Date Filed: October 06, 2026

Witness: Matthew Nelson and Michael Goldman
Request from: Public Utilities Regulatory Authority

Question:

Reference Application, Ex. CLP-IAP-1, pp. 30–31. Explain the role of performance-based regulation in the Investment Calibration Framework. State whether Eversource considers performance-based regulation necessary to keep capital investment within the calibrated range. If not, identify the specific mechanisms or controls Eversource relies upon to keep capital investment within that range.

Response:

Please refer to the Company's response to UPA-033[i] for the role of performance-based regulation in the framework.

The Company does not consider performance-based regulation necessary to keep capital investment within the calibrated range. Whether it is the right structure depends on the utility and its circumstances. Moreover, the regulatory framework in place (e.g., multi-year rate plan, PBMRP, traditional cost of service rate cases, etc) does not, in isolation, dictate whether a level of capital investment can be maintained within a calibrated range, or not. The Company is responsible to provide safe and reliable service to its customers and in that capacity must be able to respond to a emergent system conditions, such that the Company may be required to invest at levels above (or below) those anticipated, or levels which are supported within a particular regulatory framework.

That said, given the factors at play for CL&P and described in this proceeding, the Company considers the PBMRP the appropriate structure that will support the level of ongoing system investment projected for the term of the PBMRP, with annual and overall rate changes that comport with the Investment Calibration Framework described in Exhibit CLP-IAP-1. It is important to note as well that, under the Company's proposal, customers pay the lesser of the forecast or the cost of plant actually placed in service, and spending above the forecast is subject to regulatory lag for review in a future rate case proceeding. Exhibit CLP-IAP-1 describes the Company's proposal, including the capital allowance that provides revenue for the term of the PBMRP that is capped at the approved forecast and reconciled only downward, paired with an O&M-focused performance mechanism, as consistent with the regulatory toolkit identified in the Lawrence Berkeley National Lab (LBNL) LBNL study (p. 61, ll. 14–19; see also p. 30, l. 13 – p. 31, l. 3). The Company's planning testimony documents a need for sustained investment. While affordability is a major concern, the Company's historical capital costs are below benchmark, and

a capped capital envelope combined with a formula for O&M pairs that investment with cost discipline. The appropriate ratemaking structure can change and adapt over time as circumstances change.

The mechanisms and controls the Company relies upon are identified in the response to UPA-033.

Prior Referenced Response:

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[i] UPA-033 Question:
Reference Application, Ex. CLP-IAP-1, pp. 30–31. Explain the role of performance-based regulation in the Investment Calibration Framework. State whether Eversource's framework depends on implementation of a performance-based ratemaking structure to maintain capital investment within the calibrated range and identify any PIMs, metrics, or mechanisms used to evaluate capital investment. If not, identify how the framework maintains investment within the calibrated range absent performance-based regulation.

UPA-033 Response:
No ratemaking structure, performance-based or otherwise, determines whether a given investment is effective or efficient (UPA-024[i]). This determination comes as a result of the work of planning, engineering and execution, tested through the Company's project justification and alternatives analysis and, ultimately, PURA's prudence review. What a ratemaking mechanism determines is the financial environment in which those decisions are made and the underlying incentives inherent in the regulatory framework (Ex. CLP-IAP-1, p. 30, ll. 1–12).

Performance-based regulation, properly designed, is the structure that makes calibration achievable and holds it in place over the plan term (p. 30, l. 13 – p. 31, l. 3). The PBMRP follows the methodology of a comprehensive PBR plan, except that its formula applies to O&M only (Ex. CLP-ELP-1, p. 85, ll. 12–19). O&M revenue is adjusted annually by the I − X − S formula, with the Consumer Dividend as the S-Factor. Capital investment is addressed through the Capital Funding Mechanism, which limits recovery to the lesser of the approved forecast or actual plant in service and places the risk of excess capital spending on the Company (pp. 101–102).

An index applied to capital would pass input-price changes through to customers; a fixed forecast does not. The capital forecast underlying the cap was developed by the Company's engineering organization and is described by the Leadership Panel and the System Engineering Panel (Ex. CLP-ELP-1, pp. 64–72; Ex. CLP-TSP-1, pp. 39–61). The intent of the framework proposed by the Company is to advance a regulatory framework that affordably enables cost effective system investment to support the economic vitality of Connecticut, introduces PIMs for transparency and accountability for the duration of the plan, and retains appropriate incentives for the Company to control costs of both O&M and capital spending to the greatest extent possible over the course of the plan.

The framework itself does not depend on performance-based regulation; it is an evaluation lens that PURA can apply under any ratemaking structure. However, the PBMRP is the Company's proposed means of keeping investment within the calibrated range for CL&P over the plan term, balancing recovery of costs with rate stability and gradual year-over-year customer bill impacts. In addition, PBR drives efficiency in utilities working within these confines and supports cost discipline over time. Absent performance-based regulation, that evaluation would occur in base rate cases as part of the prudence review. The Company has stated that, without the PBMRP, it would expect to file rate cases as close to annually as possible (Ex. CLP-ELP-1, p. 85, ll. 1–3).

The mechanisms and controls in the PBMRP that the Company relies upon to keep capital investment within the calibrated range, and to provide transparency and accountability for performance are:

- Capital Funding Mechanism. Revenue is capped based on the approved capital expenditure forecast with an annual, downward-only reconciliation (Ex. CLP-ELP-1, pp. 101–102).
- Reliability PIMs: System Reliability PIMs for blue-sky SAIDI and SAIFI with performance-based benchmarks, and a Customer Reliability PIM targeting repeat CEMI and CELID customers, offered as part of the PBMRP (Ex. CLP-ELP-1, p. 50, ll. 1–9; pp. 106–107, Table 3). These tie the Company's financial results to the reliability the capital program is meant to support. The SAIDI and SAIFI PIMs are penalty-only, with penalties of $1.75 million to $3.5 million each; the Customer Reliability PIM is incentive-only, with an incentive of $1.5 million to $3.0 million.
- Performance Metrics: 16 proposed metrics across three categories, with descriptions, targets and PIM design in Exhibit CLP-ELP-3 (Ex. CLP-ELP-1, p. 103, ll. 10–16).
- Reporting: Capital spending against the approved plan and reliability against commitments, with regular public reporting (p. 57, ll. 3–8); cost-efficiency metrics, reported without targets or penalties (Ex. CLP-ELP-1, p. 112, Table 5; p. 113, l. 5 – p. 114, l. 16).
- Project-Level Review: The reliability benefit-cost model on the record (Ex. CLP-ELP-1, p. 67, ll. 17–19; Ex. CLP-TSP-1, p. 60, ll. 3–7) and prudence review.

The Company's proposals set forth a comprehensive framework in this proceeding, leveraging the Company's experience, and that of its expert consultants work in other jurisdictions, while conforming as closely as possible to the proposed final decisions in PURA's PBR proceedings, in order to propose a framework that could support the level of going-forward system investment needs while operating in a multi-year rate case stay out, which is a fundamental component of PBR frameworks adopted elsewhere. If PURA adopts a framework that materially differs from the Company's proposals, or is not calibrated to support the level of investment needed in the system on a going forward basis, the Company will not be in a position to commit to a rate case stay-out period of four years, which will result in more frequent rate cases, in which all components of the Company's costs will be updated to then-current levels.