STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Central Hudson Gas & Electric Corporation for Electric Service	Case 05-E-0934
Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Central Hudson Gas & Electric Corporation for Gas Service	Case 05-G-0935

DIRECT TESTIMONY AND EXHIBIT OF

THE NEW YORK STATE CONSUMER PROTECTION BOARD

Dated: May 1, 2006
Albany, New York

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INTRODUCTION

Q. Please state your names, titles and business addresses.

A. Douglas W. Elfner, Director of Utility Intervention, New York State Consumer Protection Board (“CPB”), Suite 2101, Five Empire State Plaza, Albany, New York, 12223.

My name is Hugh Larkin, Jr. I am a Certified Public Accountant licensed in the States of Michigan and Florida and the senior partner in the firm Larkin & Associates, PLLC, Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan 48154. I am appearing on behalf of the New York State Consumer Protection Board.

Tariq N. Niazi, Chief Economist, New York State Consumer Protection Board, Suite 2101, Five Empire State Plaza, Albany, New York 12223.

Q. Dr. Elfner, please summarize your background and experience.

A. My background, qualifications and experience are summarized in Attachment I.

Q. Mr. Larkin, have you testified previously in this proceeding?

A. Yes. I submitted pre-filed direct testimony and an exhibit dated November 21, 2005. That testimony includes an attachment which summarizes my regulatory experience and qualifications.

Q. Mr. Niazi, have you testified previously in this proceeding?

A. Yes. I also submitted pre-filed direct testimony and an exhibit dated November 21, 2005. That testimony includes a description of my experience and qualifications.

Q. Do you have an exhibit supporting your testimony?

A. Yes. We are sponsoring Exhibit___(CPB), consisting of three schedules.

Q. What is the purpose of your testimony?

A. On April 17, 2006, Central Hudson Gas & Electric Corporation ("Central Hudson" or "the Company"), Staff of the New York State Department of Public Service ("DPS Staff") and Multiple Intervenors ("MI") submitted a Joint Proposal ("Joint Proposal") for consideration by Administrative Law Judges ("ALJs") Michelle L. Phillips and William Bouteiller and the New York State Public Service Commisison ("PSC" or "the Commission"). That Joint Proposal would resolve all major contested matters in the above-entitled proceedings through June 30, 2008, including Central Hudson's requests for a $51.5 million (30.5%) increase in electric delivery revenues and a $17.5 million (42.5%) increase in natural gas delivery revenues effective July 1, 2006, whether a fixed price commodity option is available for Central Hudson's residential and small business customers and numerous other issues associated with a long term regulatory plan. The Joint Proposal would authorize the Company to increase electric delivery revenues by $17.9 million (10.5%) on July 1, 2006, and again by $17.9 on July 1, 2007 and

July 1, 2008. (Joint Proposal, Appendix A, Schedules 1 and 2) It would also permit the Company to increase natural gas delivery revenues by $8.0 million (19.0%) on July 1, 2006 and $6.1 million (11.8%) on July 1, 2007. (Joint Proposal, Appendix D, Schedule 1) In this testimony, we evaluate the Joint Proposal, demonstrate that it should be improved for the benefit of consumers, and explain how it should be improved.

Our testimony has five parts. In Part I, we demonstrate that the Joint Proposal does not satisfy the Commission's Settlement Guidelines. We show that it contains several provisions that are not in consumers' interest, that it is not supported by a spectrum of normally adverse parties, and that it would not likely have been the result of a litigated proceeding.

In Part II, we provide the background and context that the ALJs and the Commission should use to evaluate this Joint Proposal. We explain that because of high energy commodity prices and very large proposed delivery price increases, the Joint Proposal should be carefully reviewed to determine whether policies and practices that may have been common in an era of stable and lower energy prices, are appropriate now. Policies that deny customers the opportunity to purchase commodity from the utility at fixed prices when such options are generally not available from ESCOs at just and reasonable rates, permit unreasonably large increases in certain expense categories, enable the utility to retain ratepayer funds for unspecified purposes and require ratepayers to fund projects that are not necessary for safe and reliable service, are inappropriate at this time.

We explain in Part III that the Joint Proposal does not provide consumers additional tools to help manage high commodity prices. We demonstrate that the Commission should direct Central Hudson to offer both electricity and natural gas to its residential and small commercial customers at a fixed price. We also explain that the Commission should direct the Company to conduct additional outreach and information regarding the reason for high commodity prices, actions that consumers can take to manage and reduce their energy bills and how consumers may obtain assistance in paying their utility bills.

In Part IV we address revenue requirement and other financial issues. The CPB recognizes that electric and natural gas delivery rate increases are necessary in this proceeding. However, we explain in detail that there are approximately one-half dozen logical revisions that could and should be made to the revenue requirement provisions of the Joint Proposal that would benefit consumers, but should not affect the Company's earnings. We also identify several other adjustments that would affect the Company's earnings, are necessary to ensure just and reasonable rates, and would enable the Company to provide safe and reliable service.

In Part V, we briefly address some of the positive elements of the Joint Proposal, including some revenue requirement adjustments, the phase-in of rate increases, the low income program and the fact that it properly excludes several recommendations made by some parties in direct testimony.

Q. Please provide an overview of the CPB's position on the Joint Proposal.

A. This is one of the most important cases to come before the Commission in recent years. It is the first rate case for one of the state's large energy utilities since energy commodity prices increased substantially, and provides one of the first opportunities for the Commission to take action to help consumers address those high commodity prices. This case also involves the largest percentage delivery rate increases for a large energy utility to come before the Commission in more than a decade, and provides an opportunity for the PSC to determine how ratemaking practices that may have been appropriate in an era of generally stable delivery and energy rates, should be modified to address significant upward pressure on those prices.

Unfortunately, in our view, the Joint Proposal does not satisfactorily address either of these important issues. Regarding the impact of higher commodity prices, the Joint Proposal is virtually silent, and would provide consumers no additional tools to help manage their energy bills. The CPB made a proposal to address this issue in the pre-filed direct testimony of Mr. Niazi in this case, under which Central Hudson would offer fixed price commodity products to its mass market customers. That recommendation was not rebutted by any party, yet it is completely ignored in the Joint Proposal. Similarly, in many respects, the Joint Proposal does not appropriately recognize that regulatory practices that may have been appropriate in an era of stable energy prices and delivery rates should be reconsidered in view of high commodity prices and large proposed delivery rate increases. For example, rates should not reflect unreasonably large increases in projected expenses, projects that are not necessary for safe and reliable service should be postponed, ratemaking should match project costs and benefits instead of reflecting costs and ignoring benefits, and all reasonable means should be used to mitigate the impact of price increases.

Overall, the CPB opposes the Joint Proposal and believes that it does not adequately reflect consumer interests. We recommend that the ALJs and the Commission improve the Joint Proposal in the manner we suggest herein.

PART I - THE SETTLEMENT GUIDELINES

Q. Please provide an overview of the PSC's Settlement Guidelines.

A. The PSC assesses the reasonableness of any proposed settlement and determines whether it is in the public interest by comparing its terms against standards specified in the Commission's "Settlement Guidelines." (Cases 90-M-0255 and 02-M-0138, Opinion No. 92-2, March 24, 1992) The relevant provisions of the "Settlement Guidelines" are as follows:

> 1. A desirable settlement should strive for a balance among (a) protection of the ratepayers, (b) fairness to investors, and (c) the long term viability of the utility, and should be consistent with sound environmental, social and economic policies of the Agency and the State; and should produce results that were within the range of reasonable results from a Commission proceeding. (Id., p. 30)

Q. Does the Joint Proposal satisfy this requirement?

A. No, it does not. As we explain in detail below, the Joint Proposal does not provide adequate benefits for ratepayers nor does it achieve a result that the CPB would expect following a litigated proceeding. The CPB testified that Central Hudson should provide its customers the option to purchase electric and natural gas at a fixed price. That recommendation was not opposed or rebutted in testimony filed in this proceeding by any party. Despite the absence of any record evidence against that proposal, the issue is inexplicably omitted from the Joint Proposal – a result that would not have been expected in a litigated proceeding.

Similarly, the Joint Proposal would resolve several revenue requirement issues in a manner that would not have been expected in a litigated proceeding, as explained in detail in Point IV. For example, rate increases under the Joint Proposal are premised on capital expenditure projections that are larger than any party recommended in their initial testimony. In addition, the Joint Proposal reflects right of way maintenance expenditures of an amount proposed by the Company in initial testimony, with only a minor adjustment, which results in a projected increase of 107% beyond 2005 levels, far outside the range of reasonableness. Further, the Joint Proposal permits the Company to retain more than $20 million of available ratepayer-contributed funds, despite the compelling need to provide customers relief in this proceeding. Had this issue been addressed in the public process of litigation, it is highly unlikely that the conclusion would be that the Company should be permitted to retain these ratepayer funds. Finally, the Joint Proposal continues and expands existing programs, and includes new programs that are not necessary for safe and reliable service. Again, if those issues had been addressed in the public litigation process, it is unlikely that the conclusion would have been that ratepayers should fund unnecessary programs at this time.

The Joint Proposal is also heavily weighted toward the perceived interests of Energy Services Companies ("ESCOs"), to the detriment of consumers, as explained in detail below. This is not a result that would have been expected had this case been litigated, since not a single ESCO filed testimony in this proceeding on any issue.

For these and other reasons, we suggest certain improvements to the Joint Proposal that would more reasonably balance ratepayer and shareholder interests, be more likely to result from an open, litigated proceeding and that properly consider consumers' concerns.

Q. Does the Commission use any other criteria in evaluating settlement agreements?

A. Yes. In assessing any settlement agreement, the Commission is required to:

> 2. …give weight to the fact that a settlement reflects agreement by normally adversarial parties. (Id., pp. 30 – 31)

However, the Joint Proposal is not supported by the CPB, the sole state agency that is charged by the State Legislature and the Governor with representing the interests of the state's consumers before the PSC. It is also not supported by the

Public Utility Law Project ("PULP"), which represents the interests of residential customers and low-income customers in particular. Multiple Intervenors, a representative of industrial customers, supports the Agreement. However, it is noteworthy that one of the primary issues of concern to the CPB – a fixed price option for residential and small commercial customers – does not affect the customers represented by MI. In addition, the other main issue of concern to CPB – the Company's revenue requirement and overall rates for electric and gas delivery service – was not addressed in MI's direct testimony in this case.

Overall, no party representing solely the interests of mass market customers supports the fact that the Joint Proposal does not provide those customers the opportunity to purchase electricity and/or natural gas at a fixed price product from the utility. In addition, no party that testified on revenue requirement issues, other than the Company and DPS Staff, supports that aspect of the Joint Proposal. The ALJs and the PSC should give substantial weight to the fact that the Joint Proposal is opposed by the CPB and other representatives of mass market consumer interests, in determining whether adoption of the Joint Proposal is in the public interest.

PART II – THE CONTEXT FOR EVALUATING THE JOINT PROPOSAL

Q. Please summarize some of the important factors that should be considered by the ALJs and the Commission when evaluating the Joint Proposal.

A. Prices for electricity and natural gas commodity services have increased substantially in recent years and are expected to continue to be at high levels for several years. In particular, this past winter, Central Hudson's customers paid gas prices as much as double the price in the previous winter. (Response to CPB IR 78) Similarly, the Company's customers paid electricity prices in the fall of 2005 that were 87% higher than at the same time the previous year. (Id.) These high prices have a substantial impact on many consumers' budgets. Rather than mitigating this problem, the Joint Proposal would compound it by producing a series of large delivery rate increases for both electric and natural gas service, larger percentage increases than the Commission has considered for any large energy utility in New York State in more than a decade.

Consumers have expressed a great deal of concern about the large delivery rate increases that may result in this proceeding, through, among other things, their participation in the PSC's Public Statement Hearings. Elected representatives of consumers have also voiced their concern about the large delivery rate increases that are being considered. For these reasons, the Commission should give careful consideration to the bill increases that would result from their action in this proceeding.

Q. Please elaborate on your statement that energy commodity prices are expected to be at high levels for the next several years.

A. The commodity price of natural gas, as measured by futures prices on the NYMEX exchange as of April 26, 2006, exceeds $11.50 per Dth in each of the next two winters, and exceeds $11.00 per Dth in the winter of 2008 – 2009. That price is for delivery at the Henry Hub and does not include the cost of transportation to Central Hudson's service territory. The basis differential between Henry Hub and the NYC gate has approximated $2.50 per Dth in recent years. Assuming a similar basis of $2.50 per Dth over the next three years, the forecast price for natural gas at the NYC gate exceeds $14.00 per Dth in each of the next two winters, and exceeds $13.50 per Dth in the winter of 2008 – 2009. These prices would be the highest prices ever paid by Central Hudson customers, with the exception of portions of the winter of 2005 – 2006. High natural gas prices also lead to high electricity prices, everything else equal.

The Energy Information Administration ("EIA") has issued a similar forecast. In its Short-Term Energy Outlook issued April 2006, EIA forecasts a delivered price for the Mid-Atlantic region of $16.88 per Dth in the third quarter of 2006 and $16.83 per Dth in the third quarter of 2007. (EIA Annual Energy Outlook 2006, Table 8c, U.S. Regional Natural Gas Prices: Base Case) EIA's definition of the Mid-Atlantic region includes New York, Pennsylvania and New Jersey, and the prices for New York are generally higher than for the Mid-Atlantic region as a whole. EIA also forecasts residential electricity prices for the Mid-Atlantic region of 13.8 cents per Kwh in the third quarter of 2006 and 14.1 cents per Kwh in the third quarter of 2007. (Id., Table 10c, U.S. Regional Electricity Prices: Base Case)

Q. What do you recommend in these circumstances?

A. The PSC has recognized that action to alleviate the burden of unprecedented high commodity prices on consumers is appropriate. Additional action is required in view of the series of large delivery rate increases that would result from the Joint Proposal.

In these new circumstances, the ALJs and the Commission should ensure that policies and practices that may have been common in an era of stable, and much lower, energy commodity and delivery prices, are reassessed before they are automatically applied in this case. Regarding commodity issues, policies under which customers are denied the opportunity to purchase commodity from the utility at a fixed price even when such products are not available from ESCOs, and ESCOs are increasingly subsidized by utility customers, should be reconsidered. Similarly, regarding ratemaking issues, policies and practices sometimes accepted in the last decade should be reassessed, including those under which large increases in certain expense categories were approved, ratepayers provided funding for projects that were not necessary for safe and reliable service, and funds paid by ratepayers were retained by utilities for unspecified future purposes. This case provides an excellent opportunity for the ALJs and the Commission to review these issues from the new perspective of extremely high energy prices and potentially very large delivery price increases. We urge them to do so, by rejecting the “business as usual” approach on these issues reflected too often in the Joint Proposal and adopting the recommendations identified herein.

PART III – TOOLS TO HELP CONSUMERS MANAGE HIGH AND VOLATILE ENERGY PRICES

Q. Does the Joint Proposal provide consumers any new tools to help them manage high and volatile energy prices?

A. No. The Joint Proposal contains absolutely nothing new to address this important issue.

Q. Do you have any recommendations to help residential and small business consumers in an environment of high and volatile energy commodity prices?

A. Yes, we have two recommendations. First, we recommend that the Joint Proposal be revised to provide Central Hudson's residential and small commercial customers the opportunity to purchase electric and natural gas commodity service from the utility at a fixed price. This would help bridge the gap in Central Hudson's service territory between consumers' interest in fixed price products and the general absence of these products from ESCOs at just and reasonable prices.

Second, we recommend that the Joint Proposal be revised to require the Company to devote additional resources to the cost-effective delivery of information to consumers regarding the reasons for high energy prices and actions consumers can take to reduce and manage their energy bills.

FIXED PRICE COMMODITY OPTIONS

Q. Please summarize your position on fixed price commodity options.

A. In direct testimony in this proceeding, CPB Witness Mr. Niazi explained that consumers have shown a strong preference for fixed price energy products when they are available. He also demonstrated that only one ESCO in Central Hudson's service territory was offering electricity to residential customers at a fixed price while four ESCOs were offering them gas at a fixed price, but at a price that was substantially higher than what Central Hudson would have been able to offer. In these circumstances, he recommended that Central Hudson be required to offer fixed price electric and natural gas commodity service to residential customers on terms that assure that program costs are not subsidized by other customers. (Testimony of Mr. Niazi, November 21, 2005, pp. 32 – 35) That testimony was not rebutted by any party.

At the end of the heating season, the facts demonstrate that there is even a more compelling need for Central Hudson to offer a fixed price product for both electric and gas service. The gas supply charges paid by Central Hudson customers increased dramatically in 2005. Over the last three years, the arithmetic average of the gas supply charge paid by Central Hudson customers in the months of November – February was \$.74, \$.83 and \$1.42 per Ccf, respectively. (The November through February period is used for this illustration because of limitations in the data possessed by the CPB.) The highest monthly gas supply charges in each of the last three heating seasons were \$.8088 for March 2004, \$.8687 in November 2004 and \$1.7075 in November 2005, an increase of 96.6% in one year. (Response to CPB IR 79)

For electricity, the peak price paid by Central Hudson customers in 2003 was $.09099 in April, the highest price in 2004 occurred in February at $.08512 per kWh, and the 2005 price peak occurred in September, at $.12593. The arithmetic average of monthly prices in the last three calendar years was $.06726 per kWh for 2003, $.06193 per kWh for 2004, and $.08657 per kWh last year. (Id.) This average price increased 39.8% from 2004 to 2005.

In addition, the percentage of the Company's electric supply portfolio from sources other than fixed price contracts of 6 months or longer in duration, increased from 46% in 2004 to 63% in 2005. (Response to CPB IR 80) The Company did not provide projections of these percentages for electricity or natural gas, saying that the information is not available due to uncertainty as to factors including product availability, market prices, sales volumes and weather conditions. (Response to CPB IR 82) There is no reason to believe that Central Hudson will necessarily increase the percentage of its supply portfolio for which price risk is hedged.

Q. Didn't ESCOs satisfy mass market customers' need for fixed price products?

A. In general, customers were not satisfied by ESCO offerings for either gas or electric service. By the end of 2005, only 1,849 of Central Hudson's 63,594 residential gas customers (2.9%) were taking service from ESCOs, an increase of about 1,000 since the late summer. (Response to CPB IR 77) For electric, 2,089 residential customers, representing approximately 0.8% of Central Hudson's residential customers, were taking service from ESCOs at the end of

2005, approximately the same number as six months earlier, before the price spikes began. (2,087 residential customers had service from ESCOs in June 2005. Id.) Only one ESCO offered a fixed price product to residential customers for electric service at the beginning of this past heating season, and only one ESCO offered that product at the end of the heating season.

The data also demonstrate that even residential customers with a strong preference for fixed price products have not been satisfied with ESCO offers. 8,504 customers subscribed to the natural gas fixed price option from Central Hudson when that option was terminated on October 1, 2005. Six months later, 79% of those customers remained with the utility. (Response to PULP IR 3) Therefore, the vast majority of fixed price customers in Central Hudson's territory determined that they would rather pay the utility's variable price, even while those prices were spiking to unprecedented levels, than take service from an ESCO.

Q. Why is the availability of fixed price options important to mass market customers?

A. Customers should have the option of purchasing energy services at a stable, just and reasonable price, particularly customers on fixed incomes, since these products would facilitate household budgeting. For the same reason, fixed price products would be expected to be highly valued by low income customers. Evidence from NYSEG's service territory indicates that more than 75% of customers who affirmatively chose a commodity option, selected a fixed price option from the utility. (Case 05-E-1222, Exhibit 1, Information Request Response NYSEG ERPE0428)

A recent academic study confirms conventional wisdom that unanticipated home energy bill increases cause hardship on low income households. In an April 2005 paper published by the Center for the Study of Energy Markets, economists from the University of California, University of Virginia and National Bureau of Economic Research analyzed how household consumption responds to changes in home energy outlays. Using quarterly data from more than 50,000 households for 1990 through 2002, the study distinguishes changes in energy spending that are anticipated (winter in the northeast, for example), from those that are unanticipated, due to weather or price changes. The authors found that consumption spending does not change significantly as a result of anticipated changes in energy costs, even for low income households, since those households accumulate precautionary savings as a buffer, add to their credit card debt in these circumstances, or work additional hours. However, the authors concluded that consumers without substantial financial assets decrease spending on items such as food, personal care, and other household expenditures by 40 cents for each unanticipated dollar increase in their home energy bill, since they generally do not take precautionary steps that allow them to prepare for unanticipated changes in their energy bills. (Do Households Smooth Small Consumption Shocks? Evidence from Anticipated and Unanticipated Variation in Home Energy Costs, Julie Berry Cullen, Leora Friedberg, Catherine Wolfram, Center for the Study of Energy Markets, CSEM

WP 141, April 2005) The availability of reasonably priced fixed price products would provide low income customers a valuable tool to help avoid the need to substantially reduce their expenditures on food and other personal care items if the price of energy increases unexpectedly.

Q. Why doesn't Central Hudson offer fixed price products to its customers?

A. The Commission directed that Central Hudson terminate its fixed price option for gas service, concluding: "a fixed price supply option is a service that could and should be developed and offered by the competitive marketplace." (Case 05-G-0311, Petition of the Small Customer Marketer Coalition for a Declaratory Ruling Regarding the Fixed Price Option for all Customers with Annual Consumption Requirements Greater than 500 Ccf Operating Under Central Hudson Gas & Electric Corporation's Service Classification 1 and 2, Order Directing the Future Termination, Subject to Conditions, of a Fixed Price Offer, July 22, 2005 ("Order Directing Termination of Gas Fixed Price Option"), p. 8)

Based on PSC Orders, it appears that the Commission believes that retail competition will be inhibited if utilities offer fixed price products. For example, the PSC stated:

> The sooner customers experience pricing variations, the sooner competitive markets will provide alternatives, including fixed-price options and peak and off-peak pricings, possibly accompanied by interval metering. ESCOs, not the utilities, are expected to provide those options in the longer-term. (Case 00-M-0504, Proceeding on Motion of the Commission Regarding Provider of Last Resort Responsibilities, the Role of Utilities in Competitive Energy Markets and Fostering Development of Retail

> Competitive Opportunities, Statement of Policy on Further Steps Toward Competition in Retail Energy Markets, August 25, 2004 (Retail Competition Policy Statement), p. 31, footnote omitted)

Q. Did the PSC provide any other rationale for directing the termination of the gas fixed price option?

A. Yes. In that same Order, the PSC stated:

> The availability of ESCO alternatives addresses Central Hudson's concern that elimination of the utility-provided FPO will leave customers with no other options, and is evidence that the competitive marketplace should respond adequately to the elimination of the utility-provided FPO, as it has in other LDC service territories. (Order Directing Termination of Gas Fixed Price Offer, p. 8)

Similarly, the PSC said:

> The parties favoring that FPO option have failed to distinguish Central Hudson from the other utilities that do not offer the FPO, and have not justified allowing Central Hudson to offer that option when no other utility does. (Id., p. 9)

Q. Does the current retail market for mass market customers in Central Hudson's service territory support those conclusions?

A. No. As explained above and in the November 21, 2005 testimony of Mr. Niazi, only one ESCO offers fixed price electricity service to residential customers in Central Hudson's territory. ESCOs have generally not been able to meet mass market consumers' interest in fixed price products, even when the utility has not offered electricity at a fixed price for several years.

Similarly, only four ESCOs offered a fixed price natural gas product to residential customers at the beginning of the heating season when consumers needed it most, and their prices were higher than Central Hudson would have been expected to charge. Moreover, the vast majority of Central Hudson's fixed price customers chose to be subjected to market price volatility rather than take service from an ESCO.

These facts demonstrate that the competitive market has not responded adequately to the elimination of the utility-provided FPO and they distinguish Central Hudson from other utilities that do not offer an FPO.

Q. Does the Commission's policy on this matter offer any flexibility?

A. Yes. NYSEG and RG&E offer fixed price products to their customers. It should also be noted that the Commission has praised the benefits of "the flexible administrative course to restructuring the market that New York alone has taken." (Retail Competition Policy Statement, p. 1) Further, the Commission stated:

> Our long-term goal is for competitive suppliers to displace utilities from the commodity function (as well as any other functions that become workably competitive), but because of the differences in market maturation among service areas and customer classes, a one-size-fits-all approach to fostering migration is ill-advised. (Id., p. 25)

This approach has permitted utilities in New York state to pursue a variety of efforts to serve their customers and expand retail access, some of which have worked, and some of which have not. The ALJs and the Commission should recognize what the proponents of the Joint Proposal have not: that retail competition in Central Hudson's service territory is not meeting mass market customer needs for fixed price products, and that there is a compelling need at this time to provide mass market customers additional tools to help manage their energy bills, including the availability of fixed price products from the utility.

Q. Please summarize your position on the availability of fixed price commodity service from Central Hudson.

A. The facts demonstrate that ESCOs are not satisfactorily meeting customer needs for fixed price commodity service in Central Hudson's service territory, the market for those services is not competitive, at the same time that there is a compelling need to provide those services to mass market consumers. In these circumstances, we recommend that mass market consumers be provided the opportunity to purchase fixed price products from Central Hudson. We urge the ALJs and the Commission to recognize the market realities in Central Hudson's territory and modify the Joint Proposal so that Central Hudson offers fixed price products for both electric and natural gas service as soon as practical after a PSC Order in this proceeding.

OUTREACH AND EDUCATION REGARDING HIGH ENERGY PRICES

Q. Do you have any other recommendations regarding the impact of high commodity prices?

A. Yes. The CPB is concerned that under the Joint Proposal, Central Hudson would not devote adequate resources to outreach and education regarding high energy prices, such as the reasons for high prices and how consumers can obtain assistance. Under the Joint Proposal, Central Hudson would spend

$350,000 annually on a "Competition Education Campaign." (Joint Proposal, Section XVI (G)) The Joint Proposal, and the direct testimony of the Joint Proposal's Proponents, is completely silent, however, on outreach and education that the Company would conduct for purposes other than retail competition. In response to an information request, Central Hudson stated that it conducts such outreach, but it could not quantify the expected expenditures on those activities. (Response to CPB IR 103) Importantly, the Company did not identify plans to conduct any outreach on issues related to high commodity prices.

Q. Do you have an opinion on the absence of any mention in the Joint Proposal of outreach and education on any subject other than retail competition?

A. Yes. The Joint Proposal should be modified to ensure that the Company informs its customers about issues related to high energy prices. As explained in Point II, the prices of electricity and natural gas for the next several years are expected to continue to be high by historical standards. Consumers should be provided accurate and timely information on: (1) the cause of high energy prices, (2) actions they can take to manage their energy bills, and (3) how to obtain assistance in paying their bills. The CPB and the Department of Public Service played key roles in delivering that information to consumers this past winter, in part, as a result of the PSC augmenting its normal winter energy outreach and education efforts (see, for example, PSC Press Release, Commission Expands Winter Outreach and Education Efforts, September 21, 2005). However, there is no guarantee that the PSC will take such action again. Utilities can, and should, be instrumental in providing this important information to consumers.

Central Hudson's budget for outreach and education on these issues should be increased substantially. We recommend that the Joint Proposal be revised to redirect $175,000 that is currently planned for the "Competition education Campaign," for this purpose, including direct mail, bill inserts, information on the Company's web sites, and participating in public events. We discuss the numerous reasons for reducing the amount of spending on retail competition "education" programs below. This recommendation is fair to the Company, in that it does not affect its overall costs.

PART IV – REVENUE REQUIREMENT AND FINANCIAL ISSUES

Q. Please summarize your testimony regarding revenue requirement and financial issues.

A. The CPB recognizes that electricity and natural gas delivery rate increases are necessary and appropriate in this proceeding to help ensure that Central Hudson provides safe and reliable service. However, in certain important respects, the Joint Proposal does not balance the interests of the Company and its customers, and overstates the Company's revenue requirement. On several of those issues, we make recommendations that should not affect the Company's earnings. In particular, our proposals regarding construction expenditures and right of way maintenance expenditures would lead to more reasonable allowances in rates, while fully ensuring that the Company has the resources to provide safe and reliable service. Our proposal regarding the discount rate used in pension and OPEB expense projections also should not affect Company earnings over the term of the plan. Our recommendations regarding defined benefit pension plans, retail access, the automated meter reading program and outreach and education expenses would also not reduce the Company's earnings. Similarly, our proposals to return customer money being held by the Company for metering programs and the excess depreciation reserve surplus, would not affect Company earnings. The Joint Proposal could be easily modified to reflect all of these proposals, since they should not affect Company earnings, yet they would provide significant benefits to consumers. Only our proposals regarding storms expense, manufactured gas plant site remediation expense and return on equity would affect the Company's earnings. Those, and the CPB's other recommendations in this section, are necessary to ensure just and reasonable rates.

CAPITAL EXPENDITURES

Q. Please summarize your testimony regarding capital expenditures.

A. Central Hudson's revenue requirement under the Joint Proposal is based on projections of capital expenditures that far exceed actual capital spending by the Company in recent years. Over the last six years, the Company's total capital expenditures averaged $57.5 million. In 2005, capital spending increased by $2.6 million over the six-year average ($60.1 million minus $57.5 million), an increase of 4.5%. Under the Joint Proposal, however, capital expenditures would increase by $16.6 million (27.6%) in the 18-month period between calendar year 2005 and the 2006 rate year, July 2006 through June 2007, representing an annual percentage growth of 18.4%. The proposed increase over that 18-month interval is $10.6 million (24.6%) for the Company's electric operations, $4.9 million (47.3%) for its gas operations, and $1.1 million (16.5%) for projects that are shared by the electric and gas divisions, referred to as "common" projects. Capital expenditure increases of that magnitude are, on their face, excessive, since, among other things, the Company elected not to increase capital expenditures by this magnitude under its current rate plan when its earnings were healthy, and they do not appropriately reflect the importance of considering customer bill impacts in this proceeding.

Q. Please elaborate on the capital expenditures reflected in the Joint Proposal in relation to recent historical levels.

A. A comparison of historical capital expenditures and those underlying rates that would result from the Joint Proposal is shown in the following tables. In each of the following four tables, data are in millions of dollars, information through 2005 represents actual calendar year data, and information beginning 2006 represents rate year data. For example, data labeled "2006" is for the Rate Year beginning July 1, 2006. To facilitate comparison, the percentage increases in the following tables are calculated on an annual basis, thereby adjusting for the 18-month period between the end of calendar year 2005 and the rate year beginning July

2006. Data for gas capital expenditures include the safety enhancement program.

ELECTRIC CAPITAL EXPENDITURES

Year	Capital Spending	Annual % Increase
2002	48.261	
2003	39.001	-19.2%
2004	41.974	7.6%
2005	43.015	2.5%
2006	53.594	16.4%
2007	55.604	3.8%
2008	55.228	-0.7%

GAS CAPITAL EXPENDITURES

Year	Capital Spending	Annual % Increase
2002	10.902	
2003	9.672	-11.3%
2004	10.383	7.4%
2005	10.451	0.7%
2006	15.397	31.6%
2007	14.604	-5.2%
2008	13.244	-9.3%

COMMON CAPITAL EXPENDITURES

Year	Capital Spending	Annual % Increase
2002	7.488	
2003	3.976	-46.9%
2004	4.838	21.7%
2005	6.638	37.2%
2006	7.732	16.5%
2007	7.031	-9.1%
2008	6.930	-1.4%

TOTAL CAPITAL EXPENDITURES

Year	Capital Spending	Annual % Increase
2002	66.651	
2003	52.649	-21.0%
2004	57.195	8.6%
2005	60.104	5.1%
2006	76.723	18.4%
2007	77.239	0.7%
2008	75.402	-2.4%

The capital expenditure projections underlying the revenue requirement in the Joint Proposal exceed those recommended in initial testimony by any party, including the utility. Therefore, it is very unlikely that a litigated proceeding would have resulted in capital expenditures at such a high level.

Q. Please explain your concerns with the capital expenditure projections in the Joint Proposal.

A. Capital spending increases of this magnitude should not be approved by the Commission unless absolutely necessary. If such spending were necessary for the Company to provide safe and reliable service, the Company should have made a substantial portion of these expenditures during the term of its current rate plan, when its earnings exceeded the sharing thresholds for both electric and gas operations in 2003, 2004 and were projected to exceed those thresholds for 2005. (Response to Multiple Intervenors' IRs 7 – 8) At the time this testimony was written, the CPB did not have information regarding the Company's actual earnings for 2005.) However, the Company appears willing to increase capital spending by this magnitude only if it can obtain a large rate increase, thereby suggesting that the entire projected capital spending increase is not necessary to provide safe and reliable service. As further evidence that these projections are likely excessive, in the first three months of 2006, total capital expenditures were less than in the corresponding period of 2005. (Response to CPB IR 86)

In addition, the Joint Proposal does not properly recognize the risk that Central Hudson may not be able to complete all of the projects associated with the large increase in capital expenditures, in an efficient manner. The magnitude of the capital expenditure increases raises serious questions about whether the Company can efficiently and effectively complete such a large number of capital projects. As capital spending increases far beyond historical levels, projects may not be implemented in as cost effective a manner, thereby harming ratepayers.

The Joint Proposal contains provisions under which ratepayers would be protected if actual capital expenditures over the three-year term of the plan fall short of those on which delivery rates are based. The CPB was the only party to recommend such a measure in our pre-filed testimony (Testimony of Mr. Tariq N. Niazi, November 21, 2005, p. 23), and we strongly support its inclusion in the Joint Proposal. It does not, however, obviate the need for rates to be set based on a more reasonable projection of capital expenditures. Customers should not be required to pay rates that presume unreasonably large increases in capital expenditures.

Q. What do you recommend?

A. In a similar situation involving the electric operations of Consolidated Edison Company of New York Inc. ("Con Edison"), the CPB recommended that rates be established based on a forecast that was substantially lower than what the Company believed it would invest. We also recommended that the Company be permitted to defer, for potential future recovery, the revenue requirement impact of any capital expenditures beyond those reflected in rates, to help ensure that the Company implements all capital projects necessary for safe and reliable service. In addition, we recommended that Con Edison file annual comprehensive status reports on its capital expenditures, including the costs for each project, explanations of expenditure variations and justifications for new projects. Those reports would provide the parties and the Commission information to determine whether Con Edison's actual capital spending is reasonable, is being conducted in a cost effective manner, and whether the associated costs should be recovered. The Commission adopted a Joint Proposal reflecting those recommendations. (Case 04-E-0572, Order Adopting Three-Year Rate Plan, March 24, 2005, p. 35. The relevant provisions are contained in Appendix I, Joint Proposal, December 2, 2004, p. 11)

We recommend that the Joint Proposal in this proceeding be revised to be consistent with the approach taken in the Con Edison case. The rate increases that would result from the Joint Proposal should be revised to reflect much more reasonable projections of capital expenditures, based on recent historical spending with a reasonable allowance for growth. In particular, we recommend that rates for the first rate year be set based on the average of actual capital expenditures in the last four years, adjusted for twice the overall level of inflation since the end of 2005. In addition, Central Hudson should be permitted to defer for potential future recovery, the revenue requirement impact of capital expenditures beyond those reflected in rates. The Company should also be required to file annual comprehensive status reports on capital expenditures, including project costs, explanations of expenditure variations, and justifications for new projects, to help ensure that the parties and the Commission have information necessary to determine whether Central Hudson's actual capital spending is reasonable and is being conducted in a cost effective manner.

Modifying the Joint Proposal in this manner would be fair to the Company, in that it would ensure financial support for capital projects that are necessary for safe and reliable service. It would also be fair to ratepayers, in that the rate increase would be reduced to reflect projections of more reasonable increases in capital expenditures.

RIGHT OF WAY MAINTENANCE EXPENDITURES

Q. Please summarize your position regarding right of way maintenance expenditures.

A. The rate increases that would result from approval of the Joint Proposal are premised on extremely large increases in right of way ("ROW") maintenance expenses. We have three concerns about these projected spending increases: (1) there is substantial uncertainty regarding the level of ROW maintenance expenditures that should be reflected in rates, (2) ratepayers are not properly protected in the event that actual spending in this category is less than projected amounts, and (3) the Joint Proposal does not reflect any of the cost savings or other benefits that are expected to result from these projected increases in ROW maintenance expenses.

Q. Please elaborate on your statement that the ROW maintenance expenditure increases reflected in the Joint Proposal are extremely large.

A. Actual and projected transmission and distribution ROW maintenance expenditures are summarized in Exhibit___(CPB), Schedule 1. The Joint Proposal presumes that the Company will spend $9.991 million on ROW maintenance expense in Rate Year 1, $10.361 million in Rate Year 2 and $10.748 million in Rate Year 3. From 2000 though 2005, the Company's actual spending on these projects averaged $5.522 million, and in 2005, the Company spent $4.822 million on ROW maintenance. The Joint Proposal therefore reflects a projected increase of $4.469 million (81%) in spending on ROW maintenance activities in the first rate year beyond average spending in the last six years, and a projected increase of $5.168 million (107%) in annual spending beyond 2005 levels. Large projected increases occur in both distribution and transmission ROW maintenance expenditures, with annual distribution-related expenditures projected to increase $3.148 million (67%) and annual transmission-related expenditures projected to increase $1.320 million (152%), over their respective six-year historical averages.

The distribution ROW maintenance expense projections in the Joint Proposal are identical to those reflected in Central Hudson's initial testimony. The transmission ROW maintenance expense projections in the Joint Proposal for the first rate year are $200,000 (approximately 10%) less than reflected in the Company's initial testimony. In that testimony, the Company asserted that expense increases of this magnitude are required to address a heightened concern about the potential impact of improperly maintained ROWs on service outages, including requirements specified in the PSC's Order Requiring Enhanced Transmission Right-of-Way Management Practices By Electric Utilities, Case 04-E-0822, issued June 20, 2005. (Testimony of Company Witness Mr. Dubois, pp. 3-4) The Company also contends that it began to take action to ramp up its spending on transmission ROW maintenance in 2004, before that Commission Order.

Q. Please elaborate on your first concern, that there is substantial uncertainty regarding the level of ROW maintenance spending that should be reflected in rates.

A. As a threshold matter, the CPB recognizes that proper maintenance of Central Hudson's ROW helps ensure the reliability of the electric system. We support reasonable increases in ROW maintenance expenditures, if those expenditures are made appropriately. The question, however, is whether increases reflected in the Joint Proposal of 107% beyond 2005 levels are necessary and appropriate at this time.

The fact that Central Hudson's spending on both transmission and distribution ROW maintenance declined in 2005 from 2004 levels, also suggests that spending increases of the magnitude reflected in the Joint Proposal may not be warranted. Indeed, Central Hudson's total ROW maintenance spending in 2005, including the 6-month time period after the Commission's Order in Case 04-E-0822, reflected the lowest level of spending since 1999, if not earlier. (The CPB does not have data regarding the Company's spending on ROW maintenance before 2000.)

Proposed spending increases of the magnitude included in the Joint Proposal represent uncharted territory both for the Company and the Commission. The ALJs and the Commission should be concerned that expenditures of this magnitude may not be necessary, may not be spent in a cost effective manner, or may not be spent at all.

Q. Please elaborate on your second concern, that ratepayers are not properly protected in the event that actual spending in these categories is less than projected amounts.

A. Section X (F) of the Joint Proposal provides that any shortfall of actual electric transmission ROW maintenance expenditures over the term of the rate plan from the $6.723 million total expenditures that are projected, will be deferred for the benefit of ratepayers. However, no such ratepayer protection is provided for distribution ROW maintenance expenditures, which account for 78.4% of total ROW maintenance expenditures reflected in rates under the Joint Proposal.

Over the three-year term of the Joint Proposal, ratepayers would pay a total of $24.362 million allegedly for distribution ROW maintenance purposes, $9.777 million more than the Company spent in the last three calendar years, without any requirement that the Company actually spend those funds for that, or any, purpose.

In recognition of the extremely large increase in ROW maintenance expenditures requested by the Company and the substantial uncertainty concerning the amount of necessary ROW maintenance expenditures, CPB witness Mr. Larkin recommended in his initial testimony that ratepayers receive the benefit of any shortfall of such spending below the amount reflected in rates. (Testimony of CPB Witness Mr. Larkin, November 21, 2005, p. 38) The Joint Proposal contains this important ratepayer protection, but only for 21.6% of ROW maintenance expenditures.

Q. Do you have any recommendations to address your first two concerns about ROW maintenance expenditures?

A. Yes. We recommend two modifications of the Joint Proposal. First, the revenue requirement in the Joint Proposal should be revised to reflect projected ROW maintenance expenditures that are much closer to recent historical spending levels. In particular, we recommend that the projected ROW maintenance expenditures be reduced by $3 million in each year of the rate plan. Our recommendation would provide the Company funding to increase ROW maintenance expenditures by 27% over average annual spending in the six years 2000 – 2005 and by 45% over actual spending in 2005.

We also recommend that the Company be permitted to defer any ROW maintenance expenditures beyond the amount reflected in rates. Requests to recover such deferrals would be accompanied by comprehensive reports explaining why such expenditures were necessary. Such an approach is fair to the Company, in that it provides substantial additional funds to maintain its ROW, as well as the opportunity to fully recover any ROW expenditures beyond the rate allowance that are necessary and conducted in a cost effective manner. It is also fair to ratepayers, since it would provide substantial additional funding to enhance reliability, and give proper consideration to the need to avoid unnecessary rate increases.

Second, we recommend that the Joint Proposal be modified to include a ratepayer protection should actual distribution ROW maintenance expenditures fall short of the rate allowance. This measure is necessary because of the magnitude of the projected spending, even under the CPB's proposal, and the high degree of uncertainty concerning the appropriate level of such spending, and is fair to the Company and ratepayers.

Q. Please explain your third concern, that the Joint Proposal does not reflect any of the cost savings or other benefits that are expected to result from these projected increases in ROW maintenance expenses.

A. The Company states that increases in ROW maintenance expenses are needed to enhance system reliability. Although the revenue requirement in the Joint Proposal is based on substantial additional expenditures, it completely ignores the expected cost savings and additional revenue that would result from a reduction in the number and duration of outages.

As explained by Central Hudson witness Mr. Dubois, the Company expects to conduct ROW maintenance work to, among other things, remove "danger trees," which are defined by the PSC as

> any tree rooted outside of a ROW that due to its proximity and physical condition (i.e., mortality, lean, decay, cavities, cracks, weak branching, root lifting, or other instability), poses a particular danger to a conductor or other key component of a transmission facility. (Testimony of Mr. Dubois, p. 6)

Mr. Dubois also testified that "[t]he distribution danger tree program targets the removal of damaged trees typically outside the normal zone of trimming which are posing an imminent threat to our electrical facilities." (Id., p. 10)

Central Hudson also explained that an increase in ROW maintenance spending is required to comply with the PSC's June 20, 2005 Order in Case 04-E-0822. That Order states: "While it may not be possible to eliminate tree-caused outages completely, the utilities should continue to strive toward that goal." (Order, p. 13) It also asserts that "[t]he Commission fully expects no outages from vegetation growing inside the ROW limits." (Id., p. 16)

The additional revenue and reduction in maintenance and restoration expenses that would be expected to result from the substantial increases in ROW maintenance expense are not reflected in the revenue requirement projections in the Joint Proposal. This mismatch of costs and benefits is inconsistent with proper ratemaking principles and causes the revenue requirement in the Joint Proposal to be overstated.

Q. Do you have any recommendations to address this concern?

A. Yes. Our recommendation is addressed in the following section.

STORMS EXPENSE

Q. Please explain your recommendation regarding storms expense.

A. Rates under the Joint Proposal are based on projected storms expense of $5.197 million, $5.311 million and $5.428 million for the three rate years, respectively. These projections were derived by use of the four-year average of historical expenditures adjusted to calendar year 2005 data, and then inflated. (Response to CPB IR 96) Storm expenditures averaged $4.785 million over the last four years. Over the last six years, 2000 – 2005, Central Hudson's storms expense averaged $4.513 million. Storm expense totaled $2.177 million in 2004 and $4.221 million in 2005. These data are shown in Exhibit___(CPB), Schedule 2.

As explained previously, the Company testified that it began to substantially increase its ROW maintenance expenditures in 2004. As shown in Exhibit___(CPB), Schedule 1, total ROW maintenance expenditures increased 37% in 2004 over 2003 levels. Since that ramp up began, storms expense has averaged $3.199 million per year. It is reasonable to expect, all else equal, that storms expense will continue to decline as a result of further increases in ROW maintenance expenditures.

Accordingly, we recommend that the Joint Proposal be revised to reduce projected storms expense to the average of such expenditures beginning 2004. In his November 21, 2005 testimony, Mr. Larkin recommended that storms expense be set at the level experienced in the 12-month period of the test year April 2004 – March 2005. Our recommendation would also include actual results since March 2005, and would reduce storms expense by $2.0 million from the level in the Joint Proposal. The adjustment we recommend here would be fair to the Company, since it reflects recent historical expenditures and essentially conservatively assumes that additional ROW maintenance expenditures will not further reduce storms expense.

MANUFACTURED GAS SITE REMEDIATION

Q. Please summarize your position on the treatment of Manufactured Gas Site Remediation Costs under the Joint Proposal.

A. Central Hudson appears to be embarking on an extensive manufactured gas plant ("MGP") site investigation and remediation program. The Company should be responsible for some portion of the expenses associated with this program, because of the magnitude of these expenses, the need to constrain rates, and the importance of providing the Company an incentive to seek recovery of these expenditures from other responsible parties. However, under the Joint Proposal, ratepayers would generally be responsible for 100% of these costs.[1] The Joint Proposal should be modified to require the Company to absorb some portion of these costs.

In the test year, the Company spent $533,900 on these projects. (Testimony of Central Hudson witness Mr. Jeffrey A. Clock, Exhibit___(JACL-1), Schedule A) As of the date of its initial filing, the Company expected to spend $6.516 million, $9.820 million and $8.310 million in each of the three rate years of the Joint Proposal, respectively. These costs reflect anticipated activity at 8 sites. (Testimony of Mr. Clock, p. 2) Additional costs may be incurred at other former MGPs within the Company's service territory, including at least 5 sites identified in the Company's direct testimony.

The Joint Proposal includes a rate allowance for MGP Site Investigation and Remediation Costs of $1.650 million in each of Rate Years 2 and 3, $1.4 million for electric and $0.250 million for gas operations. It also would authorize the Company to defer for future recovery, the difference between the actual costs for MGP Site Investigation and Remediation and these rate allowances, and permit the Company to earn a return on those balances at the pretax authorized rate of return. (Joint Proposal, Section X (I))

As explained in more detail by CPB Witness Larkin in his November 21, 2005 testimony, charging current ratepayers for MGP costs would be akin to retroactive ratemaking. Instead, risks associated with environmental problems should be born by shareholders. (Larkin Testimony, pp. 24 – 34)

[1] Pursuant to Section IX (B)(6) of the Joint Proposal, if the Company's return on equity exceeds 11.0%, ratepayers may be responsible for 50% of deferred MGP site investigation and remediation costs.

In similar circumstances, the Commission required the utility to share 20% of MGP site investigation and remediation costs. The Commission stated:

> Based on the facts and circumstances presented here, however, including Niagara Mohawk's financial exposure and the need to constrain rates, we are requiring 20% utility sharing of rate year 1995 SIR costs. In the absence of price caps, sharing of SIR costs provides an additional incentive for Niagara Mohawk to contain SIR costs and for it to aggressively seek partial recovery of such expenditures from other responsible parties and/or insurance companies. (Cases 94-E-0098, 94-E-0099, et al, Opinion No. 95-21, Opinion and Order Concerning Revenue Requirement and Rate Design, December 29, 1995, p.23)

Here, as in that case, the utility is embarking on a program that is likely to involve many projects and significant costs, there is a compelling need to constrain rates and the Company should have an incentive to minimize these costs. For these reasons, in these circumstances, the CPB conservatively recommends that the Joint Proposal be modified to require the Company to absorb 10% of MGP site investigation and remediation costs that it incurs.

It is noteworthy that in previous PSC Orders regarding the accounting for Central Hudson's MGP costs, the PSC stated that although deferral of these costs is authorized, recovery is not assured, "since these costs remain subject to staff's final review, including possible consideration of an appropriate incentive mechanism to ensure proper cost controls." (Case 95-M-0874, Petition of Central Hudson Gas & Electric Corporation for Permission to Defer all Costs, Excluding Company Labor, Related to an Environmental Site Investigation and Remedial Actions at and Near the Site of its Former Coal Gas Manufacturing

Facility Near the City of Newburgh, Approved as Recommended and so Ordered by the Commission, Memorandum, May 12, 1997, p. 4) However, the Joint Proposal omits such an incentive.

The Joint Proposal also appears to modify existing PSC policy regarding deferred MGP costs in a manner that advantages the Company at the expense of ratepayers. By Order dated October 3, 2002 in Case 01-G-1821, the PSC addressed the Company's request to defer MGP costs incurred in 2002 and future years. That Order identified several tests that would be applied to determine whether the Company could recover such deferred costs. The Joint Proposal however, appears to supersede that Order, thereby eliminating those conditions upon the recovery of deferred MGP costs.

The Joint Proposal also specifies that deferred MGP balances will accrue carrying charges at the pre-tax authorized rate of return, or 10.01%. Current PSC policy applicable to Central Hudson allows deferral of MGP costs at a rate equal to the unadjusted customer deposit rate (October 3, 2002 Order in Case 01-G-1821), which is 4.75% for calendar year 2006. (Letter from Charles M. Dickson, Department of Public Service, to New York State Utilities, October 27, 2005)

Q. Please summarize your testimony regarding MGP site remediation costs.

A. The Joint Proposal should be revised so that the Company absorbs 10% of such costs. To accomplish this, the MGP-related costs embedded in the revenue requirement calculations should be reduced by 10% and the deferral and recovery provisions should be modified accordingly.

PENSION AND OPEB DISCOUNT RATE

Q. What interest rate is used in the Joint Proposal to determine the present value of accumulated pension and other post employment benefits ("OPEBs")?

A. The discount rate is the rate used to estimate the present value of an obligation that does not have to be paid until a future year. In this situation, the future obligations are pension and OPEB benefits the Company expects to have to pay. By reducing the assumed discount rate, the present value of the pension and OPEB obligations increases, thereby generating an increase in expense (or a reduction in income). Rates under the Joint Proposal are based on a discount rate for pension and OPEB obligations of 5.50%. (Response to CPB to DPS IR 6)

Q. Is there any guidance within generally accepted accounting principles regarding what discount rate should be used in the pension and OPEB expense calculations?

A. Statement of Financial Accounting Standard ("FAS") 87 addresses employers' accounting for pensions. With respect to the assumptions used in determining pension costs, FAS 87, under paragraph 44, states:

> Assumed discount rates should reflect the rates at which the pension benefits could be effectively settled. It is appropriate in estimating those rates to look at available information about rates implicit in

> current prices of annuity contracts that could be used to effect settlement of the obligation (including information about available annuity rates currently published by the Pension Benefit Guaranty Corporation). In making those estimates, employers may also look to rates of return on high-quality fixed-income investments currently available and expected to be available during the period to maturity of the pension benefits. Assumed discount rates are used in measurements of the projected, accumulated, and vested benefit obligations and the service and interest cost components of net periodic pension cost.

It has been our experience that utilities look to publicly available corporate bond yields, such as the Moody's Corporate Aa Bond rate and the Merrill Lynch 15+ Year High Grade Corporate Bond rate. While the discount rates chosen will not equal exactly the corporate bond yields reviewed, typically they are within a range close to such rates.

Q. Do you agree that a discount rate of 5.50% should be used in projecting pension and OPEB expense for Rate Years 1 – 3 at this time?

A. No. The most recent Moody's Aa Corporate Bond index available to the CPB, as of March 10, 2006, was 5.68%. More recent data is not available to us since this index is not a published index and is, therefore, only available on a current basis to subscribers. In addition, interest rates have been increasing and may increase further in the future. As demonstrated in a concurrent case before the PSC, utilities may use a discount rate in projecting pension and OPEB expense that differs somewhat from the most recent Moody's Aa Corporate Bond Index. For example, NYSEG adopted a discount rate that was nine basis points higher than the most recent Corporate Bond Index. (Case 05-E-1222, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of New York State Electric & Gas Corporation for Electric Service, Initial Brief of the New York State CPB, April 26, 2006, p 13, citing SM 3889 – 90 in that proceeding) For these reasons, the 5.50% discount rate used to establish rates under the Joint Proposal overstates likely pension and OPEB expense, and should be increased to 5.75%. The CPB does not have the information to calculate the revenue requirement impact of this proposal, although we understand that it would reduce overall revenue requirement by more than $1 million per year. Our recommendation is fair to the Company, in that Commission policy ensures that pension and OPEB expenses that are higher than reflected in rates will be recovered.

RETURN ON EQUITY

Q. What cost of equity underlies the rates in the Joint Proposal?

A. Rates under the Joint Proposal are premised on a return on equity of 9.6%. (Joint Proposal, Appendix H, Schedule 1) CPB witness Mr. Niazi testified on November 21, 2005 that Central Hudson's cost of equity is 8.71%. (Testimony of Mr. Niazi, pp. 5 – 18) DPS Staff testified at that same time that the Company's cost of equity is 8.70%. (Testimony of DPS Staff Witness Ms. Audrey L. Capers, pp. 8 – 30)

Q. What is the relationship between the 9.6% cost of equity in the Joint Proposal and the 8.7% cost of equity recommended by the CPB and DPS Staff in their initial testimony?

A. According to DPS Staff, the 9.6% cost of equity was developed using the 8.7% estimate as a starting point, and making several adjustments. (Response to CPB to DPS Staff IR 9) First, the 8.7% ROE is increased by 39 basis points based on three factors: i) CH Energy Group was removed from the proxy group; ii) the starting point for the number of shares outstanding for the calculation of the stock valuation adjustment was changed from 2006 to 2005; and iii) the weighting of the Traditional and Zero-Beta Capital Asset Pricing Model ("CAPM") was changed from 75/25 to 50/50. Second, the cost of equity estimate was increased by an additional 14 basis points to account for interest rate changes since the November 21, 2005 testimony was filed. Third, 38 basis points was added for a three year stay-out premium.

Q. Do you agree with these adjustments?

A. We agree with some, but not all, of these adjustments. First, we do not agree with two items in the first set of changes that increase the equity estimate by 39 basis points. CH Energy Group was removed from the proxy group presumably since Central Hudson is the utility whose return is being estimated in this proceeding. Parties typically do not exclude the utility whose return is being estimated from their proxy group. Further, that adjustment was not made in the Generic Finance case. In the current proceeding, Central Hudson and DPS Staff included CH Energy Group in its proxy group for its equity analysis. Similarly, in the most recent testimony filed by DPS Staff for an energy utility, DPS Staff included Consolidated Edison in its proxy group in the on-going Orange and Rockland Utilities, Inc. proceeding (Case 05-G-1494, testimony filed March 30, 2006) even though Orange and Rockland is a subsidiary of Consolidated Edison.

With regard to using 2005 instead of 2006 as the starting point for the number of shares outstanding, we have no objection. CPB used 2005 as the staring point and that is consistent with the DCF methodology approved in the Generic Finance case.

We disagree with changing the weighting between the Traditional and Zero-Beta CAPM methods from 75/25 to 50/50. In the Generic Finance case the ALJs approved the 75/25 weighting and that weighting has been used in most cases approved by the Commission. Central Hudson also used a 75/25 weighting in its pre-filed testimony.

We have no objection to the 14 basis point adjustment to account for interest rate changes since the direct testimony was filed.

Q. What is your position regarding the 38 basis point adder for a three-year stay-out premium?

A. We do not object to the calculation of that adjustment, however, we believe that it should not be made in this case. The reason for this adjustment is to recognize the additional risk that the Company is taking in agreeing to a multi-year settlement as compared to a one-year rate case. However, the revenue requirement calculations under the Joint Proposal are essentially equivalent to three one-year rate cases. In particular, both the electric and gas revenue requirements reflect projections of higher labor costs, other operations and maintenance expenses, taxes and other expenses in each rate year. For example, the electric rates are based on an additional $6.121 million of revenue requirement in Rate Year 2, and an additional $5.529 million of revenue requirement in Rate Year 3. (Joint Proposal, Appendix A, Schedule 2) The Company is not agreeing to freeze delivery rates for the term of the multi-year plan, and is therefore not absorbing the risk that its return may decline after the first year. Instead, ratepayers are being asked to commit now, to fund projected cost increases in each year of the multi-year plan, whether or not those cost increases materialize. The 38 basis point stayout premium therefore provides no value to ratepayers in these circumstances.

Q. Please summarize your recommendations regarding the rate of return on equity under the Joint Proposal.

A. Based on the methodologies developed in the Generic Finance Proceeding and adopted in numerous Commission decisions, the return on equity included in the Joint Proposal is excessive. It should be reduced to remove the effect of removing CH Energy Group from the proxy group, changing the weighting of the Traditional and Zero-Beta CAPM from 75/25 to 50/50, and the 38 basis point stayout premium.

DEFINED BENEFIT PENSIONS FOR MANAGEMENT AND EXECUTIVE EMPLOYEES

Q. What is the relevance of Central Hudson's pension plan for its management and executive employees in evaluating the Joint Proposal?

A. The main factor driving Central Hudson's rate increase requests for both electric and gas operations was pension and OPEB expense. Central Hudson witness Mr. Arthur R. Upright testified that pension and OPEB costs including the effects of a related rate base credit reversal, account for 59% of the electric increase originally proposed by the Company and about two-thirds of its originally proposed electric rate increase. (Testimony of Mr. Upright, pp. 5 – 6) However, the Joint Proposal does nothing to prevent such a situation from recurring.

Central Hudson offers a defined benefit pension plan to all of its management and executive employees, subject to certain eligibility requirements as defined in the plan. (Response to CPB IR 90) Defined benefit pension plans are generally more expensive for companies to provide than other retirement plans, such as defined contribution plans.

Q. Have other companies begun to transition away from defined benefit pension plans for their management and executive employees?

A. Yes. In recognition of the fact that these plans are generally more expensive to provide than other retirement programs, many employers have replaced their defined benefit plan with other plans, or have begun the transition away from defined benefit plans. For example, IBM, which is Central Hudson's largest customer and one of the leading employers in the Company's service territory, announced that in January 2005 that will “freeze” its defined benefit pension plan, and expects to save billions of dollars as a result. Other large corporations including Verizon, General Motors and Unisys took similar action in recent months. In addition, other New York State utilities, including Consolidated Edison Company of New York, National Grid, New York State Electric and Gas Corporation, Orange & Rockland Utilities Inc., and Rochester Gas and Electric Corporation, have begun to transition away from defined benefit pension plans for their management and executive employees. It is also generally expected that more firms will be moving away from defined benefit pension plans in the near future. Movement away from defined benefit plans shifts responsibility and risk from the employer, and its customers, for managing the pension assets of employees. Such a change also provides employees with greater flexibility, control and portability of their pension benefits.

Despite this trend, rates established under the Joint Proposal assume that Central Hudson will not begin the transition to a less expensive pension plan for the duration of the rate plan. If the Company follows other large employers in its service territory and other New York State utilities in transitioning away from defined benefit pension plans, it would retain all associated savings under the Joint Proposal.

Q. What do you recommend in these circumstances?

A. We recommend that the Commission modify the Joint Proposal to provide ratepayers two-thirds of any net savings that result from transitioning away from the current defined benefit pension plan for Central Hudson's management and executive employees over the term of the rate plan.

This recommendation is consistent with the outcome in competitive markets. In such markets, firms that adopt innovative cost reductions or productivity improvements can retain the vast majority of financial benefits of those innovations until they are generally matched by other firms in the industry. At that point, competition among firms causes the market price to decline to reflect the cost reductions, and consumers become the beneficiaries of those innovations. The last firms to adopt those cost saving innovations retain only a small portion of the cost savings.

Our recommendation is fair to the Company, in that it would provide the Company a financial incentive to pursue cost reductions. It is also fair to ratepayers, since they would share in these cost savings and help reduce the likelihood that Central Hudson will request another large rate increase based primarily on the need to fund employee pensions.

RATEPAYER FUNDS RESERVED FOR METERING

Q. How does the Joint Proposal address funds currently reserved for metering initiatives?

A. The Joint Proposal specifies that funds that are currently reserved for metering initiatives will be maintained and reserved for that purpose. (Joint Proposal, Section X(C)(2)(c)) The Company projects that approximately $466,000 that had been reserved for this purpose will be unspent as of the end of the current rate plan. (Response to CPB IR 73)

Q. Please provide a brief overview of the history of this metering initiative.

A. As part of the rate plan for Central Hudson Gas & Electric Corporation in Cases 00-E1273 and 00-G-1274, uses for the Benefit Fund, which was created as the repository for the net proceeds from the utility's sale of its generating facilities, were identified. The PSC found that the Benefit Fund could be used for competitive metering purposes. (Cases 00-E-1273 and 00-G-1274, Order Establishing Rates, October 25, 2001) Regarding metering-related initiatives, the Commission stated:

> As one such initiative which we are prepared to designate now, the company and parties should explore the development of advanced pricing and metering offerings for a broader range of its customers, including approaches that would better enable customers to respond optimally to improved price signals. Properly implemented, this initiative could result in multiple benefits, including lower customer bills; reduced wholesale market prices due to improved demand responsiveness; and reduced costs, to the utility and other load-serving entities, of recording and transmitting customer usage and billing data. In particular, the company and parties should consider: the potential benefits resulting from enhanced pricing offerings for a broad range of customers beyond those now eligible for the company's existing real-time pricing tariffs; appropriate methods for providing customers access to the education and control technologies that may be necessary to adjust their usage in response to actual market prices; and appropriate sources of funding for enhanced metering and meter reading technologies, ideally through competitive means, to effectively record and transmit usage and billing data among

> customers, the utility, and competitive load-serving entities. (October 25, 2001 Order, p. 8-9)

Q. Did that Commission Order specify an amount of money be spent in this endeavor?

A. No. The Rate Plan Order provided for a collaborative process to commence around January 15, 2002, in which proposals to make disbursements from the Benefit Fund would be addressed. It was expected that the collaborative would yield specific proposals for the enhanced metering initiative.

Q. What happened next?

A. After the collaborative process on Benefit Fund spending, Central Hudson submitted a report on the outcome of those efforts. The utility acknowledged that a metering program would draw additional amounts from the Benefit Fund, and voiced its intention to file a metering proposal "in the near future". In an October 3, 2002 Order, the Commission stated that Central Hudson had reported that enhanced metering proposals had been discussed in the collaborative, but that the development of a metering program "requires significant additional effort, which has been ongoing." (Cases 00-E-1273 and 00-G-1274, Order Authorizing Benefit Fund Disbursements, October 3, 2002, p. 4)

Q. When was metering issue addressed again by the parties?

A. No progress was made on the competitive metering initiative for more than 18 months. The issue was addressed again by the parties in 2004 as part of several modifications to the Company's rate plan. A Joint Proposal, which the CPB opposed, contemplated earmarking $500,000 for competitive metering purposes.

> Up to $500,000 from the Benefit Fund will be reserved for potential use in encouraging appropriate installations of advanced metering technologies and implementation of related pricing strategies intended to facilitate development of competitive markets. Staff will present a proposal for implementing this competitive metering initiative after consultation with Central Hudson, other parties to these proceedings, and other potentially interested parties. (Cases 00-E-1273 and Case 00-G-1274, Order Modifying Rate Plan, June 14, 2004, Attachment, Joint Proposal for Rate Plan Modification, March 29, 2004, pp.19-20)

Q. Did the CPB take a position on the metering provisions of that Joint Proposal?

A. Yes. The CPB recommended that money earmarked for metering be returned to ratepayers for the purpose of mitigating bill increases. The CPB pointed out that in the two and one-half years since the original order was issued, no reasonable metering proposal had been advanced and that ratepayers' money would be better used to help mitigate bill increases. (Cases 00-E-1273 and 00-G-1274, Comments of the New York State Consumer Protection Board Regarding Joint Proposal, April 26, 2004, pp. 7 – 9) At that time, CPB was joined by MI in opposing the continued retention of ratepayer funds for this purpose.

Q. Did the Commission agree with the CPB?

A. No. The Commission ordered that those ratepayer funds be retained again for metering related initiatives and again offered the promise that reasonable proposals for use of that money would be forthcoming. The Commission stated

> the funding commitment in the Joint Proposal, by clarifying the amount of resources available, is likely to result in specific proposals for a cost-effective metering program. And, here again, it would be shortsighted to use the $500,000 for refunds or rate base offsets when it represents an opportunity to achieve greater customer benefits through enhanced competition. (Cases 00-E-1273 and 00-G-1274, Order Modifying Rate Plan, June 14, 2004, p. 10)

Q. Were such proposals forthcoming as the Commission hoped?

A. No. However, as part of the Company's Retail Access Plan, Central Hudson included the following provision:

> Metering Initiative - the Company is working with Staff to offer web-based access to hourly electric consumption and pricing information for all customers on SC 3 and SC 13. If funding is available, this initiative may be expanded to offer the service to some smaller commercial customers on SC2. The goal is to have this software in place by April 1, 2005 to coincide with the effective date for the hourly electric pricing tariffs. (Cases 05-M-0504, Central Retail Access Plan, December 15, 2004, p.4)

Parties such as the CPB were not provided an opportunity to comment on that proposed use of funds.

Q. Did the Commission approve this use of metering funds?

A. Yes. In a June 1, 2005 Order, the Commission stated:

> Staff and the Company worked in collaboration to research appropriate metering enhancement tools. Central Hudson determined that obtaining metering software to track and monitor energy usage would be an efficient and productive tool for the S.C. 3 and S.C. 13 electric customers that are moving to hourly pricing. The company, with Staff input, developed and issued a Request for Proposals (RFP) to solicit bids for software intended to provide these hourly pricing

> customers with the ability to study and manage their energy usage, as well as assist in their solicitation of competitive offers from ESCOs. (Case 05-M-0332, In the Matter of Central Hudson Gas & Electric Corporation's Plan to Foster the Development of Retail Energy Markets, Order Accepting Retail Access Plan, Modifying Rate Plan, and Establishing Further Procedures, June 1, 2005, p 9)

The Commission admitted that "this approach differs somewhat from the metering initiative approach first envisioned in 2001." (Id., p. 10, footnote 11) The installation of the metering software to help Central Hudson's largest customers monitor their energy use was planned for May 2005.

Q. Returning to the metering provision of the Joint Proposal, please explain your position on that issue.

A. Approximately $500,000 of ratepayer money has been held by the Company and designated for use for competitive metering since 2001. For approximately four years, no legitimate use of that money had been found. Then in mid-2005, the PSC broadened the potential uses of those funds to include spending on software to assist Central Hudson's large customers, and still $466,000 is projected to remain at the end of the current rate plan. It is long past time to return that ratepayer money to ratepayers.

Permitting the Company to retain that long-held ratepayer money instead of using to mitigate the large rate increases that are expected in this proceeding, is untenable. The Joint Proposal should be modified so that this ratepayer money is finally put to good use.

AUTOMATED METER READING PILOT PROGRAM

Q. Please summarize the Automated Meter Reading pilot program included in the Joint Proposal.

A. Under the Joint Proposal, Central Hudson would develop an Automated Meter Reading ("AMR") pilot proposal including 5000 meters and using a fixed network meter technology. (Joint Proposal, Section XV (B)) The cost of that program would not exceed $1.5 million and would be funded from the unused competitive metering funds held in the Benefit Fund, or the excess depreciation reserve. No party proposed such a program in their initial testimony in this case.

Q. What is your position on the AMR pilot program?

A. That pilot program should not be implemented at this time, due to the size of the delivery rate increases that would result from the Joint Proposal and high energy costs. That program is not necessary to provide safe and reliable service. In addition, no cost benefit analysis has been conducted. Further, like many other provisions of the Joint Proposal, this provision would require ratepayers to pay the cost of the program and permit the Company to retain the resulting cost savings. The program may also be inconsistent with the Commission's apparent competitive metering agenda. A similar AMP pilot program is being conducted by at least one other utility in New York State. The results of that pilot could be shared with all New York State utilities.

In these circumstances, we recommend that the Joint Proposal be modified to remove the AMR pilot program. This would make an additional $1.5 million available to mitigate the rate increases in this proceeding.

REVERSAL OF RELIABILITY PENALTY

Q. Please summarize the Joint Proposal's provision regarding reliability penalties applicable to the Company in 2005.

A. Central Hudson's current rate plan contains an electric reliability performance mechanism that established performance targets for the frequency and duration of electric service outages, as measured by the System Average Interruption Frequency Index, or SAIFI, and the Customer Average Interruption Duration Index, or CAIDI, respectively. If the Company fails to meet a target, it is required to credit a rate adjustment for the benefit of ratepayers. By Order in Case 00-E-1273, the Commission found that Central Hudson

> failed to meet the maximum target for SAIFI frequency reliability in 2002, and it has incurred the 12.5 basis point rate adjustment that is applicable. Moreover, the company failed to meet the maximum targets for both SAIFI frequency and CAIDI duration reliability in 2004, and it has incurred the rate adjustment of 25 basis points that is applicable. A rate adjustment of 37.5 basis points is due ratepayers as a result. To effectuate that rate adjustment, the company shall book a deferred credit for future disposition to ratepayers. (Case 00-E-1273, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Central Hudson Gas & Electric Corporation for Electric Service, Electric Reliability Performance, Order Denying Petitions and Establishing Rate Adjustments, September 30, 2005, pp 18 – 19)

In addition, the Company has apparently not met these maximum targets for 2005, and has already recorded a deferred ratepayer credit of $758,000. (Response to CPB IR 105)

Under the Joint Proposal the Company would be permitted to reverse this ratepayer credit. (Joint Proposal, Section XIV, (C))

Q. What is your position on this provision of the Joint Proposal?

A. The Joint Proposal would deny ratepayers this financial benefit by essentially ignoring the fact that the Company did not meet the electric reliability targets in its current rate plan. It is virtually inconceivable that such a result, in which key provisions of an approved rate plan are essentially ignored, would have occurred in a litigated proceeding. This provision also may reduce incentives for any utility to comply with regulatory standards and targets in the future.

RETAIL ACCESS ISSUES

Q. Please summarize the retail access provisions of the Joint Proposal.

A. Under the Joint Proposal, several measures considered by some to facilitate competition would continue and be enhanced, including a Market Match Program, Market Expo, Energy Fairs, ESCO Satisfaction Mechanism, ESCO Ombudsman, Competition Awareness and Understanding Survey, the so-called Competition Education Campaign and the ESCO Referral Program. (Joint Proposal, Section XVI)

The Joint Proposal also contains several retail-access-related provisions that are detrimental to consumers. It would establish a two-tiered Merchant Function Charge (MFC”), apparently based on the perception that some ESCOs prefer this approach, (Joint Proposal, Section VI (C)), even though such charges are likely to be more confusing to consumers than a single MFC. The Joint Proposal would also further delay the commencement of cost-based backout credits or MFCs until July 1, 2007 (Joint Proposal, Section VI (A)), thereby increasing costs to be borne by ratepayers. This is apparently also being done to benefit ESCOs, despite the fact that the PSC’s stated policy since 2001 has been to move toward cost-based backout credits and DPS Staff’s direct testimony called for unbundling to be conducted in a cost based manner and be completed on January 1, 2007. (November 21, 2005 testimony of DPS Staff Unbundling Panel, pp. 6 – 7) The Joint Proposal would also apparently modify existing Commission Orders applicable to Central Hudson, by providing that incremental costs of the ESCO Referral Program incurred before the effective date of the Joint Proposal, be deferred for future recovery from ratepayers. (Joint Proposal, Section XVI (H))

Q. What is the impact of these provisions on rate levels under the Joint Proposal?

A. Curiously, the Joint Proposal does not quantify the costs of these programs, with the exception of the “Competition Education Campaign,” which we address in the following section. The CPB asked Central Hudson for that information, but was told “[t]he Company has not developed a forecast of the expected expenditures outlined in the Retail Access section of the Joint Proposal." (Response to CPB IR 92) That response is curious and out-of-character, since well-managed Companies typically seek to understand the cost of obligations to which they agree.

The CPB also requested an estimate of the dollar amount of backout credits that would be recovered from ratepayers under the Joint Proposal, to help determine the impact on consumers of further delaying the commencement of cost-based backout credits. DPS Staff responded that a forecast of the cost of those backout credits "was not made." (Response to CPB to DPS Staff IR 7) That response is also curious and out-of-character.

Overall, the general absence of estimates of the costs of the retail-access related provisions of the Joint Proposal stands out as inconsistent with the rest of the Joint Proposal and raises serious questions about whether the ALJs and Commission will be provided complete information about the consumer impact of including these retail access provisions of the Joint Proposal.

Q. You mentioned that the Joint Proposal also contemplates the continuation of Central Hudson's ESCO Referral Program. Do you have any comments regarding that program?

A. Yes. This program was created as a result of the Company's retail access collaborative and was approved by the Commission with a commencement date of February 1, 2006. (Case 05-M-0332, Order Adopting ESCO Referral Program Guidelines and Approving an ESCO Referral Program Subject to Modifications, December 22, 2005, p 65) An e-mail from Central Hudson dated March 16, 2006 announced that due to lack of participation, a meeting that had been scheduled for March 21, 2006 to solicit interest in that program, had been canceled until further notice. (E-mail from Mr. James Voltz of Central Hudson to interested parties, March 16, 2006, attached as Exhibit___(CPB), Schedule 3) According to the Company's tariff, at least two ESCOs providing supply service and serving residential customers are required to participate in the program or it will not be offered and advertising will not commence. (Cases 05-M-0858 and 05-M-0332, Central Hudson Gas and Electric Corporation Energy Switch Program, January 13, 2006, Electric Tariff No. 15 Section 35, Gas Tariff No. 12 Section 41) The CPB understands that these requirements have not yet been met.

Q. What do you recommend?

A. As explained in Point II, retail competition for mass market customers in Central Hudson's service territory is weak at best, despite considerable effort and expenditure of ratepayer funds. Further, the general absence of interest from ESCOs in the ESCO Referral Program in the more than four months since the Commission approved that "best practice," suggests that this situation may not improve in the near future. That, coupled with high energy bills and the likelihood of a series of large delivery rate increases, suggests that the Commission should carefully assess the reasonableness of the retail access provisions identified in this section. As a necessary first step, the ALJs should direct the Joint Proposal's proponents to identify the revenue requirement impact of these provisions. That information is necessary to provide the CPB, other parties and ultimately the Commission, information to determine whether the provisions are in the public interest at this time, or whether they should be modified or rejected.

Absent this information, we recommend that the retail access-related requirements imposed on Central Hudson be curtailed considerably, with a reduction of the revenue requirement under the Joint Proposal of $100,000 each year. Based on available information, a revenue requirement reduction of this amount would represent a much better use of scarce ratepayer dollars at this time than these retail access programs and would help begin the transition in Central Hudson's territory, away from ratepayer subsidization of functions that could and should be conducted by ESCOs, including advertising, marketing, customer acquisition, billing, collection, advocacy and representation in proceedings before the PSC. This recommendation is fair to the Company, in that its costs and revenues would be reduced by the same amount.

COMPETITION EDUCATION BUDGET

Q. Please summarize those provisions of the Joint Proposal that address competition education.

A. The Joint Proposal includes an allowance of $350,000 for each of the three rate years, for a "competition education campaign aimed at promoting customer migration." The campaign would be developed by the Company "in collaboration with Staff and interested ESCOs." (Joint Proposal, Section XVI(G))

Q. What is the CPB's position on this matter?

A. This provision should be modified in several respects. First, the budget for competition education should be reduced. As explained above, retail competition for mass market customers in Central Hudson's service territory continues to languish and Central Hudson's customers are facing extremely high energy prices and a series of very large increases in both natural gas and electricity delivery rates. Especially in this environment, all ratepayer-funded spending by utilities should be scrutinized to ensure that it is cost effective and in consumers' interest.

The prefiled testimony of the Joint Proposal's proponents does not contain or reference any analyses or studies demonstrating that Central Hudson's previous ratepayer-funded outreach and education efforts regarding retail competition have been cost effective. Moreover, as explained in the previous section, there has been a noteworthy lack of ESCO interest in the much heralded ESCO referral program in Central Hudson's territory, and in the matters being addressed in this proceeding. In these circumstances, ratepayers' subsidization of advertising, promotion and other customer acquisition activities that could and should be conducted by ESCOs, should decline substantially. We recommend that the Joint Proposal be revised so that ratepayers fund no more than $175,000 annually of these retail competition outreach and education programs, or one-half of the amount reflected in the Joint Proposal. As explained above, the remaining $175,000 should be spent on outreach and education programs to inform consumers of the reason for high energy prices and action they can take to help manage their energy bills.

Q. What are your other concerns regarding this proposal?

A. The CPB is also concerned with the objective of the competition education campaign, which is described as "promoting customer migration." (Id.) The purpose of ratepayer funded competition education programs should be to provide balanced information on retail competition to consumers, including an accurate assessment of the potential benefits and risks associated with obtaining service from an ESCO. It is inappropriate to use ratepayers' money to finance one-sided "education" campaigns designed only to promote migration, especially in an environment of high energy prices and large delivery rate increases and where ESCOs have generally not met the needs of Central Hudson's residential customers, as explained in detail above.

The CPB is also concerned that the Joint Proposal would exclude the CPB and other representatives of consumers from participating in the design of the "education" campaign. A program that prohibits input and participation by parties that represent the interests of the consumers who fund the campaign, such as the CPB, is not in the public interest.

Moreover, precluding the CPB from participating in this effort would be contrary to PSC policy. The Commission recently stated:

> Whether or not a party is a signatory to a joint proposal is not a reasonable basis for determining whether or not it should be served with copies of certain reports or the extent to which it should be

> consulted on issues of interest to it. Such a distinction is contrary to our long-standing policy of affording all interested parties equal opportunities to participate fully and effectively in our proceedings.[2] Such a distinction also undermines cooperation we would expect from all parties in various future collaboratives that will ensue. Accordingly, in all instances where it is proposed that information will be filed and served on interested signatory parties, such information must also be served on any other interested party who expressly requests such information following our decision in this case. Moreover, in instances where it is proposed that consultations be limited in part to signatory parties, all interested active parties interested in participating in such consultative process shall have exactly the same right to participate upon request. (Case 04-E-0572, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Electric Service, Order Adopting Three-Year Rate Plan, March 24, 2005, p. 105)

Q. Please summarize your recommendations regarding the competition education portion of the Joint Proposal.

A. The CPB recommends that the Joint Proposal be revised so that ratepayers fund no more than $175,000 for competition education programs annually, an amount equal to that dedicated to education on high energy prices. The purpose of that program should also be revised, to provide balanced information for the benefit of Central Hudson's customers who fund that program, and not to serve solely the needs of ESCOs. Finally, the Joint Proposal should be revised so that representatives of customers who fund this program are not denied the opportunity to participate in the design of that program.

[2] 16 NYCRR §4.3(c)(1).

ADDITIONAL MEASURES TO MITIGATE THE RATE INCREASES

Q. Are additional measures available to help mitigate rate increases?

A. At least two such measures are available. First, excess funds are available in the electric depreciation reserve. Some of this excess is being used to fund the phase-in of the electric rate increase. Under the Joint Proposal, approximately $20 million of excess electric depreciation reserve would be available, having a pre-tax equivalent of $32.992 million. (Joint Proposal, Appendix G, Schedule 3) The Joint Proposal appears to anticipate that this reserve might be used for two purposes: (1) to fund the AMR pilot if competitive metering funds are no longer available (Joint Proposal, Section XV (B)(3)) and (2) to fund the cost of electric backout credits through June 30, 2007 (Joint Proposal, Section VI (A) (1)) We have fully explained above, why the AMR pilot should not be conducted at this time. Although a forecast of the dollar amount of the electric backout credits for the first Rate Year was apparently not made by the proponents of the Joint Proposal (Response to CPB to DPS Staff IR 7), it appears that the vast majority of the excess depreciation reserve deficiency is available to be used for customer benefit. That represents overpayments by electric ratepayers, which could, and should, be used to help reduce the amount of the electric rate increase at this time. This $20 million could be used to reduce the electric rate increases under the Joint Proposal, by approximately $6 million in each of the three years of the rate plan, without affecting the Company's earnings.

Second, as fully explained in the November 21, 2005 testimony of Mr. Larkin, the PSC could extend the amortization of large and unusual losses that

Central Hudson incurred in 2001 and 2002 on its retirement plan assets. Actuarial losses of $100,225,064 of actuarial losses were incorporated into the Company's net periodic pension accruals in 2002, and another $59,779,947 of actuarial losses were incorporated within the net periodic pension accrual in 2003. Under the Joint Proposal, these losses would be amortized over 10 years. Extending the amortization for an additional 10 years, would reduce the 2005 total net periodic pension accrual by $9,294,109, thereby reducing the electric rate increase by approximately $5,228,866 ($9,294,109 times the allocation percentage of 56.26%) and reducing the gas rate increase by approximately $1,211,952 ($9,294,109 times the allocation percentage of 13.04%). (Testimony of Mr. Larkin, November 21, 2005, pp. 11 – 15)

The CPB recommends that the Joint Proposal be revised to reflect our first recommendation regarding the use of the electric depreciation reserve surplus. We also recommend that the Commission consider our second proposal, should additional rate migitation be required. Both of these proposals are fair to the Company, in that they do not affect the Company's earnings. They are also fair to ratepayers, in that they represent a better use of ratepayer money than contemplated under the Joint Proposal.

PART V – POSITIVE ELEMENTS OF THE JOINT PROPOSAL

Q. Please summarize some of the positive elements of the Joint Proposal.

A. The CPB submitted pre-filed direct testimony in this proceeding. We also participated in negotiations which resulted in this Joint Proposal to help ensure that: (1) Central Hudson's electric and gas delivery rates are "just and reasonable" and "in the public interest" (Public Service Law ("PSL") §§ 72, 65(1) and 65(5)), (2) residential and small business customers in the Company's service territory have the opportunity to purchase commodity service at a fixed price from the utility, and (3) other important consumer benefits are secured.

The Joint Proposal achieves some of those benefits. For example, it takes an important step in reducing the size of the rate increases requested by Central Hudson, phases in the electric delivery rate increase to help ameliorate customer impacts and establishes a new program to provide additional assistance to Central Hudson's low income customers in a cost effective manner. The Joint Proposal also correctly excludes several proposals made by parties in their pre-filed direct testimony including a ratepayer-funded incentive to the Company for migrating customers to ESCOs that was supported by the Company and DPS Staff, and a Provider of Last Resort Surcharge proposed by the Company. These results are important and should be approved by the Commission.

CERTAIN ASPECTS OF REVENUE REQUIREMENT

Q. Please explain the relationship between the rate increases that would result from Central Hudson's original proposal and those that would occur if the Joint Proposal was approved.

A. Central Hudson initially requested rate increases of $51.5 (30.5%) for its electric delivery operations and $17.5 million (42.5%) for its natural gas operations, effective July 1, 2006. Under the Joint Proposal, the Company's required electric rate increases would be $41.383 million, $6.121 million and $5.529 million, before phase-in, in Rate Years 1 – 3, respectively. (Joint Proposal, Appendix A, Schedule 1) The gas rate increases under the Joint Proposal would be $8.0 million and $6.1 million in Rate Years 1 and 2, respectively. (Joint Proposal, Appendix D, Schedule 1)

The Joint Proposal represents an important step in reducing the size of the rate increases that could occur in this proceeding. However, as explained in detail in Point IV above, much more can, and should, be done to reduce them further.

PHASE-IN OF RATE INCREASES

Q. Please explain how the Joint Proposal phases-in the delivery rate increase.

A. In partial recognition of the impact that increases would have on consumers, the Joint Proposal phases-in the first rate increase in a manner that results in equal dollar rate increases of $17.89 million in each of the three years of the rate plan. (Id., Schedule 2) A phase-in is necessary and appropriate and should be reflected in any Commission decision in this proceeding in which the first year electric delivery rate increase exceeds approximately 10%.

Q. Please explain how the gas rate increase is moderated under the Joint Proposal.

A. The gas delivery revenue requirements under the Joint Proposal reflect moderation resulting from deferring a portion of the first year rate increase and amortizing it along with revenue requirement increases in Rate Years 2 and 3. (Joint Proposal, Section IV (A)) That amount is anticipated to be recovered over a seven-year period beginning at the start of Rate Year 2. This approach is reasonable in these circumstances and should be retained.

LOW INCOME PROGRAM

Q. Please summarize the low income program contained in the Joint Proposal.

A. The Joint Proposal includes a program to provide financial assistance to the Company's low income customers consisting of two parts: (1) an Interim Program that would begin July 1, 2006 and continue no later than September 1, 2007 and (2) an Enhanced Powerful Opportunities Program ("EPOP"). The Interim Program is intended to provide the transition from the original Powerful Opportunities Program ("POP") to the EPOP. The EPOP, currently under development by the parties, will feature: increased funding in Rate Years 2 and 3, direct administration of the program by Central Hudson, an arrears forgiveness incentive of up to $100 per month with suspension of balance-due late charges, an annual bill discount based on income level and family size, budget billing, referral to NYSERDA's Empower NY Program for energy efficiency and conservation programs, and a specific format and schedule for program reporting and evaluation. The Interim Program will include all of the above EPOP provisions except that the participants will receive a $5 discounted customer charge per month for gas service and $5 per month for electric service ($10 total charge for dual service customers). (Joint Proposal, Section XI)

Q. Why does the CPB support these provisions?

A. The CPB testified that significant changes are required to the Company's existing POP to ensure that it provides the intended benefits to Central Hudson's eligible customers and operates in a cost effective manner. (Testimony of CPB Witness Ms. Donna M. DeVito, November 21, 2005, pp. 4 - 14) We support the proposed low income program in the Joint Proposal because, among other things, it provides greater discounts to customers with more need, an increased arrears forgiveness incentive, and direct management by Central Hudson to help ensure a more focused and cost effective program.

ABSENCE OF RETAIL MIGRATION INCENTIVE

Q. Please summarize your position on the absence of a retail access migration incentive in the Joint Proposal.

A. In direct testimony in this case, Central Hudson recommended that it be provided a financial incentive, in certain conditions, based on the number of customers that migrate to ESCOs in its service territory. In its direct testimony, DPS Staff supported the recommendation that the Company have such an incentive. The CPB was the only party to oppose such an incentive in our direct testimony. (Testimony of Mr. Niazi, p. 27)

The Joint Proposal omits such a mechanism. The absence of such a migration incentive is a positive element of the Joint Proposal and should be preserved. A migration incentive is not required for Central Hudson to provide safe and reliable service. Moreover, as a general matter, incentives should align utility interests with those of customers who fund them, whereas a customer migration incentive is intended to align the utility's incentives with those of ESCOs. A migration incentive is particularly inappropriate in the context of the high energy costs faced by ratepayers and the magnitude of the rate increase proposed in this proceeding. The absence of such an incentive in the Joint Proposal is a positive feature, particularly since many rate plans for other utilities include such a measure.

Q. Does this conclude your testimony?

A. Yes.

ATTACHMENT

ATTACHMENT 1

QUALIFICATIONS OF DR. DOUGLAS W. ELFNER

Q. Dr. Elfner, please summarize your educational and employment experience.

A. I received a B.A. with honors and distinction in economics and mathematics from the University of Delaware in 1976, and a Ph.D. in Economics from the University of Michigan in 1982. From 1982 through 1984 I was an Assistant Professor of Economics at the University of Vermont, where I taught courses in econometrics and microeconomics. I was employed from December 1984 to January 1989 by AT&T in Bedminster, New Jersey, where I held positions of increasing responsibility as an Economist in the Market Analysis and Forecasting organization. My responsibilities included developing revenue and quantity forecasts for existing services; analyzing opportunities for new services and the effects of changing the price and rate structures of existing services; and producing forecasts and market analyses for regulatory purposes.

Since January 1989, I have been employed by the New York State Consumer Protection Board. As Director of Utility Intervention, I am responsible for all aspects of analysis, policy development, and advocacy on behalf of New Yorkers regarding the regulation of utilities. I am also responsible for the CPB's outreach and education programs on all consumer issues.

I am a member of Phi Beta Kappa, the American Economic Association and the National Association of Business Economists. I have presented original papers at conferences sponsored by the American Economic Association and the Econometrics Society.

Q. Have you previously testified before the Commission?

A. Yes. I have testified in numerous cases before the New York State Public Service Commission.

EXHIBIT