STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 7342

Petition of Central Vermont Public Service Corporation for Approval to issue up to $65 million of Hybrid Capital Unsecured Debt, pursuant to 30 V.S.A. §108	))))

Order entered: 11/20/2007

I. Introduction

On July 25, 2007, Central Vermont Public Service Corporation ("CVPS" or "Company") filed a petition, pursuant to 30 V.S.A. §108, with the Vermont Public Service Board ("Board") seeking approval to issue up to $65 million in Hybrid Capital Unsecured Debt ("hybrid debt"). Proceeds from the loan would be used to finance the acquisition of equity units in Vermont Transco, LLC ("Vermont Transco"). In support of the petition, CVPS submitted the prefiled testimony and exhibits of Pamela Keefe, Vice President, Chief Financial Officer and Treasurer .

On September 21, 2007, the Department of Public Service ("Department") informed the Board that it had reviewed the petition. Based on its review, the Department determined that CVPS's filing was consistent with the *Vermont Electric Plan*, pursuant to 30 V.S.A. § 202(f). By separate letter dated November 7, 2007, the Department notified the Board that it had concluded that CVPS's petition was consistent with the general good of the state, provided the terms of the proposed issuance are consistent with those presented in the petition and supplemental supporting materials. According to the Department, the proposed debt issuance provides CVPS with financial stability and additional financial resources to expand its investment in Vermont Transco.

On October 29, 2007, CVPS submitted responses to my request for additional information. CVPS filed revised responses to the information request on November 5, 2007, after further discussions between CVPS and its investment bankers.

No party has requested a hearing in this matter.

Based on the evidence submitted, I conclude that CVPS's request to borrow up to a maximum aggregate amount of $65 million is consistent with the general good of the state. The funds provided by the proposed loan would be used to acquire newly issued equity units in Vermont Transco.[1] Earnings of approximately $5.7 million from the proposed investment in Vermont Transco, net of cost, would be used to offset CVPS's revenue requirement and result in lower retail rates than would otherwise be the case.[2] In addition, the proposed unsecured debt is considered by rating agencies to be part equity and part debt. As such, the proposed issuance of hybrid debt would enhance CVPS's credit statistics and promote the Company's financial restoration plan.[3] Therefore, I recommend that the Board approve CVPS's petition and issue an order to that effect without hearings or further investigation.[4]

II. Findings

Based on the record evidence, I hereby report the following findings of fact in accordance with 30 V.S.A. § 8.

1. CVPS is a company as defined by 30 V.S.A. § 201, and is subject to the jurisdiction of the Vermont Public Service Board pursuant to 30 V.S.A. § 203. Petition at 1.

2. CVPS intends to purchase its pro rata share of the equity units being offered in Vermont Transco, and may also purchase additional equity units if such units become available through Vermont Transco's over-subscription process. Keefe pf. at 3.

3. CVPS intends to enter into a hybrid capital financing facility to finance the purchase of the proposed equity units in Vermont Transco. Keefe pf. at 4.

4. "Hybrid capital" (also called "junior subordinated debt") is unsecured debt that is considered, in part, to be equity by ratings agencies because it is (a) subordinated to other debt of the issuer, (b) has a maturity date that may be up to 60 years after issue, (c) may have a "call"

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1. *See*, Petition of Vermont Transco, LLC for Authority to Issue up to $150 million in Class A and B Units of Equity, Docket 7310.

2. Exh. CVPS PJK - 4R, Attachment A3.

3. Keefe pf. at 2.

4. To the extent that the final equity unit offering is less than initially planed by Vermont Transco in Docket No. 7310, then CVPS's allotment would be reduced in accordance with the Operating Agreement between Vermont Transco and its members. *See* Docket 7310, Order of October 30, 2007.

feature that requires a "Replacement-Capital Covenant" before the maturity date, (d) may include an option to defer interest payments and (e) has tax-deductibility benefits. These features cause the hybrid debt to have lower priority than the issuer's other debt, and to have higher priority than the issuer's preferred or common stock. It is considered "hybrid" because, for ratings purposes, it has attributes of both unsecured debt and equity. Keefe pf. at 1, 2; exh. CVPS PJK-1.

5. CVPS expects that the proposed financing would be considered to be equivalent to 50% debt/50% equity by the rating agencies. This treatment would support the Company's goal of returning to investment grade by lowering the ratio of total debt to total capitalization, which enhances the Company's adjusted credit statistics. If all of the proposed borrowing were considered to be debt, the resulting adjusted credit metrics would be less favorable to the Company's goal of achieving investment grade status. Keefe pf. at 2.

6. CVPS considered several other options to finance the acquisition of Vermont Transco equity units including but not limited to issuing secured debt. Issuing secured debt would have been a less expensive option, but would have negative consequences on CVPS's plan to improve the Company's credit rating. Issuing common equity shares would have been too expensive and would likely result in few, if any, net benefit to ratepayers. Keefe pf. at 5.

7. CVPS's earnings on current holdings of Vermont Transco equity units have provided financial benefits to the Company and its ratepayers through offsetting the Company's revenue requirement that would otherwise be recoverable through rates. Keefe pf. at 3.

8. CVPS reflected in Docket 7321 (its pending rate proceeding) roughly $5.7 million in net benefits as a result of the spread between the interest rate on the proposed hybrid debt facility and the earnings on Vermont Transco equity units. The positive earnings are expected to result in lower retail rates than would otherwise be the case. Keefe pf. at 5; exh. CVPS PJK - 4R, Attachment A3.

9. CVPS anticipates that the hybrid debt facility would include a 30-year term, call options after 5 or 10 years with a call premium, a "replacement capital" covenant, and other commercial terms consistent with such facilities and the Company's existing financing covenants. Keefe pf. at 4, exh. CVPS PJK - 4R, pg. 4.

10. The replacement capital covenant requires the replacement of the principal amount of the proposed hybrid debt, at maturity or redemption prior to maturity, with the securities for which CVPS receives an equivalent amount of equity credit from the rating agencies. Exh. CVPS PJK - 4R, pg. 2.

11. The interest rate of the proposed hybrid debt facility may be based on the 5- or 10-year Treasury bill, plus 275 to 300 basis points. Depending on the option CVPS chooses at the time of closing, the interest rate would be fixed for either the first five or ten years of the loan. Keefe pf. at 4, exh. CVPS PJK - 4R, pg. 4.

12. The underwriting fee for the proposed hybrid debt facility is 2.5 percent of the total amount of the debt securities to be issued, and the legal fees are not anticipated to exceed $50,000. Keefe pf. at 4-5.

13. The effective interest rate of the proposed hybrid debt is approximately 8.01 percent. This rate includes an amortization of the underwriting and legal fees, in accordance with GAAP, over 10 years and is based on a nominal interest rate of 7.75 percent. Exh. CVPS PJK - 4R, pg. 2 and Attachment A3.

14. Investments in Vermont Transco equity units are expected to yield an after-tax return of 11.5 percent. Exh. CVPS PJK - 4R, Attachment A3.

15. If CVPS were to call the hybrid debt prior to the end of the initial fixed rate period, CVPS would have to pay a "make-whole" premium. Exh. CVPS PJK - 4R, Attachment A1a and pg. 3 -6.

16. Prior to the end of year 10, rating agencies are likely to treat the proposed hybrid facility as 50% equity/50% debt, which would provide CVPS with additional credit metric support. After year 10, the rating agencies may treat the proposed hybrid debt as 100% debt. On CVPS's books the proposed hybrid facility is booked as 100% debt and would provide CVPS with tax benefits because the interest expense would be tax deductible. Exh. CVPS PJK - 4R, pg. 5.

17. In the event of a material change in the terms or conditions of the proposed hybrid debt facility, CVPS would notify the Board and the Department. Keefe pf. at 8.

18. CVPS's Board of Directors has provided its preliminary approval of the proposed financing. However, the Company must also receive further approval by the Executive Committee of its Board of Directors. Keefe pf. at 8.

19. The proposed financing is consistent with the Vermont Electric Plan, pursuant to 30 V.S.A. §202(f). Department letter of September 21, 2007.

III. Conclusion

Based on the evidence, I find that CVPS's request to issue hybrid debt up to the aggregate amount of $65,000,000 is consistent with the public good. Proceeds from the unsecured debt issuance would be used to acquire additional equity units in Vermont Transco. The net earnings from the Vermont Transco investment would then be credited by CVPS as a reduction to the Company's revenue requirement. In addition, terms of the proposed hybrid debt issuance support CVPS's goal of returning to investment grade status, as 50 percent of the debt would be considered by the rating agencies to be a form of equity. As a result, the Company's ratio of debt to total capitalization would be reduced for the purpose of assessing CVPS's credit quality. Because the proposed financing request is expected to result in net benefits to CVPS ratepayers, I recommend that the Board consent to the Company's request, as proposed, without hearing or further investigation. To the extent that the number of equity units issued and offered by Vermont Transco is less than CVPS anticipates, the amount of hybrid debt securities issued should be reduced to fund only CVPS's pro rata share of equity units offered in accordance with Vermont Transco's operating agreement.

I further recommend that the Board's order provide that it does not constitute approval of any particular capital or operating expenditure nor the underlying capital structure that CVPS may implement, and that it shall not preclude the Department or any other party, or the Board, from reviewing and/or challenging those expenditures and/or CVPS's resulting capital structure in any future proceeding.

Opportunity to File Exceptions and Present Argument

By letter dated November 2, 2007, CVPS filed a waiver of its rights to file exceptions and present arguments under 3 V.S.A. § 811. By separate letter dated November 7, 2007, the Department also filed its waiver of rights under 3 V.S.A. § 811.

Dated at Montpelier, Vermont, this 16th day of November, 2007.

s/ Thomas S. Lyle
Thomas S. Lyle
Hearing Officer

IV. ORDER

IT IS HEREBY ORDERED, ADJUDGED AND DECREED by the Public Service Board of the State of Vermont that:

1. The Findings, Conclusion and recommendations of the Hearing Officer are adopted.

2. Central Vermont Public Service Corporation's ("CVPS") request to issue Hybrid Capital Unsecured Debt ("hybrid debt"), as described herein, in an amount that is not to exceed $65 million is consistent with the general good of the state and is approved.

3. Should the amount of Vermont Transco equity units issued and offered to CVPS be less than anticipated in this filing, CVPS shall reduce the amount of hybrid debt necessary to acquire such equity units actually issued and offered by Vermont Transco.

4. This Order does not constitute approval of any particular capital or operating expenditure nor the underlying capital structure that CVPS may implement. Nothing in this approval shall preclude the Department or any other party, or the Board, from reviewing and/or challenging those expenditures and/or CVPS's resulting capital structure in any future proceeding.

5. CVPS shall obtain prior final approval from the Executive Committee of its Board of Directors and provide a copy of the Executive Committee's resolutions to the Board and Department.

6. CVPS shall inform the Board and the Department of any material change in the terms and conditions of the hybrid debt, if any, prior to closing.

7. Upon request, CVPS shall provide the Board and the Department with a complete set of final executed documents.

Dated at Montpelier, Vermont, this 20th day of November, 2007.

s/ James Volz	)	PUBLIC SERVICE
	)	
s/ David C. Coen	)	BOARD
	)	
	)	OF VERMONT
s/ John C. Burke	)	

OFFICE OF THE CLERK

FILED: November 20, 2007

ATTEST: s/ Susan M. Hudson
Clerk of the Board

NOTICE TO READERS: This decision is subject to revision of technical errors. Readers are requested to notify the Clerk of the Board (by e-mail, telephone, or in writing) of any apparent errors, in order that any necessary corrections may be made. (E-mail address: psb.clerk@state.vt.us)

Appeal of this decision to the Supreme Court of Vermont must be filed with the Clerk of the Board within thirty days. Appeal will not stay the effect of this Order, absent further Order by this Board or appropriate action by the Supreme Court of Vermont. Motions for reconsideration or stay, if any, must be filed with the Clerk of the Board within ten days of the date of this decision and order.