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FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

In Reply Refer To:
Office of Enforcement
Docket No. FA19-8-000
February 4, 2022

The Connecticut Light and Power Company
Attention: [redacted]
Director, Federal Regulatory Policy
107 Selden Street
Berlin, CT 06037

Dear [redacted]

1. The Division of Audits and Accounting (DAA) within the Office of Enforcement (OE) of the Federal Energy Regulatory Commission (Commission) has completed an audit of The Connecticut Light and Power Company (CL&P). The audit covered the period from January 1, 2015 through December 31, 2019.

2. The audit evaluated CL&P's compliance with: (1) approved terms, rates, and conditions of its transmission formula rate mechanism as provided in the ISO New England Inc. Transmission, Markets, and Services Tariff on file with the Commission; (2) accounting requirements of the Uniform System of Accounts Prescribed for Public Utilities and Licensees under 18 C.F.R. Part 101; (3) reporting requirements of the FERC Form No. 1, Annual Report of Major Electric Utilities, Licensees and Others, under 18 C.F.R. § 141.1; and (4) the requirements in Preservation of Records of Public Utilities and Licensees under 18 C.F.R. Part 125. The enclosed audit report contains five findings of noncompliance with the requirements listed above, one other matter, and 26 recommendations that require CL&P to take corrective action.

3. On January 20, 2021, you notified DAA that CL&P accepts the five findings and 26 recommendations in the draft audit report and will submit within 30 days of the issuance of the final audit report a plan for implementing the audit recommendations. A verbatim copy of your response is included as Section VI of the audit report. I hereby approve the audit report.

4. CL&P should submit its implementation plan to comply with the recommendations within 30 days of issuance of this letter order. CL&P should make

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quarterly submissions to DAA describing the progress made to comply with the recommendations, including the expected completion date for each corrective action. As directed by the audit report, these submissions should be made no later than 30 days after the end of each calendar quarter, beginning with the first quarter after this audit report is issued, and continuing until all the corrective actions are completed.

5. The Commission delegated the authority to act on this matter to the Director of OE under 18 C.F.R. § 375.311. This letter order constitutes final agency action. CL&P may file a request for rehearing with the Commission within 30 days of the date of this order under 18 C.F.R. § 385.713.

6. This letter order is without prejudice to the Commission's right to require hereafter any adjustments it may consider proper from additional information that may come to its attention. In addition, any instance of non-compliance not addressed herein or that may occur in the future may also be subject to investigation and appropriate remedies.

7. I appreciate the courtesies extended to the auditors. If you have any questions, please contact Mr. Gerald Williams, Director and Chief Accountant, Division of Audits and Accounting at (202) 502-8277.

Sincerely,

JANEL BURDICK Digitally signed by JANEL BURDICK Date: 2022.02.02 07:53:14 -05'00'

Janel Burdick
Director
Office of Enforcement

Enclosure

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Federal Energy Regulatory Commission
Office of Enforcement
Division of Audits and Accounting

AUDIT REPORT

Audit of The Connecticut Light and Power Company's Compliance with:

- Tariff requirements governing its FERC jurisdictional rates;
- The accounting requirements of the Uniform System of Accounts Prescribed for Public Utilities and Licensees;
- The reporting requirements of the FERC Form No. 1; and
- The requirements in Preservation of Records of Public Utilities and Licensees.

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I. Executive Summary

A. Overview

The Division of Audits and Accounting (DAA) within the Office of Enforcement of the Federal Energy Regulatory Commission (Commission) has completed an audit of The Connecticut Light and Power Company (CL&P). The audit evaluated CL&P's compliance with: (1) approved terms, rates, and conditions of its transmission formula rate mechanism as provided in the ISO New England Inc. (ISO-NE) Transmission, Markets, and Services Tariff on file with the Commission; (2) accounting requirements of the Uniform System of Accounts Prescribed for Public Utilities and Licensees under 18 C.F.R. Part 101; (3) reporting requirements of the FERC Form No. 1, Annual Report of Major Electric Utilities, Licensees and Others, under 18 C.F.R. § 141.1; and (4) the requirements in Preservation of Records of Public Utilities and Licensees under 18 C.F.R. Part 125. The audit covered the period January 1, 2015 to December 31, 2019.

B. The Connecticut Light and Power Company

CL&P is an electric transmission and distribution utility operating in Connecticut that is a wholly owned subsidiary of Eversource Energy (Eversource), a public utility holding company. CL&P's electric transmission operations are located within the ISO-NE footprint, and its transmission rates are calculated according to a formula rate in Attachment F of the ISO-NE Open Access Transmission Tariff (OATT).[1] CL&P serves residential, commercial, and industrial customers in Connecticut. It owns and maintains transmission facilities that are operated by ISO-NE.

During the audit period, CL&P's distribution business consisted primarily of the purchase, delivery, and sale of electricity to its residential, commercial, and industrial customers. It furnished retail franchise electric service to approximately 1.2 million customers in 149 cities and towns in Connecticut, covering an area of 4,400 square miles. CL&P did not own any electric generation facilities.

C. Summary of Compliance Findings

Audit staff's compliance findings are summarized below. Section IV of this report contains a detailed discussion of each finding. Audit staff found five areas of noncompliance:

[1] *See* ISO New England Inc. Transmission, Markets, and Services Tariff, Section II, Attachment F 24.0.0.

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1. *Allowance for Funds Used During Construction* (*AFUDC*) – CL&P improperly included accumulated other comprehensive income and unamortized debt-related balances in long-term debt and equity balances used to compute its AFUDC rates. As a result, CL&P over-accrued AFUDC amounts included in utility plant accounts, which led it to overstate its annual transmission revenue requirement and overbill transmission customers.

2. *Accounting for Compromise Settlements* – CL&P incorrectly accounted for compromise settlement costs in operating expense accounts instead of Account 426.3, Penalties, or Account 426.5, Other Deductions, as required. The operating expense accounts used were included in CL&P's transmission formula rate calculations. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

3. *Accounting for Tax Receivables* – CL&P incorrectly recorded accounts receivable that represented refunds for overpayments of income taxes in Account 165, Prepayments, instead of in Account 143, Other Accounts Receivable. The incorrect accounting led to an overstatement of CL&P's rate base used in its transmission formula rate calculations. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

4. *Merger Transaction Costs* – CL&P improperly included merger transaction costs in operating accounts, contrary to the Commission's long-standing policy that such expenses be recorded in nonoperating accounts. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

5. *Application of Nonapproved Depreciation Rates* – CL&P used a depreciation rate for accounting and transmission ratemaking purposes that was not filed with, and approved by, the Commission. As a result, the Commission was not afforded an opportunity to review or decide on the appropriateness of the inclusion of the depreciation rate in the transmission service rate determination.

D. Other Matter

1. *Transparency of the Derivation of Service Company Capital Costs in Jurisdictional Rates* – CL&P included capital cost charges from its service company, Eversource Energy Service Company (EESCO), in jurisdictional rate determinations. CL&P is encouraged to disclose the EESCO cost components and attributes that are considered in the derivation of the capital cost charges and included in CL&P's transmission rates in its future transmission formula rate annual informational updates and true-up filings. Such disclosure will ensure the filings include information useful in determining how service company capital

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costs are derived that are included in CL&P's jurisdictional rates and recovered from its transmission customers.

E. List of Recommendations

Audit staff's recommendations to remedy the compliance findings are listed below. Details are in Section IV. Audit staff recommends that CL&P:

Allowance for Funds Used During Construction

1. Revise and implement procedures to ensure that AFUDC rate calculations are consistent with Commission accounting requirements.

2. Provide training to relevant staff on the revised AFUDC rate calculation procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

3. Recalculate AFUDC for capital work orders, in a manner consistent with Electric Plant Instruction (EPI) No. 3(A)(17) that corrects the improper inclusion of accumulated other comprehensive income and unamortized debt-related balances in AFUDC rate calculations during the audit period.

4. Submit proposed accounting entries and supporting documentation to DAA that reflect the correction of the Construction Work In Progress-Electric (CWIP), electric plant in service, accumulated depreciation, Accumulated Deferred Income Taxes (ADIT), and other accounts impacted by over-accrual of AFUDC within 60 days of issuance of the audit report.

5. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) calculation of refunds resulting from correction of excess AFUDC in plant included in transmission formula rate annual transmission revenue requirement determinations during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

6. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

7. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

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Accounting for Compromise Settlements

8. Revise existing or establish new policies, procedures, and controls to account for and track legal settlements and associated expenses relating to compromise settlements consistent with Commission accounting requirements.

9. Provide training to relevant staff on the methods to account for expenses relating to such compromise settlements. Also, develop a training program that supports the provision of periodic training in this area, as needed.

10. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) calculation of refunds resulting from the exclusion of compromise settlement amounts from transmission formula rate calculations during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

11. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

12. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

Accounting for Tax Receivables

13. Revise accounting policies and procedures to account for income tax refunds consistent with Commission accounting requirements.

14. Provide training to relevant staff on the revised accounting policies and procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

15. Submit proposed accounting entries and supporting documentation to DAA that reflect the correction of the accounts receivable and prepayment balances within 60 days of issuance of the audit report.

16. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) the calculation of refunds that results from excluding income tax account receivable balances from transmission rates during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

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17. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

18. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

Merger Transaction Costs

19. Enhance accounting policies and procedures for tracking and accounting for merger-related costs consistent with Commission accounting requirements.

20. Provide training to relevant staff on the revised accounting policies and procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

21. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) calculation of refunds resulting from correcting the improper inclusion of merger transaction costs in transmission formula rates during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

22. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

23. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

Application of Nonapproved Depreciation Rates

24. Revise and implement processes and procedures to ensure that depreciation rates and related studies are filed with the Commission for consideration and decision before being used for transmission ratemaking purposes.

25. Provide training to relevant staff on the revised procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

26. File a depreciation study and associated depreciation rate for the Norwalk Harbor-Northport underground transmission line in a docket relating to its transmission formula rate within 60 days of issuance of the audit report.

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F. Compliance and Implementation of Recommendations

Audit staff further recommends that CL&P submit the following:

- A plan for implementing the audit recommendations within 30 days after the audit report is issued;

- Quarterly reports describing progress in completing each corrective action recommended in the audit report. Quarterly nonpublic submissions should be made no later than 30 days after the end of each calendar quarter, beginning with the first quarter after the audit report is issued, and continuing until all recommended corrective actions are completed; and

- Copies of written policies and procedures developed in response to the recommendations. These documents should be submitted in the first quarterly filing after CL&P completes a written policy or procedure.

II. Background

A. Eversource

Eversource, the parent company of CL&P, is headquartered in Boston, Massachusetts and Hartford, Connecticut. Eversource is a public utility holding company primarily engaged in the energy delivery business through its wholly-owned regulated electric utility subsidiaries – CL&P, NSTAR Electric Company, Public Service Company of New Hampshire, and Western Massachusetts Electric Company.[2] Eversource also owns the following natural gas and water utilities: Yankee Gas Services Company, NSTAR Gas Company, and Aquarion Water Company.[3]

Eversource was created in 2012 pursuant to a stock-for-stock merger of Northeast Utilities (NU) and NSTAR wherein NSTAR became a wholly-owned subsidiary of NU.[4] The Commission authorized the merger on July 6, 2011.[5] As a result of the merger, Eversource became New England's largest energy delivery company. The company operates more than 4,270 circuit miles of transmission lines, 72,000 pole miles of distribution lines, 578 substations, 449,737 distribution transformers, and 11,821 miles of natural gas distribution pipelines across its service territory.

Eversource's wholly owned centralized service company is EESCO. EESCO provides accounting, administrative, engineering, financial, information technology, legal, operational, planning, purchasing, and other services to Eversource and its subsidiaries, including CL&P. EESCO charges Eversource and its subsidiaries individually for services provided. During the audit period, Eversource and its subsidiaries were invoiced by EESCO for the cost of services provided through direct

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[2] Western Massachusetts Electric Company merged with and into NSTAR Electric Company, with NSTAR Electric Company as the surviving entity, in a transaction approved by the Commission in Docket No. EC17-62-000. *See NSTAR Electric* Co., 158 FERC ¶ 62,155 (2017) (delegated order).

[3] Eversource also owns Eversource Gas Company of Massachusetts, an entity formed to own all of the assets acquired from Bay State Gas Company d/b/a Columbia Gas of Massachusetts on October 9, 2020. *See NiSource Inc*., 172 FERC ¶ 61,067 (2020).

[4] Eversource's name was changed from NU pursuant to an amendment of its Declaration of Trust filed with the Secretary of the Commonwealth of Massachusetts on April 30, 2015.

[5] *NSTAR*, 136 FERC ¶ 61,016 (2011).

charges when EESCO determined that the service provided benefited a particular company; alternatively, they were invoiced by EESCO through an allocation method when EESCO determined that a service benefited multiple companies. EESCO's allocation methodologies are filed with the Commission in the FERC Form No. 60, Annual Report of Centralized Service Companies. In 2019, EESCO provided services amounting to almost $944 million to Eversource and its subsidiaries. Of the total, approximately $418 million were directly charged to one or more specific affiliates, and $526 million were allocated to affiliates indirectly, i.e., via an allocation method.

B. Transmission Formula Rate

CL&P is a Participating Transmission Owner in ISO-NE. During the audit period, CL&P's transmission service rates were calculated based on a formula rate for Regional Network Service (RNS) and a formula rate for Local Network Service (LNS).[6] Costs recovered using the RNS formula were associated with Pooled Transmission Facilities (PTF), which were facilities greater than 69 kV that met certain conditions and that were connected to other entities' transmission lines or transmission systems and operated by and under ISO-NE authority. Costs recovered under the LNS formula were largely associated with non-Pooled Transmission Facilities (non-PTF), which were facilities connected to CL&P's system that were primarily radial transmission lines. CL&P operated and offered transmission service over non-PTF, and ISO-NE exercised limited operating authority over the non-PTF.

CL&P calculated its PTF annual transmission revenue requirement, for use in developing RNS billing charges, pursuant to Attachment F of the ISO-NE OATT. Attachment F provides for the allocation of costs to the transmission function using a transmission wages and salaries allocation factor, plant allocation factor, PTF transmission plant allocation factor, and the direct assignment of costs using actual, functional data that is specifically identified and reported in the FERC Form No. 1. The transmission wages and salaries allocation factor allocates general plant cost based on labor dollars. It is the ratio of transmission-related direct wages and salaries to total direct wages and salaries. The plant allocation factor is the ratio of CL&P's total investment in transmission plant and transmission-related general plant to total plant in service. The PTF transmission allocation factor is the ratio of PTF transmission plant to total investment in transmission plant.

During the audit period, CL&P did not use the wages and salaries allocation factor to allocate its general plant costs. Instead, CL&P used data reported in its FERC Form

[6] *See* ISO-New England Inc. Transmission, Markets, and Services Tariff, Section II.H Other Transmission Provisions, Schedule 9 Regional Network Service 3.0.0. and Schedule 21 Local Service 1.0.0, respectively.

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No. 1 as the basis for allocation of transmission-related general plant costs. CL&P identified actual costs by utility function in footnotes of its FERC Form No. 1. In addition, CL&P used balances for transmission rate base and expenses as reported in its FERC Form No. 1 in lieu of the plant allocation factor provided in the formula rate.

CL&P's local transmission service consisted primarily of services offered through ISO-NE's Schedule 21-ES.[7] Through this schedule, CL&P recovered its annual revenue requirement for, among other items, LNS and local point-to-point transmission services. Under Schedule 21-ES, CL&P recovered costs not otherwise recovered through RNS rates. CL&P calculated the associated annual transmission revenue requirement for LNS and local point-to-point service under Attachment ES-H of Schedule 21-ES.[8]

[7] ISO-New England Inc. Transmission, Markets, and Services Tariff, Section II.28 Local Service 1.0.0, Schedule 21 Local Service 1.0.0, Schedule 21-ES 20.0.0.

[8] *Id.*

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III. Introduction

A. Objectives

The audit evaluated CL&P's compliance with: (1) approved terms, rates, and conditions of its transmission formula rate mechanism as provided in the ISO-NE Transmission, Markets, and Services Tariff on file with the Commission; (2) accounting requirements of the Uniform System of Accounts Prescribed for Public Utilities and Licensees under 18 C.F.R. Part 101; (3) reporting requirements of the FERC Form No. 1, Annual Report of Major Electric Utilities, Licensees and Others, under 18 C.F.R. § 141.1; and (4) the requirements in Preservation of Records of Public Utilities and Licensees under 18 C.F.R. Part 125. The audit covered the period January 1, 2015 to December 31, 2019.

B. Scope and Methodology

Audit staff performed the following specific actions to facilitate the audit and the testing and evaluation of CL&P's compliance with requirements relevant to the audit objectives:

Audit Planning, Processes, and Administration

To address overall audit objectives, audit staff:

- *Review of Public Information* – Conducted an extensive review of public information before commencing the audit. This review entailed a detailed examination of CL&P's corporate structure, the services it provided, major events affecting operations and finances, mergers, significant contracts, prior audit issues, and other key regulatory and business activities. Examples of materials reviewed include Eversource's annual reports and SEC Form 10-K filings, CL&P's FERC Form No. 1, and EESCO's FERC Form No. 60 submissions, prior relevant FERC audit reports, corporate web sites, and other relevant regulatory and media sources.

- *Collaboration with Commission Staff* – Conferred with Commission staff in other offices to ensure audit report findings were consistent with Commission precedent and policy.

- *Identification of Regulatory Standards and Audit Criteria* – Identified regulatory requirements and criteria to use in evaluating CL&P's compliance with Commission accounting and reporting requirements in 18 C.F.R. Parts

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101 and 141, and other Commission rules, regulations, and letter orders generally applicable to jurisdictional service companies and public utilities.

- *Issuance of Data Requests* – Issued data requests to collect information not commonly available to the public. This information related to internal policies, procedures and controls, business practices, risk management, corporate structure, contractual agreements, financial accounting and reporting activity, corporate compliance, regulatory filings, and other pertinent information. This information was used to test and evaluate compliance with Commission requirements relevant to the audit objectives.

- *Interviews and Meetings* – Held teleconferences with CL&P staff to discuss audit objectives, scope, processes, procedures and operations, testing, data request responses, technical and administrative matters, and compliance concerns.

- *External Auditor Work Papers Review* – Audit staff reviewed CL&P's external auditors' work papers prepared as part of CL&P's annual audits for 2016 to 2018 to determine the level of their audit coverage in areas to be reviewed by audit staff.

- *Site Visit to CL&P Headquarters* – Conducted one site visit to CL&P's headquarters in Berlin, CT to discuss, observe, and evaluate procedures, practices, and controls intended to ensure compliance with Commission regulations. The visit enabled audit staff to:

    - Discuss CL&P's corporate structure, departmental functions, and employee responsibilities, and meet with key company officials;

    - Learn about CL&P's transmission system and operations, in particular, the assets, departments, activities, functions, systems, and processes used in its operations;

    - Interview executives, managers, and staff responsible for accounting, financial reporting, transmission operations, and corporate compliance;

    - Review Board of Directors and Audit Committee meeting minutes and internal and external audit reports;

    - Discuss management and operation of CL&P's corporate compliance program;

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- Discuss and observe internal accounting and reporting procedures, processes, and controls relevant to the audit's scope; and

- Discuss CL&P's preservation of records policies, procedures, and practices.

Compliance with Transmission Formula Rate

Audit staff performed these actions to evaluate CL&P's compliance with the requirements of its transmission formula rate:

- *Transmission Tariff* – Reviewed CL&P's transmission formula rate template included in Attachment F of the ISO-NE OATT. Reviewed CL&P's rate filings with the Commission and reviewed the components comprising rate base, revenue requirements, return calculations, adjustments, supporting calculations, and allocators. Verified that FERC Form No. 1 references were accurate.

- *Formula Rate Procedures* – Evaluated CL&P's processes, procedures, and controls used for preparing and reviewing its annual transmission revenue requirement filings and their supporting work papers.

- *Interviewed Employees* – Interviewed CL&P employees responsible for providing data inputs into the transmission formula rate and calculating the annual transmission revenue requirement. Assessed the level of oversight and controls employed by CL&P to ensure complete and accurate transmission formula rate inputs.

- *Formula Rate Input Reconciliation* – Reconciled the transmission formula rate inputs to figures reported in CL&P's FERC Form No. 1 reports for 2015 through 2018. Evaluated the adequacy of disclosures provided by CL&P for formula rate inputs not derived from its FERC Form No. 1 reports.

- *Mathematical Accuracy* – Evaluated the mathematical accuracy of computations performed by CL&P in applying its transmission formula rate to test whether inputs and computations were accurate. For example, audit staff reviewed supporting documentation for the depreciation rate used to test whether amounts were correctly populated into the transmission formula rate template.

- *Formula and Input Analysis* – Reconciled the components of the approved formula rate to the corresponding calculations in the annual transmission

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revenue requirement filings. Analyzed and assessed CL&P's compliance with the Commission's required accounting treatment of select formula rate inputs. Reviewed CL&P's calculation and application of the allocation factors used in the transmission formula rate to test whether the correct amounts were used in these calculations.

Compliance with Accounting Regulations

- *Accounting Processes and Procedures* – Evaluated CL&P's accounting processes, procedures, and internal controls used to comply with Commission accounting regulations under 18 C.F.R Part 101. Held discussions with and interviewed CL&P employees regarding accounting practices, adherence to CL&P accounting policies and procedures, system processes used for FERC accounting, and internal controls intended to achieve compliance with FERC accounting requirements.

- *Accounting Systems* – Reviewed CL&P's accounting systems used to capture, manage, and retain financial information, including CL&P's general ledger, work order systems, expenses and billing systems, and other key processes. Examined the systems' ability to capture transactions consistently to ensure information reported in financial statements and other reports was accurate and complete.

- *Significant Accounting Matters* – Tested select balance sheet and income statement accounts to test whether the nature of the costs recorded in those accounts complied with the USofA under 18 C.F.R. Part 101. Audit staff performed select testing of these accounting matters:

    - *Transmission versus Distribution* – Reviewed certain transmission operating and maintenance accounts to test whether costs related to transmission or, alternatively, distribution were appropriately recorded in the correct functional expense accounts;

    - *A&G Expenses* – Tested select A&G expense accounts to determine whether CL&P recorded salaries, office supplies, outside services (e.g., consultant fees), pensions, and employee benefits, etc., consistent with the accounts' instructions;

    - *Non-operating Expenses* – Examined summaries for non-operating expense accounts to test whether CL&P appropriately recorded non-operating expenses, such as political and charitable contributions, in these accounts. Examined the accounting for expenses for employment practices that judicial or administrative decrees found to be discriminatory

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or that were the subject of settlements to verify that CL&P had recorded these expenses in the proper non-operating expense account consistent with Commission policy;

- *Cost Allocations* – Examined the support for, and tested the application of, corporate and associated company allocation methodologies for allocating and recording shared service costs among affiliates, and billing and accounting for non-power goods and services provided among associated companies. For example, audit staff reviewed allocation ratios and tested selected costs to test whether CL&P was allocated, and had correctly accounted for, the costs of shared services. Audit staff also reviewed affiliate billing procedures and select invoices to test whether CL&P recorded the proper amounts in accordance with those affiliate billing procedures;

- *Accumulated Deferred Income Taxes* – Reviewed a monthly summary of deferred taxes that flowed into the rate base component of the transmission formula rate. Analyzed supporting documentation to evaluate how CL&P calculated the deferred tax component and underlying accounting entries made to FERC deferred income tax accounts (i.e., Accounts 190, 282, and 283);

- *Income Taxes and Tax Allocation Agreements* – Evaluated CL&P's consolidated income tax allocation agreement and the tax payment structure between CL&P and the consolidated group, including the methodology used to allocate the tax benefits/burden to members of the consolidated group. Reviewed supporting documentation to validate the calculation of tax accruals and deferred income taxes;

- *Depreciation* – Reviewed CL&P's monthly depreciation and amortization expense and supporting calculations to determine whether CL&P used the proper accounts and recorded the correct amounts. Reviewed CL&P's depreciation expense calculation to test whether it derived monthly depreciation expenses using approved depreciation rates on file with the Commission;

- *Contingent Liabilities* – Reviewed the Notes to the Financial Statements in CL&P's FERC Form No. 1 filings and identified information about accruals for potential future obligations. Analyzed information on commitments and environmental and legal contingencies, and assessed whether these amounts affected the transmission formula rate's resulting annual transmission revenue requirement and billing rates; and

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- *AFUDC* – Reviewed CL&P's AFUDC rate calculation for consistency with EPI No. 3 and other Commission AFUDC guidance. Reviewed CL&P's methodology for determining the annual AFUDC rate to test whether it was based upon CL&P's own debt and equity book balances and to ensure that the short-term debt rate variance did not exceed 25 basis points. Reviewed work orders to test whether CL&P ceased accruing AFUDC during the following instances: (1) when an asset was placed in-service, (2) during periods of suspension of construction, and (3) when plant was abandoned. Examined the components of CL&P's CWIP balances to determine whether they only included amounts related to construction activities and properly allocated overheads.

Compliance with FERC Form No. 1 Reporting and Recordkeeping Requirements

Audit staff performed these actions to evaluate CL&P's compliance with Commission reporting requirements under 18 C.F.R. Part 141 and record preservation requirements under 18 C.F.R. Part 125:

- *Reporting Processes and Procedures* – Evaluated CL&P's financial reporting processes, procedures, and quality controls used to prepare its FERC Form No. 1 filings.

- *Financial Reporting Instructions* – Evaluated CL&P's financial reporting to determine whether it complied with the account and page instructions of FERC Form No. 1 reports for 2015 through 2019.

- *Financial Statement Account Balances* – Tied the account balances reported in CL&P's FERC Form No. 1 filings to its books and records (i.e., its general ledger). To facilitate the review, audit staff reviewed selected transactions to confirm the balances.

- *Variance Analysis* – Performed variance analyses for accounts reported in the FERC Form No. 1 by investigating accounts with large balances, unusual activity, and/or significant year-to-year fluctuations. Followed up with CL&P on each account fluctuation to understand the nature of the fluctuation, and where necessary, obtained additional information and support deemed necessary.

- *Notes to Financial Statements* – Reviewed the Notes to Financial Statements beginning on page 123.1 of the FERC Form No. 1 for significant accounting matters and followed up with CL&P on these matters to understand financial statements and transmission formula rate implications, if any.

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- *Preservation of Records* – Reviewed the retention schedules that were included in CL&P's record retention program. Interviewed employees responsible for record retention to understand processes, procedures, and controls for administration and maintenance of records. Sampled selected records to ascertain whether their retention period aligned with Commission preservation of records regulations, and whether any records prematurely destroyed or lost were reported to the Commission.

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IV. Findings and Recommendations

1. Allowance for Funds Used During Construction

CL&P improperly included accumulated other comprehensive income and unamortized debt-related balances in long-term debt and equity balances used to compute its AFUDC rates. As a result, CL&P over-accrued AFUDC amounts included in utility plant accounts, which led it to overstate its annual transmission revenue requirement and overbill transmission customers.

Pertinent Guidance

- Order No. 561 states in relevant part:

  > The balances of long-term debt, preferred stock, and common equity for use in the formula for the current year will be the balances in such accounts at the end of the prior year….[9]

- 18 C.F.R. Part 101, EPI No. 3(A)(17), Allowance for Funds Used during Construction, states in part:

  > The rates shall be determined annually. The balances for long-term debt, preferred stock and common equity shall be the actual book balances as of the end of the prior year.

- *Portland Natural Gas Transmission System*, 142 FERC ¶ 61,197, at P 263 (2013), *reh'g denied,* 150 FERC ¶ 61,107 (2015) (quoting *System Energy Resources, Inc.*, 96 FERC ¶ 61,165, at 61,740 (2001)), states in relevant part:

  > It is the gross proceeds of a company's long-term debt, *i.e.*, the total principal outstanding, that belong in the capital structure because this reflects the company's total obligation with respect to long-term debt.

[9] *See Amendments to Uniform System of Accounts for Public Utilities and Licensees and for Natural Gas Companies (Classes A, B, C and D) To Provide for the Determination of Rate for Computing the Allowance for Funds Used During Construction and Revisions of Certain Schedule Pages of FPC Reports*, Order No. 561, 57 FPC 608, at 610 (Order No. 561), *reh'g denied*, Order No. 561-A, 59 FPC 1340 (1977) (Order No. 561-A), *order on clarification*, 2 FERC ¶ 61,050 (1978).

REDACTED

- The Commission order that established Account 219, Accumulated Other Comprehensive Income, *Accounting and Reporting of Financial Instruments, Comprehensive Income, Derivatives and Hedging Activities*, Order No. 627, 101 FERC ¶ 61,032, at PP 70-71 (2002) (footnote omitted), states:

> 70. One commenter recommended that the Commission state it will not incorporate derivative instruments, hedging activities, and other comprehensive income into its ratemaking process for utilities, because the value of these instruments are certain to change over time and the Commission would set rates incorrectly.
>
> 71. As stated in the NOPR, the proposed rule was not intended to prescribe the ratemaking treatment for items of other comprehensive income or for derivative instruments and hedging activities. The adoption of any particular rate treatment for these amounts is beyond the scope of this rulemaking. The Commission will decide the appropriate treatment, for these transactions on a case-by-case basis in individual rate proceedings.

Background

AFUDC represents the financing cost of construction and consists of two components: Allowance for Borrowed Funds (debt) and an Allowance for Other Funds (equity) used for construction. The Commission's predecessor agency, the Federal Power Commission, in Order No. 561, established the current formula for capturing these components of AFUDC.[10] EPI No. 3(A)(17) provides the uniform formula for calculating a utility's maximum AFUDC rate. Audit staff reviewed CL&P's AFUDC rate calculations and the inputs that were factored into the debt and equity components during the audit period, as well as CL&P's application of its AFUDC rate to CWIP balances. This process included interviewing CL&P's plant accounting staff and testing a sample of construction work orders, invoices, and other support documents pertaining to capital projects.

Audit staff found that CL&P included balances recorded in Accounts 181, Unamortized Debt Expenses; 189, Unamortized Loss of Reacquired Debt; 225, Unamortized Premium on Long-Term Debt; 226, Unamortized Discount on Long-Term Debt; and 257, Unamortized Gain on Reacquired Debt, as part of long-term debt for purposes of computing its AFUDC rates, thus effectively including its *net* long-term debt balances in the AFUDC rate calculations. However, in accordance with Commission precedent, CL&P was required to use the *gross* proceeds of long-term debt in the

[10] *See id.*

REDACTED

AFUDC rate calculation, i.e., the *total* principal outstanding, as the long-term debt balance.[11] CL&P should have excluded amounts from the unamortized debt-related accounts from the long-term debt balance used to calculate its AFUDC rate.

Additionally, CL&P improperly included Account 219, Accumulated Other Comprehensive Income, in the equity component when computing its AFUDC rate. AFUDC includes the cost of borrowed funds used during construction and an allowed rate on equity capital used for construction. The amounts in Account 219 represent unrealized gains and losses. Since the amounts in the account were unrealized, the balances recorded therein were not available to CL&P to finance construction, or any other activity. Consequently, those amounts should not have been considered as funds available for construction in deriving the AFUDC rates. Further, the creation of Account 219 was for accounting purposes; no general use of Account 219 for ratemaking purposes has been prescribed by the Commission.[12]

As a result of these errors, CL&P over-accrued AFUDC that was capitalized as a component of the cost of CWIP and subsequently included in Accounts 106, Completed Construction Not Classified – Electric (Major Only), or 101, Electric Plant in Service (Major Only). In addition, CL&P overbilled transmission customers for the excessive AFUDC costs included in utility plant and factored into CL&P's annual transmission revenue requirement determinations during the audit period.

Recommendations

DAA recommends that CL&P:

1. Revise and implement procedures to ensure that AFUDC rate calculations are consistent with Commission accounting requirements.

2. Provide training to relevant staff on the revised AFUDC rate calculation procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

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[11] *Portland Natural Gas*, 142 FERC ¶ 61,197 at P 263 ("It is the gross proceeds of a company's long-term debt, *i.e.*, the total principal outstanding, that belong in the capital structure …").

[12] Order No. 627, 101 FERC ¶ 61,032 at PP 70-71 (Account 219 created for accounting, not ratemaking, purposes, and "[t]he Commission will decide the appropriate treatment" for ratemaking purposes "on a case-by-case basis in individual rate proceedings").

REDACTED

3. Recalculate AFUDC for capital work orders, in a manner consistent with EPI No. 3(A)(17) that corrects the improper inclusion of accumulated other comprehensive income and unamortized debt-related balances in AFUDC rate calculations during the audit period.

4. Submit proposed accounting entries and supporting documentation to DAA that reflect the correction of the CWIP, electric plant in service, accumulated depreciation, ADIT, and other accounts impacted by over-accrual of AFUDC within 60 days of issuance of the audit report.

5. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) calculation of refunds resulting from correction of excess AFUDC in plant included in transmission formula rate annual transmission revenue requirement determinations during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

6. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

7. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

REDACTED

2. Accounting for Compromise Settlements

CL&P incorrectly accounted for compromise settlement costs in operating expense accounts instead of Account 426.3, Penalties, or Account 426.5, Other Deductions, as required. The operating expense accounts used were included in CL&P's transmission formula rate calculations. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

Pertinent Guidance

- Accounting Release (AR) No. 12,[13] Discriminatory Employment Practices, discusses expenses "resulting from employment practices that were found to be discriminatory by a judicial or administrative decree or that were the result of a compromise settlement or consent decree" and states in relevant part:

> The Uniform System of Accounts provides that all charges to utility operating expense accounts must be just and reasonable. Expenditures of the nature mentioned above [i.e., relating to employment practices found to be discriminatory or that were the result of a compromise settlement consent decree] that can be readily identified and quantified should not be considered as just and reasonable charges to utility operations and should be classified to the appropriate nonoperating expense accounts.[14]

[13] Accounting releases are informal interpretations of the USofA to be followed in the absence of specific reference to prescribed accounting regulations and other Commission decisions. These interpretations express the views of the Chief Accountant as to the correct application of the provision of the USofA that the Commission has prescribed. As provided for in General Instruction No. 5 in the USofA, these interpretations do not preclude any company from submitting questions of doubtful interpretations to the Commission on matters dealt with in accounting releases.

[14] Accounting Release AR-12, Discriminatory Employment Practices (Feb. 1, 1980), *available at* www.ferc.gov/discriminatory-employment-practices (Accounting Release AR-12).

REDACTED

- 18 C.F.R. Part 101, Account 426.3, Penalties, states:

  This account shall include payments by the company for penalties or fines for violation of any regulatory statutes by the company or its officials.

- 18 C.F.R. Part 101, Account 426.5, Other Deductions, states in part:

  This account shall include other miscellaneous expenses which are nonoperating in nature, but which are properly deductible before determining total income before interest charges.

Background

Audit staff analyzed CL&P's accounting for expenditures resulting from employment practices that were found to be discriminatory by a judicial or administrative decree, or that were the result of a compromise settlement or consent decree. Audit staff found that from 2015 to 2018, CL&P directly made $343,000 of compromise settlement payments to resolve employee discrimination claims. The company recorded the payments in Accounts 184, Clearing Accounts; 586, Meter Expenses; and 923, Outside Services Employed. The amounts recorded in Account 184 were subsequently cleared to various balance sheet and income statement accounts, some of which were inputs to the transmission formula rate, as well as Accounts 586 and 923.

Additionally, audit staff discovered that EESCO incurred about $902,000 of compromise settlement costs to resolve employee discrimination claims that it recorded in Accounts 903, Customer Records and Collection Expenses; 920, Administrative and General Salaries; 925, Injuries and Damages; and Account 923. Pursuant to its allocation processes and practices, EESCO allocated about $410,000 of these compromise settlement expenses to CL&P. CL&P recorded the allocated costs using the same accounting that EESCO used to originally record the costs.

CL&P's accounting for the compromise settlement expenditures was not consistent with Commission accounting requirements. In accordance with the requirements of AR No. 12, expenses incurred resulting from employment practices found to be discriminatory by a judicial or administrative decree or that were the result of a compromise settlement or consent decree must be accounted for as nonoperating expenses in Account 426.3, Penalties, or Account 426.5, Other Deductions, as appropriate. CL&P's improper accounting led to the inclusion of the cost in its transmission formula rate calculations. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

REDACTED

Recommendations

DAA recommends that CL&P:

8. Revise existing or establish new policies, procedures, and controls to account for and track legal settlements and associated expenses relating to compromise settlements consistent with Commission accounting requirements.

9. Provide training to relevant staff on the methods to account for expenses relating to such compromise settlements. Also, develop a training program that supports the provision of periodic training in this area, as needed.

10. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) calculation of refunds resulting from the exclusion of compromise settlement amounts from transmission formula rate calculations during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

11. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

12. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

3. Accounting for Tax Receivables

CL&P incorrectly recorded accounts receivable that represented refunds for overpayments of income taxes in Account 165, Prepayments, instead of in Account 143, Other Accounts Receivable. The incorrect accounting led to an overstatement of CL&P's rate base used in its transmission formula rate calculations. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

Pertinent Guidance

- 18 C.F.R. Part 101, Account 143, Other Accounts Receivable, states in part:

  > A. This account shall include amounts due the utility upon open accounts, other than amounts due from associated companies and from customers for utility services and merchandising, jobbing and contract work.

- 18 C.F.R. Part 101, Account 165, Prepayments, states:

  > This account shall include amounts representing prepayments of insurance, rents, taxes, interest and miscellaneous items, and shall be kept or supported in such a manner as to disclose the amount of each class of prepayment.

- The Commission affirmed the accounting for income tax refunds in *Midwest Independent Transmission System Operator, Inc.*, wherein the Commission stated:

  > [A] federal income tax refund is an account receivable, not a prepayment, and should be excluded from rate base. The Commission has defined prepayments included in Account 165 as expenses for a service or a supply paid in advance that will be consumed in future periods, such as rent and insurance. Accordingly, we find that Ameren's federal tax refund should not be booked to Account 165 (Prepayments), and instead be booked to Account 143, (Other Accounts Receivable).[15]

Background

CL&P is party to a tax sharing agreement with Eversource, wherein CL&P is obligated to pay, to Eversource, amounts owed for its share of consolidated federal and

[15] *Midwest Independent Transmission System Operator, Inc.*, 148 FERC ¶ 61,206, at P 171 (2014).

REDACTED

state income tax liabilities. Eversource remits the monies received from CL&P to tax authorities for the estimated consolidated tax liability.

Audit staff reviewed consolidated tax returns and various other documents supporting these returns throughout the audit. In addition, audit staff examined CL&P's tax procedures, computations, and related documentation supporting tax accruals, refunds, and prepayment balances recorded in Account 165, as well as tax payments made to Eversource. Audit staff verified that CL&P made quarterly payments to Eversource for its share of estimated federal and state tax liabilities during the audit period. When estimated amounts paid by CL&P exceeded its portion of the actual tax liabilities, it recognized an amount on its books in Account 165 for the overpayment.

From 2015 through 2019, CL&P included federal and state income tax refund amounts in Account 165 as prepaid taxes with end of year balances of approximately $33.2 million, $9.4 million, $23.1 million, $29.9 million, and $33.9 million, respectively. Under some circumstances, where an overpayment of tax is applied to a future tax liability, Account 165 may be appropriately used to reflect the application of these tax overpayments to pay a future liability. However, amounts refunded to CL&P in the succeeding period after each year end should have been recorded in Account 143. As such, these refunds represented receivable amounts appropriately recordable in Account 143, instead of prepayments recordable in Account 165. Per CL&P's formula rate, prepayments recorded in CL&P's Account 165 are included in transmission rate base balances that are used to calculate transmission service rates. Accordingly, the misclassification of the income tax refunds as prepayments rather than as other accounts receivable led CL&P to overstate its annual transmission revenue requirements and overbill transmission customers.

Recommendations

DAA recommends that CL&P:

13. Revise accounting policies and procedures to account for income tax refunds consistent with Commission accounting requirements.

14. Provide training to relevant staff on the revised accounting policies and procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

15. Submit proposed accounting entries and supporting documentation to DAA that reflect the correction of the accounts receivable and prepayment balances within 60 days of issuance of the audit report.

REDACTED

16. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) the calculation of refunds that results from excluding income tax account receivable balances from transmission rates during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

17. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

18. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

4. Merger Transaction Costs

CL&P improperly included merger transaction costs in operating accounts, contrary to the Commission's long-standing policy that such expenses be recorded in nonoperating accounts. As a result, CL&P overstated its annual transmission revenue requirement and overbilled transmission customers.

Pertinent Guidance

- The Commission's long-standing precedent stipulates that transaction costs incurred by public utilities associated with a merger are nonoperating in nature and should be charged to Account 426.5, Other Deductions, to the extent the costs are not retained by the parent holding company. The Commission has stated:

  > It is Commission policy that costs incurred to consummate a merger are non-operational in nature and must be recorded in Account 426.5, Other Deductions. These costs may include, but are not limited to, internal and external third-party labor costs for legal, consulting, and professional services incurred to consummate the merger.[16]

- 18 C.F.R. Part 101, Account 426.5, Other Deductions, states:

  > This account shall include other miscellaneous expenses which are nonoperating in nature, but which are properly deductible before determining total income before interest charges.

[16] *ITC Holdings Corp.*, 143 FERC ¶ 61,256, at P 168 (2013) (footnote omitted), *order dismissing as moot requests for reh'g and clarification*, 151 FERC ¶ 61,266 (2015); *accord Exelon Corp.*, 138 FERC ¶ 61,167, at P 133 (2012) ("we have required [merging] entities to record the transaction costs in Account 426.5"); *BHE Holdings Inc.*, 133 FERC ¶ 61,231, at P 51 (2010) ("Costs incurred to effectuate a merger are not considered an operating activity under the Commission's accounting regulations and therefore should not be recorded in Account No. 923 as proposed by the Applicants. The Commission has required companies to record merger-related transaction costs in Account No. 426.5, Other Deductions. Account No. 426.5 includes miscellaneous expense items which are non-operating in nature") (footnotes omitted); *Midwest Power Sys., Inc. and Iowa Illinois Gas and Elec. Co.*, 71 FERC ¶ 61,386, at 62,509 (1995) ("[w]e will, therefore, direct Applicants to record the transaction costs associated with the merger in Account 426.5").

Background

On December 4, 2017, Eversource consummated a merger transaction involving the acquisition of Aquarion Water Company from Macquarie Infrastructure Partners and British Columbia Investment Management Corporation. The transaction did not require Commission approval prior to consummation. Rather, the transaction was approved by three jurisdictional state regulators – the Connecticut Public Utilities Regulatory Authority, the Massachusetts Department of Public Utilities, and the Maine Public Utilities Commission – and was subject to U.S. Department of Justice review.

Eversource's merger costs were comprised of transaction and transition costs, which included, among other things, internal labor costs and employee expenses. To track the merger costs it incurred, Eversource established special accounting processes and procedures, and distributed time reporting instructions to EESCO employees who were assigned to work on the merger project. Pursuant to the instructions, EESCO employees' labor costs and external expenses were required to be charged to a special merger project work order. Costs charged to the work order were supposed to be restricted from allocation to the Eversource public utilities. However, during discussions with company personnel, audit staff was informed that several EESCO employees who performed work on the merger did not charge time associated with the merger duties they performed to the special work order. Audit staff analyzed EESCO documentation on employees that improperly charged their time. Audit staff found that the portion of these employees' time and associated labor cost that involved performance of merger-related activities was excluded from the special merger project work order; and as a result the associated labor cost was allocated to the public utilities.

According to Eversource's time reporting policy, employees were generally not required to directly charge internal labor hours to a specific work order or project, unless they spent at least 4 hours a week on the project. For time spent less than 4 hours a week, when employees did not identify duties performed as being provided for a particular project, predetermined default allocators in the timekeeping system allocated labor cost associated with hours worked to Eversource subsidiaries. Eversource explained that some employees did not work more than 4 hours per week on the merger project, and as such did not directly charge their labor hours to the project. Consequently, the portion of these employees' labor cost associated with duties performed for the merger were charged to CL&P and other Eversource subsidiaries.

EESCO estimated that approximately $209,000 of labor costs were erroneously allocated to Eversource subsidiaries, which included $73,000 charged to CL&P. CL&P recorded the costs in operating expense accounts that included balances used to populate its transmission formula rate. However, the Commission has long held that costs incurred to consummate a merger are non-operational in nature and must be recorded in

Account 426.5, Other Deductions. As a result, CL&P overstated its annual transmission revenue requirement and overbilled its transmission customers.

Recommendations

DAA recommends that CL&P:

19. Enhance accounting policies and procedures for tracking and accounting for merger-related costs consistent with Commission accounting requirements.

20. Provide training to relevant staff on the revised accounting policies and procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

21. Submit a refund analysis, within 60 days of issuance of the audit report, to DAA for review that explains and details the following: (1) calculation of refunds resulting from correcting the improper inclusion of merger transaction costs in transmission formula rates during the audit period, plus interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) refunds will be made.

22. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

23. Refund the amounts disclosed in the refund report to customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

REDACTED

5. Application of Nonapproved Depreciation Rates

CL&P used a depreciation rate for accounting and transmission ratemaking purposes that was not filed with, and approved by, the Commission. As a result, the Commission was not afforded an opportunity to review or decide on the appropriateness of the inclusion of the depreciation rate in the transmission service rate determination.

Pertinent Guidance

- 18 C.F.R. § 35.13(a) states in part:

> *General rule*. Every public utility shall file the information required by this section, as applicable, at the time it files with the Commission under § 35.1 all or part of a rate schedule, tariff or service agreement to supersede or otherwise change the provisions of a rate schedule, tariff or service agreement filed with the Commission under § 35.1. Any petition filed under § 385.207 of this chapter for waiver of any provision of this section shall specifically identify the requirement that the applicant wishes the Commission to waive.

- 18 C.F.R. § 35.13(h)(10) states in part:

> *Statement AJ – Depreciation and amortization expenses*. Statement AJ consists of statements of depreciation and amortization expenses for Period I and Period II.
>
> . . . . .
>
> (iv) For Period I and Period II, the utility shall show the annual depreciation rate applicable to each function and subfunction for which depreciation expense is reported. The utility shall indicate the bases upon which the depreciation rates were established. If the depreciation rates used for Period I or Period II data differ from those employed to support the utility's prior approved jurisdictional electric rate, the utility shall include in or append to Statement AJ detailed studies in support of such changes. These detailed studies shall include:
>
> (A) Copies of any reports or analyses prepared by any independent consultant or utility personnel to support the proposed depreciation rates; and

> (B) A detailed capital recovery study showing by primary account the depreciation base, accumulated provision for depreciation, cost of removal, net salvage, estimated service life, attained age of survivors, accrual rate, and annual depreciation expense.

- Order No. 618; *Depreciation Accounting*, at footnote 25, states in relevant part:

> To change prices charged for power sales or transmission services (whether determined by stated rates or formula rates) to reflect a change in depreciation, a utility would first have to make a filing with us, pursuant to sections 205 or 206, 16 U.S.C. 824d, 824e, as appropriate, to that effect.[17]

Background

Audit staff evaluated CL&P's depreciation processes and procedures to determine whether they complied with the Commission's accounting and rate regulations. Audit staff found that CL&P applied a depreciation rate to utility plant that was not the rate on file with, and approved by, the Commission. Specifically, CL&P applied depreciation rates ranging from 3.17% to 3.26% to the cost of its Norwalk Harbor-Northport underground transmission line recorded in Account 358, Underground Conductors and Devices. The approved rate on file with the Commission for the transmission line's balances recorded in the account was zero (0%).

The zero depreciation rate for the Norwalk Harbor-Northport underground transmission line was filed with the Commission in Docket No. ER03-1247-000 and, was part of an uncontested offer of settlement among the stakeholders, which was ultimately approved by the Commission on September 16, 2004.[18] During the audit, CL&P acknowledged that the depreciation rate used was not filed with the Commission, as required, and explained that the assets used to develop the zero depreciation rate were fully depreciated by 2004 when the associated depreciation study was filed with the Commission. CL&P stated that, in 2008, new assets were added to the Norwalk Harbor-

[17] *Depreciation Accounting*, Order No. 618, 92 FERC ¶ 61,078, FERC Stats. & Regs. ¶ 31,104, at 31,695 n. 25 (2000).

[18] *See Northeast Utilities Service Co*., Open Access Transmission Service Filing, Docket No. ER03-1247-000 (Aug. 26, 2003), *order on settlement*, 108 FERC ¶ 61,240 (2004), *clarification granted*, 111 FERC ¶ 61,333, at P 6, n.10 (clarifying that issue involving a memorandum of understanding was pending before ALJ).

REDACTED

Northport line that CL&P began to depreciate based on an engineering study that predicted a life expectancy for the installed assets of 40 years.

CL&P's explanation for its use of an engineering study and associated depreciation rates for transmission ratemaking purposes does not justify its departure from Commission precedent as provided in Order No. 618, and 18 C.F.R. §§ 35.1(e) and 35.13(h)(10) of the Commission's regulations. CL&P should have filed its engineering study and associated depreciation rate with the Commission for review and consideration under section 205 of the Federal Power Act prior to using the rate for ratemaking purposes.

Recommendations

DAA recommends that CL&P:

24. Revise and implement processes and procedures to ensure that depreciation rates and related studies are filed with the Commission for consideration and decision before being used for transmission ratemaking purposes.

25. Provide training to relevant staff on the revised procedures. Also, develop a training program that supports the provision of periodic training in this area, as needed.

26. File a depreciation study and associated depreciation rate for the Norwalk Harbor-Northport underground transmission line in a docket relating to its transmission formula rate within 60 days of issuance of the audit report.

REDACTED

V. Other Matter

1. Transparency of the Derivation of Service Company Capital Costs in Jurisdictional Rates

EESCO is a centralized service company within the Eversource holding company system. EESCO provides accounting, administrative, engineering, financial, information technology, legal, operational, planning, purchasing, and other shared services to Eversource and its subsidiaries. EESCO charges the companies for the cost of the services that it provides. The cost that EESCO charges is comprised of its actual incurred operations cost plus an additional amount of compensation. EESCO explained that the additional compensation charge is the cost for use of its capital to provide the services.

In accordance with Commission regulations, franchised public utilities that have captive customers, or that own or provide transmission service over jurisdictional transmission facilities, may only purchase or receive nonpower goods and services from centralized service companies, such as EESCO, at cost.[19] For accounting purposes, the service cost of a centralized service company that is charged to such public utilities is deemed to be appropriate when based on a fair allocation of the total amount of expenses incurred by the service company plus an amount that provides compensation to the service company for the use of its capital.[20] The portion of a service cost that provides compensation for use of a service company's capital should represent recovery, by the service company, of its cost of interest on borrowed funds and a *reasonable* return on

[19] *See* 18 C.F.R. § 35.44 (2021), Protections Against Affiliate Cross-Subsidization; *id*. at § 35.44(b)(3) ("A franchised public utility that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities, may only purchase or receive non-power goods and services from a centralized service company at cost").

[20] *See* 18 C.F.R. § 367.25 (2021), Determination of Service Cost, stating:

> A service must be deemed at cost and fair allocation of costs requires an accurate accounting for the elements that makes [sic] up the aggregate expense of conducting the business of the service company. In the accounts prescribed in this part, the total amounts included in the expense accounts during any period plus the amount that appropriately may be added as compensation for the use of capital constitute cost during that period.

REDACTED

capital investments used for the performance of services or construction work for, or the sale of goods to, associate companies.[21]

Audit staff reviewed EESCO's method and inputs used to calculate its service cost, focusing on the portion of the cost that represented compensation for use of its capital. EESCO's capital compensation cost included recovery of its debt interest expenses and a return on equity (ROE). The debt interest expense amounts were derived from actual monthly short-term and long-term debt interest expenses incurred by the company. EESCO calculated the amount of ROE charges monthly by applying an annual ROE rate to total equity reported on its books as of the previous month-end. EESCO's ROE rate was comprised of state regulator-approved and FERC-approved ROE rates for all the electric and natural gas companies in Eversource's corporate structure.[22]

State regulator-approved ROE rates were used for Eversource electric company subsidiaries with distribution segments and its natural gas companies. FERC-approved ROE rates were used for Eversource electric company subsidiaries with transmission segments. EESCO combined the multiple state and FERC ROE rates to calculate a single weighted average ROE rate that was applied to EESCO's total equity balance. The product of that calculation was then divided by 12 and allocated monthly as a component of service cost charged. In 2019, EESCO's weighted ROE rate used to determine its capital compensation cost was 9.80%. EESCO charged over $165 million in capital compensation cost to its affiliates, including CL&P, from 2016 to 2019. CL&P was charged $65 million during this period.

While reviewing CL&P's calculation of its annual transmission revenue requirement during the audit period, and certain of its retail rate of return calculations, audit staff noted that the EESCO capital compensation cost were included in CL&P's retail and Commission-jurisdictional transmission service rate determinations. However, inclusion of the cost in CL&P's retail rates was more transparent than the inclusion in Commission-jurisdictional transmission rates. For example, CL&P's retail rate case filed with the Connecticut Public Utilities Regulatory Authority (CT PURA) included standardized schedules and a formula calculation that demonstrated and provided notice to CT PURA of the EESCO capital compensation cost proposed for inclusion in CL&P's

[21] *See* 18 C.F.R. § 367.29 (2021), Compensation for Use of Capital.

[22] During the audit period, the EESCO ROE rate was comprised of the ROE rates of six electric and natural gas companies.

REDACTED

retail service rates.[23] Whereas, the transmission formula rate filing to the Commission does not provide this detailed disclosure of information.

Pursuant to 18 C.F.R. § 367.29 of the Commission's regulations, a service company's return on its capital investment is required to be reasonable. Also pursuant to the same regulation, EESCO is to provide to CL&P "[a]n annual statement to support the amount of compensation for use of capital billed for the previous 12 months and how it was calculated . . . ." The Commission also generally requires that formula rates be stated with sufficient specificity, clarity, and transparency so as to be understandable and reviewable by those affected by them and by the Commission. Moreover, in December 2015, pursuant to section 206 of the FPA, the Commission found that ISO-NE's Transmission, Markets, and Services Tariff was unjust and unreasonable because it lacked adequate transparency and challenge procedures with regard to the transmission formula rate protocols for ISO-NE Participating Transmission Owners (PTO)s, including CL&P.[24]

In June 2020, the ISO-NE PTOs jointly filed an offer of settlement to resolve all issues in the section 206 proceeding. To address the transparency concerns, the ISO-NE PTOs proposed replacing the then-existing formula rate narrative method with a new formula rate template and attachments with associated worksheets that provide for disclosure of the components and calculations of cost inputs to the template.[25] The settlement participants did not contest the filing. In December 2020, the Commission approved the filing as an uncontested settlement.[26] The effective date for the new formula rate template and attachments is January 1, 2022.[27]

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[23] *See In re: Application of the Connecticut Light and Power Company d/b/a Eversource Energy to Amend its Rate Schedule,* State of Connecticut Public Utilities Regulatory Authority, Docket No. 17-10-46 (filed Apr. 18, 2018).

[24] *ISO New England Inc. Participating Transmission Owners Admin. Comm.*, 153 FERC ¶ 61,343, at PP 1, 4-9 (2015), *reh'g denied*, 154 FERC 61,230 (2016).

[25] *See* ISO-New England Inc. Transmission, Markets, and Services Tariff, Section II.H Other Transmission Provisions, Attachment F, Annual Transmission Revenue Requirements 24.0.0, Appendix A 1.0.0., and Appendix C, Formula Rate Protocols 1.0.0.

[26] *ISO New England Inc. Participating Transmission Owners Admin. Comm.*, 173 FERC ¶ 61,270, at P 6 (2020).

[27] *See ISO New England Inc. Participating Transmission Owners Admin. Comm.,* Open Access Transmission Tariff Filing, Docket No. ER20-2054-001 (filed Jan. 27,

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Pursuant to the formula rate and formula rate protocols, CL&P is required to submit with its annual transmission revenue requirements information included in attachments and worksheets that render its submission understandable and reviewable by ratepayers and others affected by CL&P's rates and by the Commission. In order to avoid the transparency concerns identified by audit staff in the transmission formula rate annual informational updates and true-up filings submitted during the audit period, CL&P is encouraged to disclose the EESCO cost components and attributes that are considered in the derivation of the service company capital cost charges and included in CL&P's transmission rates in its future transmission formula rate annual informational updates and true-up filings. Such disclosure will ensure the filings include information useful in determining how service company capital costs are derived that are included in CL&P's jurisdictional rates and recovered from its transmission customers. To improve disclosure and ultimately transparency, CL&P should consider providing this information in a worksheet or attachment to its filings.

2021); *see also ISO New England Inc.*, Delegated Letter Order, Docket No. ER20-2054-001 (Feb. 24, 2021).

VI. CL&P's Response to Draft Audit Report

EVERSOURCE ENERGY

The Connecticut Light and Power Company
107 Selden Street
Berlin, CT 06037
(202) 508-0902
E-mail: donna.fulton@eversource.com

Donna J. Fulton
Director – Federal Regulatory Policy

January 20, 2022

Gerald Williams
Director and Chief Accountant
Federal Energy Regulatory Commission
888 First Street, N.E., Room 5G-06
Washington, DC 20426

Re: The Connecticut Light and Power Company
Office of Enforcement; Docket No. FA19-8-000

Dear Mr. Williams:

The Connecticut Light and Power Company (CL&P) appreciates the opportunity to respond to the draft report concerning the audit of CL&P in the above-referenced docket (Draft Audit Report), provided by the Office of Enforcement, Division of Audits and Accounting (DAA), of the Federal Energy Regulatory Commission (Commission) on December 27, 2021. The audit evaluated CL&P's compliance with: (1) approved terms, rates, and conditions of its transmission formula rate mechanism as provided in the ISO New England Inc. (ISO-NE) Transmission, Markets, and Services Tariff on file with the Commission; (2) accounting requirements of the Uniform System of Accounts Prescribed for Public Utilities and Licensees under 18 C.F.R. Part 101; (3) reporting requirements of the FERC Form No. 1, Annual Report of Major Electric Utilities, Licensees and Others, under 18 C.F.R. § 141.1; and (4) the requirements in Preservation of Records of Public Utilities and Licensees under 18 C.F.R. Part 125. The audit covered the period January 1, 2015 to December 31, 2019.

In the Draft Audit Report, DAA staff made five findings of noncompliance and made recommendations with respect to each finding. CL&P's response to each of the findings and recommendations is as follows:

Staff finding No. 1:

Allowance for Funds Used During Construction (AFUDC) – CL&P improperly included accumulated other comprehensive income and unamortized debt-related balances in long-term debt and equity balances used to compute its AFUDC rates.

Response:

CL&P agrees with the above finding and will comply with all recommendations in Numbers 1 through 7.

Staff finding No. 2:

Accounting for Compromise Settlements – CL&P incorrectly accounted for compromise settlement costs in operating expense accounts instead of Account 426.3, Penalties, or Account 426.5, Other Deductions, as required.

Response:

CL&P agrees with the above finding. CL&P will comply with all the recommendations in Numbers 8 through 12.

Staff finding No. 3:

Accounting for Tax Receivables – CL&P incorrectly recorded accounts receivables that represented refunds for overpayments of income taxes in Account 165, Prepayments, instead of in Account 143, Other Accounts Receivable.

Response:

CL&P agrees with the above finding. CL&P will comply with all the recommendations in Numbers 13 through 18.

Staff finding No. 4:

Merger Transaction Costs – CL&P improperly included merger transaction costs in operating accounts, contrary to the Commission's long-standing policy that such expenses be recorded in nonoperating accounts.

Response:

CL&P agrees with the above finding. CL&P will comply with all the recommendations in Numbers 19 through 23.

Staff finding No. 5:

Application of Nonapproved Depreciation Rate – CL&P used a depreciation rate for accounting and ratemaking purposes that was not filed with, and approved by, the Commission.

Response:

CL&P agrees with the above finding. CL&P will comply with all the recommendations in Numbers 24 through 26.

For all of the above findings, CL&P will prepare and submit to FERC Audit staff on a nonpublic basis a compliance plan to be submitted to DAA staff within 30 days of the date of issuance of the final audit report. CL&P will make nonpublic quarterly submissions to DAA staff describing the progress in implementing all recommendations until all are complete, and will include copies of any written policies and procedures developed in response to the recommendations for audit staff's review in the first quarterly filing after CL&P develops any such policies and procedures.

Other Matter:

Transparency of the Derivation of Service Company Capital Costs in Jurisdictional Rates – CL&P included capital cost charges from its service company, Eversource Energy Service Company (EESCO), in jurisdictional rate determinations. CL&P is encouraged to disclose the EESCO cost components and attributes that are considered in the derivation of the capital cost charges and included in CL&P's transmission rates in its future transmission formula rate annual informational updates and true-up filings or in the annual EESCO FERC Form 60. Such disclosure will ensure the filings include information useful in determining how service company capital costs are derived that are include in CL&P's jurisdictional rates and recovered from its transmission customers.

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Response:

CL&P will seek to implement DAA's suggestion.

In addition, CL&P offers in the attachment hereto a small number of suggested minor revisions in order to correct or clarify language in certain discrete sections of the Draft Audit Report. If you have any questions, please contact me at 202 508-0902.

Sincerely,

/s/ [redacted]
Director – Federal Regulatory Policy