent directors and the applicability of those criteria to VLITE director-

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<sup>23</sup> MOU at ¶ 7.

<sup>24</sup> MOU at 8; tr. 4/4/2012 at 128 (Miller); tr. 4/4/2012 at 24 (Powell).

<sup>25</sup> MOU at ¶ 11.

<sup>26</sup> MOU at ¶ 11.

<sup>27</sup> MOU at ¶ 11; tr. 3/28/2012 at 32, 33 (Dutton).

<sup>28</sup> Tr. 4/3/2012 at 166 (Reilly); tr. 4/3/2012 at 234-236 (Powell); tr. 4/4/2012 at 121 (Miller).

nominees to VELCO's board, so that the number of independent directors on VELCO's board will be increased rather than decreased — have recently been resolved in those discussions, and that a formal agreement addressing these issues signed by most if not all of VELCO's owners will be filed in the near future, certainly before reply briefs are due in this case.<sup>29</sup> In the absence of a forthcoming agreement, the Public Service Board might consider offering guidance on these criteria and encouragement that VLITE's three VELCO director nominees meet independence criteria.<sup>30</sup> Independence in this context should mean, at a minimum, no significant business, financial, or familial relationship with VELCO or any of its shareholders, or its or their officers, directors, or shareholders. A good model for such criteria can be found in the New York Stock Exchange standards for independent directors.<sup>31</sup>

#### CONCLUSION

There is abundant evidence in the record regarding the benefits that the merger of GMP and CVPS offers to their customers and Vermont as a whole. VELCO's CEO has offered his strong personal endorsement of the merger in testimony and in other public settings, and VELCO's comments on the governance issue are not, and have never been, intended to establish a roadblock to approval of the merger.<sup>32</sup> As

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<sup>29</sup> Testimony before the Board suggested that it was appropriate for VELCO's owners to discuss and resolve items left open by the Settling Parties' MOU. See., e.g., tr. 4/4/2012 at 126, 131-132 (Miller); tr. 3/28/2012 at 43, 45 (Dutton).

<sup>30</sup> VELCO is not seeking Board approval of its governance structure or any changes to it that do not require Board approval under existing law.

<sup>31</sup> New York Stock Exchange Listed Company Manual § 303A.02 (Nov. 25, 2009).

<sup>32</sup> Tr. 3/28/2012 at 33 (Dutton).

recognized in this proceeding, however, VELCO serves an important function in the state and has a long track record of meeting the needs of its customers and serving the public interest. The Board in this proceeding should be, and hopefully as a result of the MOU and additional agreement among VELCO shareholders and the DPS will be, confident that VELCO's ability to fulfill its public service obligations in a reliable, safe, efficient and cost-effective manner will not be compromised inadvertently.

Dated: April 23, 2012  
Rutland, Vermont



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