

APPRAISING UTILITIES

Under RSA 83-F the Department of Revenue (DRA) is given the statutory authority to develop an opinion of value for every utility property in New Hampshire. To accomplish this, DRA utilizes valuation techniques that conform to USPAP (Uniform Standards of Professional Appraisal Practice), a nationally recognized series of guidelines that require the appraiser to “correctly employ those recognized methods and techniques necessary to produce a credible appraisal” (USPAP Standard Rule 1-1).

The process by which an assessor or tax administrator arrives at an opinion of value for a property is the appraisal or valuation process. In appraising utility properties, the most frequently utilized methodology is the *unit appraisal* concept, which is defined as follows:

"This is an appraisal of an integrated property as a whole without any reference to the value of its component parts. It is to be distinguished from fractional appraisal, which is a valuation of one of the parts without reference to the value of the whole, and from the summation appraisal, which is a valuation of the whole derived by adding two or more fractional appraisals."¹

The unit valuation method most accurately estimates the value of that which is being appraised, namely, the company or unit in its entirety. Typically, public utility properties extend into several taxing jurisdictions and retain/optimize their value by synergistically operating as a system or unit. The individual portion of the system that is located within a designated taxing district has a value that is contributory to the entire system.

The origins of unit valuation began with the valuation of railroads wherein, in order to value each section of track, the overall value of the railroad as a going concern first had to be estimated. This value was then distributed across the entire line, based on the argument that each rail section was essential to realizing the potential of the overall enterprise. Without the track in one taxing jurisdiction, the remaining miles of track and related facilities located elsewhere had very little value. By the same argument, each mile of track contributed equally to company value. This method of estimating market value came to be known as the unit (or unitary) approach (or rule). It is based on the argument that assembled and operating tangible assets are worth more in real-world markets than the sum of the individual unassembled parts.²

From this integrated perspective, any one particular component or asset in this complex array of many property items defies individual or segregated valuation. This is because a particular component would fail to reflect the natural synergism of all the assets assembled to assure the long-term viability of the entire utility entity. In actuality, when a property is distributed across multiple jurisdictions, the principle that the value of the components is best understood by valuing the integrated whole property first is not restricted to utility property. In New Hampshire and elsewhere, whenever a single property straddles two (or more) jurisdictions, it is common practice for the local assessing authority to value the entire property according to the property's highest and best use, and then allocate a percentage of the total value to each municipality.

¹ *Appraisal of Railroad and Other Public Utility Property for Ad valorem Purposes*; National Association of Tax Administrators, June 1954, Page 2.

² *The Unit Approach to the Taxation of Railroad and Public Utility Property*; G. Cornia, D. Crapo, L. Walters, Lincoln Institute of Land Policy, May 2013, Page 133.

With the preceding in mind, two important concepts emerge, as follows: 1) While the courts refer to five acceptable approaches to value, three of these refer to variations of the cost approach. The result is the same three approaches (income, cost, and sales comparison) apply to both regulated and unregulated assets; 2) the concept and practice of allocating total value to multiple municipalities applies to both regulated and unregulated utilities.

APPRAISAL OF REGULATED UTILITY PROPERTIES

Regulatory constraints are imposed on utilities when government exercises its right to protect the general welfare and safety of the public through what is known as "police power." In the context of valuing utility properties, the exercise of police power only diminishes the rights of the fee simple estate; it does not create separate estates. The resulting diminished property rights become inextricably intertwined with the real estate. In New Hampshire, utility properties can be regulated by either (or both) the NH Public Utility Commission (NH PUC) and/or the Federal Energy Regulatory Commission (FERC). The regulatory compact between the regulating agency and the utility enables the regulating agency to do such things as: a) establish limitations on the rates charged by the utility; b) establish limitations on the rate of return the utility is allowed to achieve on its investments; c) establish limitations on the type of assets (and investments) that the utility is allowed to earn a return on; d) mandate sufficient maintenance and capital expenditures in order to assure reliability and viability of the utility property; e) require approval by the regulating agency for the sale of the property; and f) in order to assure reliability and viability of the whole unit, the severability of a local segment of the network to an independent buyer is highly unlikely or, at a minimum, subject to rigorous scrutiny and administrative delays.

From a valuation perspective, the practical implications of these regulatory constraints and diminished property rights are considerable. Firstly, because the basis for the regulatory constraints identified above is derived from the state's exercise of its police power, the impact flows directly to the legal permissibility test in the determination of highest and best use (HBU), similar to zoning considerations. Because a properly executed HBU analysis is the foundation of the entire appraisal that follows, once the HBU analysis is completed, every aspect of the appraisal must adhere to the consistent introduction of assumptions, selection of market data, and application of valuation techniques associated with the HBU conclusion. This is known as the principle of "consistent use." For instance, the appraiser cannot reach a conclusion for the HBU of vacant land as residential, and then proceed to develop an analysis predicated on industrial comparables and industrial market data.

Typically, the impact of regulation on value is considered in the context of external/economic obsolescence. To better understand the impact of regulation on economic obsolescence in the valuation of real estate, an intuitive comparison can be found in a residential market subject to rent control.

Rent regulation (or rent control) is a system of laws administered by a court or a public authority, which aim to ensure the quality and affordability of housing and tenancies in the rental market. Generally, a system of rent regulation involves the following: a) price controls or limits on the rent that landlord may charge; b) standards by which a landlord may terminate a tenancy; c) obligations on the landlord or tenant regarding adequate maintenance of the property; d) a system of oversight and enforcement by an independent regulator; and e) the likely diminution of value at the time of resale (as compared to similar but unregulated residential properties) due to the

decreased income potential and diminished pool of likely buyers. Overall, the objective is to protect the public by limiting the price that would result from the market, where inequality of bargaining power between landlords and tenants produces continually escalating prices without any stable market equilibrium. Clearly, the intent and administrative mechanisms associated with rent control are strikingly similar to that of utility regulation and, as an intangible "intimately intertwined with the Property, cannot be separated from the Property..." *Epping Senior Housing Associates LP v. Town of Epping, BTLA* (2005).

Indeed, regulation that impacts the market value of real estate must be incorporated into any valuation analysis that leads to an opinion of market value. NH case law including: *Royal Gardens Co. v. City of Concord*, 114 N.H. 668, 671-72 (1977), *Demoulas v. Town of Salem*, 116 N.H. 775, 781 (1976), and *Stuart J. Steele & a. v. Town of Allenstown*, 124 N.H. 487 (1984), affirm this principle.

Therefore, the process of formulating an opinion of value must take into consideration the impact of regulation.

When developing a sales comparison approach to value of a rent-regulated property, sales of similar rent-regulated properties would be compared and contrasted. By extension, sales of unregulated properties should not be relied upon.

When developing the income approach to value of a rent-regulated property, because the fee simple estate remains intact and is only diminished, the rent restricted income would be incorporated into the income approach analysis (even for the purpose of ad valorem taxation in NH). In addition, elevated maintenance and administrative expenses would be introduced due to regulatory requirements, and additional risk factors would be required in the terminal cap rate to account for the likely reduced reversion (or resale) of the encumbered real estate. This would result in a value below that of a property not subject to rent control restrictions, all else being equal.

When developing the cost approach to value of a rent-regulated property, the per unit costs derived from a cost manual such as the Marshall Valuation Service would proceed in exactly the same manner as an identical property not encumbered by rent control restrictions, including the calculation of physical depreciation. However, a credible solution to the valuation problem requires all forms of depreciation to be identified and accounted for in the appraisal. Because the economic loss associated with the rent restrictions results in external/economic depreciation or obsolescence, a further adjustment is required. Until this last step is taken, any valuation that does not consider the adverse economic impact resulting from the diminished property rights remains incomplete.

With the diminished property rights associated with utility regulation in mind, the valuation of a regulated utility would progress in a manner similar to rent regulated property, with several additional considerations. Because a utility owns assets distributed across multiple municipalities, it is convenient to think of these geographically distinct assets as separate marketable segments in isolation of one another. However, recalling that the purpose of regulation is to protect the public by preserving system reliability and govern utility rates, the legal and economic consequences of regulation extends to all the assets. In other words, the diminished property rights associated with the HBU determination of a regulated utility is

intertwined throughout the entire integrated system. Whether viewed from the perspective of the entire enterprise, or from the perspective of the smallest segment, the consequences of regulation are intertwined with the real estate and must be valued as such. Therefore, the valuation of a segment must take into account the same HBU considerations as the valuation of the enterprise, including the greatly reduced severability and marketability of the assets at the segment level imposed by the regulating agency.

For this reason, a credible valuation of a regulated utility will consider the following:

To develop a sales comparison approach to value of a regulated utility, sales of regulated properties would need to be compared and contrasted. However, that there are few, if any, sales of local segment assets, confirms and supports the integrated HBU of regulated utility assets as a unified enterprise. Because the regulating agency will review and must approve any request to transfer assets to another owner, a local segment is not automatically severable and, if it was, the segment would be subject to severe constraints on marketability and control, and would suffer from illiquidity issues. The same absence of immediate legal permissibility also applies to an ostensibly marketable generation asset/segment owned by the regulated parent company. Therefore, a discount for the diminished marketability of the regulated segment assets, even if in varying degrees, would be expected in the projected sale price of an individual segment. Once again, the absence of segment sales (regionally and nationally) is a compelling indicator of the limited market for these localized assets, and why discounting is required in conformity with classic valuation/finance theory and well-recognized practices. Regarding enterprise-level sales, these transfers of ownership are not only infrequent, they are generally clouded with too many investor/finance-related considerations to allow extraction of reliable and meaningful indicators of value. Classic finance theory reminds us that investors will not pay more for assets than that amount on which they can earn a return. Therefore, while minor variations in sale prices, higher or lower than the regulatory agency's approved net book value would be expected, excessive differences are expected to reflect investor-related decisions that are not related to market value. Hence, net book is only a logical and reasonable point of departure to understand market value and, after further analysis, because the market is dynamic on a year-to-year basis (cap/discount rates vary in response to perceived market risk, housing starts and consumer confidence varies, natural gas prices vary, plant retirements and additions vary, demand and capacity varies, energy policy varies, etc.) the concluded market value might be higher or lower but would be expected to be within a reasonable range of net book. The statutory underpinning of RSA 83-F (as well as RSA 72:8 and 75:1 that guide the local municipality in its own assessments) is market value, not investor value. Constitutionally and statutorily, the DRA and the local assessor are both charged with the requirement that market value remain the basis for the valuation exercise. For all of these reasons, the direct comparison of enterprise-level multi-jurisdictional utility sales to a local municipal segment is not a sound or credible practice.

In regard to the income approach to value of a regulated utility, the unavailability of reliable sale data makes it very difficult to extract reliable capitalization or yield rates from sales. In response, the “buildup” technique is a universally accepted method to develop rates. A built-up rate is the sum of financial risk factors that combine a market-derived safe rate (risk-free), and rates reflective of the industry, equity requirements, and size. This technique reflects the principle that investors generally require a greater return on assets that are more risky and that meet the needs of both debt and equity. The rate components in the buildup method for utility-related assets are extracted from market sources on an after-tax basis because that is how

investors generally analyze and report investments. Therefore, because finance theory requires that we match rates and cash flows, after-tax cash flows are utilized to model net operating income. Use of EBITDA (earnings before interest, taxes, depreciation and amortization) as NOI or as a multiplier is not a credible unit of comparison because of the dissimilar accounting practices across firms, even while in compliance with GAAP. As a result, EBITDA fails on two counts: 1) given the variability in internal accounting procedures across firms, it is extremely difficult to extract reliable finance data for the purpose of comparison; and 2) EBITDA fails to take into account the necessary capital expenditures (CapEx) required, in addition to yearly maintenance, to retain the utility assets into perpetuity. CapEx in utility valuation modeling is intended only to replace existing long-term assets that will be retired. Properly modeled, CapEx is not intended to increase the scope of the existing assets.

In regard to gross revenue, because the fee simple estate remains intact and is only diminished by regulation, projected revenue is predicated on the retail rates approved by the regulating agency. In addition, the following considerations would be expected in a credible income analysis: elevated maintenance expenses expected of regulated utilities (regulator enforced reliability); additional administrative expenses to comply with regulation; additional risk factors required in the rate to account for the regulatory lag associated with adverse revenue timing factors (rate case appeals to modify allowed rates, rate base additions between rate cases, operating cost changes between rate cases, regulatory disallowance of prudent costs, loss of contracts, equity ratio increases during construction periods); consideration for the assets owned by the utility but not allowed to earn a return such as Construction Work in Progress (CWIP), Contributions in Aid of Construction (CIAC) and acquisition adjustments; and an elevated terminal cap rate to account for the uncertainty/risk of delays associated with the regulator's approval of a proposed sale or merger.

When developing the cost approach to value of a regulated utility property, the economic loss attributable to the diminished property rights associated with regulatory restrictions must be considered. Some of the factors associated with regulatory external obsolescence include: reliance on original cost minus book depreciation by the regulating agency, rather than trended cost, for calculation of rate-base and the allowed return on equity; regulatory lag associated with adverse revenue timing factors, such as a rate case to modify allowed rates; and uncertainty/risk of delays associated with the regulator's approval of a proposed sale or merger. Each of these issues is associated with external/economic depreciation or obsolescence, and a credible solution to the valuation problem requires all forms of depreciation to be identified and accounted for in the appraisal. Until this last step is taken, any valuation that does not consider the economic impact resulting from the diminished property rights remains incomplete.

Importantly, whether valued from the top as an enterprise, or valued from the bottom at the segment level, the impact of the diminished property rights attributable to the regulator's enforcement of police powers and regulation, must be addressed in the appraisal.

APPRAISAL OF UNREGULATED UTILITY PROPERTIES

The appraisal of unregulated utilities adheres to all the same valuation techniques as regulated utilities, including the necessity to study and adjust for external/economic obsolescence. However, important distinctions emerge, as follows: 1) In the income approach, market-derived factors (projected wholesale rates and expected rates of return) are substituted for the

rates imposed by the regulatory agency; 2) In the cost approach, if any external/economic depreciation or obsolescence is identified, the adjustment may be applied but the source of the depreciation will not be attributable to regulation and the exercise of police powers by the state; and 3) in the sales comparison approach (if able to complete in a credible manner) the selection of appropriate comparables will be derived from other unregulated sales. As a result, there are three steps to the unit valuation method:

1. Identify the unit or total assemblage of assets to be appraised;
2. Form an opinion of the total unit's value by the appropriate approaches to value; and
3. Allocate a portion of the total unit to the appropriate assessing tax district(s).

The “Unit Method” then becomes the platform for the application of traditional valuation techniques. The traditional valuation methodologies are: the Cost, Sales Comparison, and Income approaches to value. A brief explanation of each technique and their respective strengths and weaknesses follows:

1. **COST approach to value:** This approach considers the depreciated cost of the assets, including land. The relevance of a cost approach is very intuitive, because a property's value should be similar to what someone paid to build it. When the property is new, this may be true. However, even at this optimal point in time, the market perceived value might not equal cost. A classic example is the swimming pool that a homeowner spent \$20,000 to have installed, while the typical residential market response is to immediately depreciate the pool's “value” substantially.

In general though, when discussing the cost approach it is important to consider the particular market the entity is associated with.

If a utility entity is associated with the unregulated market, independent of rate-base requirements associated with compliance with the New Hampshire Public Utilities Commission, there are at least two significant reasons why the unregulated market typically does not rely on the cost approach as the primary basis for determining value: 1) All three types of depreciation (physical, functional, and economic/external) must be considered, and these estimates can be very speculative. Of the three types of depreciation, physical depreciation is the easiest to estimate. However, functional and economic/external depreciation are usually understood in the context of an economic analysis of the entity's performance relative to the market, and this can be difficult to quantify, and; 2) The appraisal must evaluate an entity the way an investor would, and most investors in the unregulated market simply rely on the cash flow as the basis for negotiating a purchase or sale agreement. Overall, however, the cost approach can be a useful technique when developed properly and completely, and is also used in conjunction with other supporting approaches to value.

If, however, one is considering a utility entity associated with the regulated market, wherein the utility is required to comply with rate-base requirements associated with the New Hampshire Public Utilities Commission, the relevance of the cost approach is treated differently than for the unregulated market. This is because this sub-market (of NH PUC regulated utilities) attaches significant relevance to the prevailing rate-base established by the PUC, and to the elements of consideration that the PUC relies on to derive the rate-base for a specific utility. Overall, these elements of consideration are more closely identified with the cost approach than the income

approach, and because rate-base is relatively similar to a cost approach, it is reasonable that additional emphasis be attached to the cost approach, over and above that of the income approach.

2. SALES or MARKET COMPARISON approach to value: This approach develops an opinion of value for the appraised property by comparing similar or conforming properties to the property being appraised. However, as a special purpose property, the availability of reliable comparable sale data is typically very limited. Additionally, as previously described, the negotiated sale price is often clouded with complex financial and accounting offsets that hinder establishing a meaningful per-unit sale price.

3. INCOME approach to value: This approach considers the capitalized value of the net operating income of a utility company. Two primary analytical options are available, either Direct Capitalization or Discounted Cash Flow (DCF).

Direct capitalization attempts to convert a single year's net operating income into an estimate of value, and this technique is most relevant when the cash flow is expected to be uniform or stable over time. Alternatively, a discounted cash flow assumes a series of projected cash flows over several years (typically 10 to 25), plus the projected resale of the property at the end, and then discounts these values back to the current date to reflect the time value of money (the concept that \$1 received today is worth more than \$ received in the future, due to the certainty of payment today versus the unknown risks in the future and inflation). Overall, each of these capitalization techniques has its strengths and weaknesses, and the selection of either technique is best determined only after studying the appraised property. One advantage of the income approach to value is that depreciation (all three types) does not have to be separately calculated as it is automatically captured in the analysis. If the company's assets are in physical disrepair, its operations will be less efficient and its net income will be lower. Conversely, if the assets are maintained properly, its net income will be higher. Continuing with this reasoning, if there are reasons why a company's operations are not functionally conforming to market expectations, or if there are economic/external constraints on its business, such as governmental regulation, these impacts will also be reflected in the company's cash flow and/or capitalization or yield rate.

At this juncture, it is important to remind the reader that one of the fundamental principles of both valuation and finance theory is that the cash flow must match the selected rate, and vice versa, when developing an income approach to value. There are no exceptions to this principle, regardless of the type of property being appraised.

This principle is universally understood and is applied every day by national and local assessors and valuation experts in several ways. Two common valuation scenarios serve to illustrate the application of this principle, as follows:

1) The market derived capitalization/discount rates available for typical commercial property (industrial, office, retail, apartments, etc.) are on a pre-income tax basis and, as a result, the subsequent cash flow is also rendered on a pre-income tax basis;

2) When constructing a cash flow for assessment purposes, the expense for property taxes is typically excluded resulting in a net operating income (NOI) greater than it would be otherwise and a higher property value, all else being equal. However, the artificially high NOI is then offset by adding a property tax component to the

capitalization or discount rate, thus reducing the value. Theoretically, all else being equal, the results are the same; i.e., whether the property tax expense is included and the rate is not adjusted, or the property tax expense is excluded and the rate is adjusted.

Indeed, the mathematical relationship between a rate and cash flow is so intertwined that if you were to begin with an after-income-tax rate and utilize a pre-income-tax cash flow, a simple adjustment to the after-income-tax rate will theoretically lead to the same result had a pre-income-tax rate been applied at the beginning, all else being equal. The reverse is also true wherein if you were to begin with a pre-income-tax rate and utilize an after-income-tax cash flow, a simple adjustment to the pre-income-tax rate will theoretically lead to the same result had an after-income-tax rate been applied at the beginning, all else being equal. The formulas to convert each rate are widely available, but a simple illustration below demonstrates the results are identical when the rate is properly matched to the cash flow:

If we assume a pre-income-tax cash flow of \$1,000 and a pre-income-tax rate of 10%, the value is $\$1,000 / 10\% = \$10,000$.

Alternatively, if we assume an income tax rate of 40%, the pre-income-tax cash flow and pre-income-tax rate are both adjusted by the income tax rate, and the result is identical to the preceding pre-income-tax value, as follows: $\$1,000 (1-40\%) / 10\% (1-40\%) = \$10,000$.

Therefore, in the specific instance of utility property valuation, the income approach (whether direct capitalization or discounted cash flow) is predicated on an after-income-tax analysis. This is because the market derived rates for the utility sector are reported on an after-income-tax basis. As a result, because both finance and valuation theory requires the cash flow to match the rate, depreciation and income taxes must be introduced into the cash flow analysis when valuing utility properties. This brings the cash flow into conformity with the after-income-tax rate.

Importantly, while appraisal theory considers each of the three techniques above (cost, sales, and income) to be independent of the others because each valuation technique relies on different types of data and assumptions, there are frequently elements of each analysis that are intertwined; since, “in applying the sales comparison approach appraisers often analyze conclusions derived in the other approaches to determine the adjustments to be made to the sale prices of comparable properties.”³ For instance, the sales comparison approach requires adjustments for the varying economic or legal characteristics (such as supply and demand, the principles of substitution, reversionary trends, market anticipation, zoning and/or other external forces such as regulatory considerations) that distinguish each sale comparable from the appraised property⁴. Similarly, “the analysis of cost and sales data is often an integral part of the income capitalization approach, and capitalization techniques are frequently employed in the cost and sales comparison as well.”⁵ Hence, the introduction of elements (or variations of same) from one approach to value into another approach to value is in conformity with valuation theory and has a role in the Department’s calculation of external/economic depreciation or obsolescence. For instance, in developing this adjustment the Department typically relies on an income-loss calculation wherein the appraised property’s actual performance is compared to the market. Specifically, this calculation effectively compares how the return on assets of the subject

³ *The Appraisal of Real Estate*; Appraisal Institute 14th Edition, 2013, Pages 377.

⁴ *The Appraisal of Real Estate*; Appraisal Institute 14th Edition, 2013, Pages 45-47.

⁵ *The Appraisal of Real Estate*; Appraisal Institute 14th Edition, 2013, Pages 439, 564, 565.

(subject's net operating income/depreciated assets) compares with market expectations and performance (market's net operating income/depreciated assets). When deriving these comparative calculations, we are drawing upon estimates of net operating income, normally associated with the income approach, and applying the adjustment to the cost approach. Importantly, not only is the cross-pollination of concepts in each approach permissible, but the Department deliberately looks outside the income approach for independent market-related sources of information to support the comparison. Hence, the return on assets derived from the subject's performance is compared to a return on assets derived from the market and the income and cost approaches to value remain independent of one another. As a result, there is no circularity of reasoning associated with the calculation and/or the Department's methodology.

In regard to the relative weighting attached to the final results of each approach to value, or the reconciliation, utilization of more than one technique (when possible) is considered to be desirable since each serves as a proof-check on the others. From a practical standpoint, the ability to develop a particular analysis is usually determined by the availability, reliability, and relevance of the data to the particular market the property is associated with. It is also important to note that the selected reconciliation factors, like any other information gleaned from market activity such as capitalization rates, is not expected to remain static from year-to-year. The selected weighting factors are dependent on the economic swings that influence market activity, such as expected changes in investor activity, consumer confidence, the strength or weakness of housing starts, shifting supply and demand patterns and the availability of investment capital to specific markets, and even external considerations such as local and/or national regulatory actions and foreign events that ripple through the market.

In regard to regulated utilities, DRA typically receives sufficient information to complete both a cost and income approach to value. When more than one valuation technique is utilized, a single opinion of final value must be derived from the different approaches to value and, as described above, is known as reconciliation. While reconciliation occurs throughout the appraisal process as various assumptions are adjusted and brought into conformity with the appraised property, the last phase of a valuation problem is also known as reconciliation. Generally, a reconciliation of the different values derived from the cost and income approaches is largely determined by the criteria described above: the quality and reliability of the data available to any particular valuation technique, and the relevance of any particular technique to investors or a particular market. For instance, in the course of our discussion with utility owners, operators, and utility analysts, DRA has come to conclude that investors in utility properties regulated by the NH PUC or FERC are more attuned to its depreciated cost than the cash flow, because the depreciated cost or regulated rate base is what determines the rate of return the entity can earn. Therefore, if a property is subject to the rate-base constraints imposed by the NH PUC and/or FERC, the cost approach to value may receive the greatest weighting in the final reconciliation. Conversely, the DRA has come to conclude that investors in utility properties not regulated by the NH PUC or FERC are more interested in the cash flow performance than depreciated cost. As a result, the income approach is frequently given the greatest weighting in our reconciliation.

It is also worth noting that, in regard to evaluating the merits of any final reconciliation decision, the underlying factors of consideration are not always as clear-cut as distinguishing between regulated vs. unregulated. For instance, the utility formerly known as Public Service of New Hampshire (PSNH, and now known as Eversource Energy) is regulated both by the NH PUC and FERC, wherein the allowed rates of return are imposed by the various regulatory agencies. In

addition, the regulatory agencies will retain the final administrative decision on the sale of the utility as a whole, or the sale and severability of limited segment-related assets. Alternatively, the New Hampshire Electric Cooperative (NHEC) is a member-owned and controlled electric distributor that is not governed by NH PUC rate based requirements and establishes its own projected rate of return. However, because of the integrated nature of NHEC's electric distribution assets, the NH PUC retains the final administrative decision on the sale of the utility as a whole, or the sale and severability of limited segment-related assets. The NH PUC performs this role in order to fulfill its statutory mandate to protect the public interest. Therefore, in this unusual instance, the Department assigns greater emphasis to NHEC's income approach to value than the cost approach, because NHEC's governing board has assumed the same role in evaluating and directing its own financial performance as other unregulated companies. It is also important to note that assigning greater weight to the income approach does not negate the unified nature and HBU of NHEC's assets and/or the underlying regulatory oversight associated with any proposed sale of the whole, or the sale and severability of limited segment-related assets. These last comments are included to illustrate the nuance and complexity associated with appraising utility property.

One additional step remains after the reconciliation and the final opinion of unit or total utility value is completed. Because utility property is frequently distributed over several taxing/geographic jurisdictions, the total reconciled unit market value of a company is then allocated to the various municipalities on an original cost basis. By utilizing gross original cost before depreciation is taken, each municipality with utility assets is assured they receive consideration for the asset's presence, even if fully depreciated on the company's books. Therefore, if the final (total) unit value of Company XYZ is \$1,000,000, and the cost basis for Company XYZ is 70% in Londonderry and 30% in Manchester, then the allocation of value to Londonderry is \$700,000 ($\$1,000,000 \times 70\% = \$700,000$), and the allocation of value to Manchester is \$300,000 ($\$1,000,000 \times 30\% = \$300,000$). The appraised company typically provides the specific assignment of the cost basis to each municipality, and DRA completes the geographic allocation on a percentage basis. Importantly, the allocation percentages can vary from year to year as a company adds or retires assets in one or multiple municipalities. In addition, whenever possible and if provided sufficient information to isolate specific assets, such as exempt pollution control assets, to a municipality the department will make every effort to effect the allocation on a local basis in the interest of local and state-wide equity.

In conclusion and as previously described, the statutory underpinning of RSA 83-F (as well as RSA 72:8 and 75:1 that guide the local municipality in its own assessments) is market value consistent with the utility's highest and best use and not investor value. In order to accomplish this, the methodology adhered to by the Department is consistently grounded in market-derived assumptions, well-established valuation and finance theory, and "correctly employs those recognized methods and techniques that are necessary to produce a credible appraisal."⁶

⁶ *Uniform Standards of Professional Appraisal Practice (USPAP) 2014-2015*; The Appraisal Foundation, Standards Rule 1-1(a).