

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Proceeding on Motion of the Commission as to
the Rates, Charges, Rules and Regulations of
Consolidated Edison Company of New York for
Electric Service

Case 08-E-0539

DIRECT TESTIMONY AND
EXHIBIT
OF
TARIQ N. NIAZI

Dated: September 8, 2008
Albany, New York

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1 Q. Please state your name, title and business address.

2 A. Tariq N. Niazi, Chief Economist, New York State Consumer Protection Board
3 ("CPB"), Suite 2101, Five Empire State Plaza, Albany, New York 12223.

4
5 Q. Mr. Niazi, please summarize your background and experience.

6 A. I passed my candidacy examination, completed all required course work and
7 passed all comprehensive examinations in the Doctoral Program in Managerial
8 Economics at Rensselaer Polytechnic Institute. I have a Master's Degree in
9 Economics from the State University of New York at Albany. I also received a
10 Master's Degree in Public Administration from Punjab University in Pakistan
11 and a Bachelor's Degree in Economics and Political Science at Forman
12 Christian College in Pakistan.

13 I have been employed by the CPB since March 1981, first as an
14 economic consultant and then as a rate analyst. Later, I was promoted to the
15 position of Principal Economist. I was appointed to my present position in
16 October 1990. I have worked on numerous issues in electric, gas, telephone
17 and water proceedings. My responsibilities are in the areas of economic and
18 financial analysis, rate design, policy analysis, cost of service, tariff analysis
19 and cost of capital.

20 I serve as the CPB's representative at the New York Independent
21 System Operator ("NYISO"). The CPB has been designated by the NYISO as

1 the statewide consumer advocate and is a formal voting member of the
2 NYISO's decision making committees. I also represent the CPB on the
3 Natural Gas Reliability Advisory Group as a consumer representative. Finally,
4 I also serve on the New York State Energy Research and Development
5 Authority's System Benefit Advisory Group.

6

7 Q. Have you previously testified before the New York State Public Service
8 Commission?

9 A. Yes. I have testified in numerous proceedings before the Public Service
10 Commission ("PSC" or "Commission")

11

12 Q. What is the purpose of your testimony?

13 A. My testimony has two parts. In Part 1, I demonstrate that Consolidated
14 Edison Company of New York, Inc.'s ("Con Edison" or the "Company")
15 requested return on equity of 11.0% for its electric business is overstated
16 and that the Company's current cost of equity is 9.91%. I also respond to
17 several assertions made by the Company in support of its return estimate
18 and identify several errors in its presentation.

19 In Part II, I address the Company's rate design proposal regarding
20 customer charge increases to SC1 and SC 7, and recommend that these
21 charges not be increased.

1 Q. Have you prepared an exhibit for your testimony?

2 A. Yes. I am sponsoring Exhibit ___ (TNN), consisting of two schedules.

3

4 **PART I - RATE OF RETURN ON EQUITY**

5

6 Q. What return on common equity is Con Edison requesting for its electric
7 operations?

8 A. Con Edison is requesting a return on common equity of 11.0%. Its
9 recommendation is based on averaging the results of multiple estimates from
10 three different methods: 1) an average of 11.4% using the discounted cash
11 flow method ("DCF") based on four different estimates ranging from 11.0% to
12 11.6%; 2) an average of 11.2% using the capital asset pricing model ("CAPM")
13 based on two estimates of 11.0% and 11.4%; and 3) an average of 10.3%
14 using the Risk Premium method based on two estimates of 10.5% and 10.1%.
15 In addition, Con Edison is recommending a 0.3% premium for committing not
16 to seek further rate increases for three years. As I discuss in my testimony,
17 the equity returns based on the DCF and CAPM methods are overestimated
18 and should be rejected, while equity returns based on the Risk Premium
19 method should be discarded as the use of this method has been repeatedly
20 rejected by the Commission. Finally, a premium for an extended stay out, as I
21 discuss later in my testimony, should also be rejected at this time.

22

1 Q. What is your recommended rate of return or capitalization rate for Con
2 Edison?

3 A. I recommend a total equity return of 9.91% for Con Edison. My equity cost
4 estimate is based on application of the DCF and CAPM methods to a proxy
5 group of electric and combination electric and gas companies with investment
6 grade debt ratings by Moody's and Standard & Poor's ("S&P"). This rating
7 criterion is different from the "A/A" rated proxy group for combination electric
8 and gas companies reflected in the Recommended Decision in the Generic
9 Finance Case (91-M-0509). As explained below, this change in the rating
10 standard is appropriate and necessary to arrive at a proxy group of sufficient
11 size to obtain reliable results. In other respects, my approach is consistent
12 with the Recommended Decision in the Generic Finance Case.

13 The DCF approach applied to the proxy group results in a median
14 equity cost estimate of 9.76%. The CAPM approach applied to the same proxy
15 group produces an equity cost of 10.03% for the traditional CAPM and 10.37%
16 for the zero-beta CAPM. The average of the two CAPM methods results in an
17 equity return of 10.20%. The CAPM analysis is based on a 11.4% market
18 return, a .81 proxy group beta, a risk free rate of 4.18% and a risk premium of
19 7.22%. Applying weightings of 2/3 to the median DCF result and 1/3 to the
20 average of the CAPM results, in accordance with the Recommended Decision
21 in the Generic Finance case and the Commission's decision in several recent

1 cases,¹ I arrive at an equity return of 9.91% for Con Edison's electric
2 operations.

3

4 A. Proxy Group

5

6 Q. How did you select the proxy group companies for your analysis?

7 A. I used the following criteria in selecting the electric proxy group: 1) each
8 company must be listed by Value Line as an electric utility company composed
9 of electric or combination electric and gas distribution companies; 2) each
10 company must have investment grade debt rated by Moody's and Standard &
11 Poor's; 3) over 70% of each company's total revenues must be derived from
12 regulated utility operations; and 4) the company should not be involved in
13 merger/acquisition activity.

14 Based on the stated criteria, I started the selection of the proxy group by
15 looking at all 59 electric and combination electric and gas companies listed by
16 Value Line. I used the latest issues of the Value Line Investment Survey dated
17 May 30, 2008, June 27, 2008, and August 8, 2008 listing electric utility
18 companies in the Eastern, Central and Western states respectively. In step
19 two, I discarded any company that was rated below investment grade by either

¹ See, most recently, Case 05-E-1222, New York State Electric & Gas Corporation, Order Adopting Recommended Decision with Modifications, August 23, 2006, Cases 02-E-0198 and 02-G-0199, Rochester Gas and Electric Corporation, Order Adopting Recommended Decision with Modifications, March 7, 2003, p. 72 and Case 07-E-0523, Consolidated Edison Company of New York, Inc., Order Establishing Rates for Electric Service, March 25, 2008.

1 Moody's or Standard & Poor's. As a result of this screen, 9 companies rated
2 below investment grade were discarded, leaving 50 companies in the proxy
3 group. Next, I reviewed the level of regulated operations of the 50 companies
4 with an investment grade debt rating in the proxy group, discarding companies
5 with less than 70% of total annual revenues derived from regulated utility
6 operations. As a result of this criteria, an additional 15 companies were
7 excluded from proxy group, leaving 35 companies. I further discarded 4
8 companies; Energy East Corporation from the proxy group as it is in the
9 process of being acquired by Iberdrola SA, El Paso Electric since it is not
10 paying any dividends, ITC Holding Corp. as it is a transmission only electric
11 company and UIL Holding Corp. as its debt is rated only by Moody's and not
12 Standard & Poor's. After discarding companies that did not meet the criteria for
13 inclusion in the proxy group listed above, the proxy group I have used for my
14 analysis is comprised of 31 companies as shown in Exhibit__ (TNN), Schedule
15 1.

16

17 Q. Why did you not follow the criteria established in the Generic Finance Case for
18 the selection of the proxy group?

19 A. It has become virtually impossible to follow the criteria for selecting proxy
20 groups established in the Generic Finance Case because there is not a large
21 enough sample on which to establish a reliable estimate. Since the Return on

1 Equity Consensus Document ² (dated June 2, 1993) and the Recommended
2 Decision in the Generic Finance Case (dated July 19, 1994) were issued,
3 significant changes have occurred in the electric industry in terms of debt
4 ratings and the level of regulated utility operations. When the Return on Equity
5 Consensus Document was issued, there were 33 electric and combination
6 electric and gas companies that were rated "A/A" by Moody's and Standard &
7 Poor's. That number has now dwindled to six companies, two of which have
8 regulated revenues less than 70% of total revenues. In other words, only four
9 companies would make the proxy group based on "A/A" rating as established
10 in the Generic Finance Case. That is not a large enough sample on which to
11 establish a reliable estimate of the cost of equity. In Con Edison's last
12 proceeding (Case 07-E-0523), the Judges made the following observation:

13 With respect to the use of proxy group results, it has become
14 increasingly difficult to find representative firms, in sufficient
15 numbers, for the electric combination and the natural gas utility
16 companies that operate in New York.

17 * * *

18
19
20 As long as the Generic Finance Case approach can be
21 sustained, we do not recommend that the Commission revert to
22 the approach that it previously used that relied predominantly on
23 the market data available for the company it was addressing in a
24 particular rate proceeding (Recommend Decision, p. 135)
25

² Prepared by Signatory Members of the Electric and Gas Industry Group that included the Department of Public Service and all New York utilities including the Consolidated Edison Company of New York, Inc.

1 Q. Did the Generic Finance Case establish a level of regulated operations for
2 inclusion in the electric proxy group?

3 A. No. The only criteria established in the Generic Finance Case for the electric
4 company proxy group was that all companies included must have senior debt
5 rated in the "A" category by Moody's and Standard & Poor's.³ Presumably,
6 most electric utilities at that time had exclusively regulated operations; hence,
7 the level of revenues derived from regulated operations was not an issue.
8 However, the Generic Finance Case did address the issue of regulated versus
9 unregulated operations in regards to the establishment of the gas proxy group
10 composed of "pure play" gas distribution companies. It required that over 96%
11 of each company's total revenues must be derived from gas utility operations.⁴

12 The proxy group of 31 companies I used for my analysis has an
13 average of 88.5% of its revenues coming from regulated operations. Con
14 Edison in comparison has 82.5% of its revenues derived from regulated
15 operations.

16

17 B. Discounted Cash Flow Model

18

19 Q. How did you arrive at your DCF equity return estimate for Con Edison?

20 A. I applied a two-stage DCF growth model to the proxy group. This is the same

³ Id., at 6.

⁴ Id.

1 model that was developed in the Generic Finance Proceeding and was
2 adopted by the ALJs in their Recommended Decision. It has been consistently
3 relied upon by the Commission for over a decade, including the Company's
4 last proceeding (Case 07-E-0523, Consolidated Edison Company of New
5 York, Inc.). As shown in Exhibit__ (TNN), Schedule 1, page 3 of 3, this resulted
6 in a median equity return of 9.76% for Con Edison.

7
8 Q. Could you please briefly describe the DCF method that you applied?

9 A. Yes. The DCF method is a market based approach that determines the return
10 on equity from the investor's perspective. The familiar DCF formula is:

$$11 \quad P_0 = \frac{D_1}{k-g}$$

12
13
14
15 This fundamental equation states that a rational investor equates the
16 current market price (P_0) of a stock to the expected future returns from that
17 stock. Future returns from the stock are the expected stream of dividends
18 discounted at the market-required return (k), net of the effect of growth (g).

19 D_1 is the first year dividend.

20 Since the capitalization rate is not directly observable, the basic idea of
21 the DCF approach is to derive the cost of equity from the observed share price
22 and an estimate of investor expected future dividends. This is based on the

1 intuitive concept that dividends plus capital appreciation reflect the investor's
2 total expected return.

3 The DCF formula can be rewritten by solving the above equation for the
4 cost of equity (k).
5

$$6 \quad k = D_1/P_0 + g$$

7
8 In terms of the rewritten DCF formula, the cost of equity (k) is equal to the sum
9 of the expected dividend yield (D_1/P_0) and the expected growth rate of future
10 dividends (g).
11

12

13 Q. What is the first component of the DCF formulation [$k = D_1/P_0 + g$]?

14 A. The first component of the DCF formulation is the expected dividend yield
15 (D_1/P_0). It is the quotient of the expected future dividends and the current
16 stock price. A stock's dividend yield, in comparison with the dividend yield of
17 other stocks, indicates whether it is an income or a growth asset. For
18 example, bonds generally have high yields and low growth, and are hence
19 considered income assets. Conversely, common stocks of growing firms have
20 low yields and high growth, and are generally considered growth assets.

21

22 Q. What is the growth term (g) in the standard DCF formula?

23 A. The growth term in the DCF formula represents the growth in the value of the

1 firm's common stock as reflected through dividend and stock price increases.
2 The DCF approach assumes that the firm is operating in a "steady state." If
3 the steady state holds, the growth rates in earnings per share, dividends per
4 share and book value per share are the same, and are a product of the
5 retention ratio and the expected return on equity.

6 In reality, it is not possible to achieve a "true" steady state. Thus, book
7 value per share, dividends per share and earnings per share generally grow at
8 different rates that may all differ from the growth rate indicated by the retention
9 ratio and expected return on equity.

10

11 Q. How did you estimate the two-stage proxy group DCF equity returns for Con
12 Edison?

13 A. I estimated the two-stage proxy group DCF equity return, relying on the model
14 used in the Generic Finance Proceeding by the Electric and Gas Industry
15 Group. The six-month average prices for the companies in the proxy group
16 are the average of the monthly high and low closing price of each stock. I
17 used the period February 1, 2008 to July 31, 2008. The other data, including
18 dividends per share, earnings per share, book value per share and the shares
19 of common stock, are all taken from the May 30, 2008, June 27, 2008, and
20 August 8, 2008, issues of the Value Line Investment Survey. As shown in

21

1 Exhibit__ (TNN), Schedule 1, page 3 of 3, the median equity return based on
2 this method is 9.76%.

3

4 C. Capital Asset Pricing Model

5 Q. What were the results of your application of the CAPM methodology to
6 estimate Con Edison's equity return?

7 A. The CAPM produced a required return on equity of 10.03% for the traditional
8 CAPM and 10.37% for the zero-beta CAPM approach. The average of the two
9 CAPM approaches resulted in an equity return of 10.20%. Exhibit__ (TNN),
10 Schedule 2 provides a detailed explanation of the calculations used to
11 determine the equity return under the CAPM.

12

13 Q. Have you used the same CAPM methodology that was adopted in the Generic
14 Finance Case?

15 A. Yes. The only difference is the use of Merrill Lynch based expected return
16 rather than one based on historic data from Ibbotson Associates. Once again,
17 the Commission adopted this change from the Generic Finance methodology
18 over a decade ago and has consistently relied upon it. In Case 05-E-1222, the
19 Commission said the following:

20

21

22

As for the CAPM, NYSEG's reliance on the historic Ibbotson data and a DCF of the S&P 500 to estimate the market return is

1 rejected. The historic Ibbotson data is inconsistent with more
2 recent forward-looking Ibbotson estimates and the S&P 500
3 DCF relies upon the single growth DCF model which the
4 Commission has not employed for over a decade.

5
6 (Order Adopting Recommended Decision with Modifications,
7 Issued and Effective August 23, 2006, at 96.)
8
9

10 Q. Please briefly describe the CAPM approach for estimating equity returns.

11 A. The CAPM formally describes the trade-off between risk and required return
12 for securities. The equation below illustrates that the rate of return required by
13 investors (R_c) consists of a risk-free return (R_f), plus a premium compensating
14 investors for bearing the risk commensurate with the stock's market risk (Beta)
15 and the market price of risk ($R_m - R_f$). The risk premium varies from stock to
16 stock. The traditional CAPM formula is stated as:

$$17 \quad R_c = R_f + \text{Beta} (R_m - R_f)$$

18 A basic premise underlying the CAPM is that there is less risk
19 associated with an investment in a relatively stable stock than in the stock of a
20 small speculative venture. As a result, investors in a speculative venture stock
21 will require higher returns than investors in a stable stock, because they are
22 assuming additional risk. The CAPM quantifies the additional return investors
23 require for accepting this higher risk.

24

25 Q. Please describe Exhibit__ (TNN), Schedule 2.

1 A. Exhibit__ (TNN), Schedule 2 consists of two pages. Page 1 shows the
2 traditional CAPM formula used to derive the required return for the proxy
3 group, while page 2 shows the zero-beta CAPM application. The required
4 return is the sum of the risk-free rate and the market-risk premium adjusted
5 using the proxy group average beta.

6
7 Q. How did you determine the risk free rate, market return and beta used in this
8 analysis?

9 A. To determine the risk-free rate, I used a six-month average ending July 31,
10 2008, of 30-Year and 10-year Treasury Bond Yields as reported by the Federal
11 Reserve Board. (Federal Reserve Statistical Release, Historical Data) That
12 average is 4.18%.

13 The beta of 0.81 used to adjust the market risk-premium was derived
14 from the proxy group as the average of the individual company betas as
15 reported by Value Line. These are the same electric and combination electric
16 and gas proxy group companies used for the DCF analysis.

17 The market return of 11.4% I used is based on the August 11, 2008
18 issue of Merrill Lynch Quantitative Profiles - Monthly Insights for Equity
19 Management. The 11.4% estimate is the implied return for a portfolio of 1,162
20 firms.

21 The risk premium was derived by subtracting the risk-free rate of 4.18%

1 from the market return of 11.4%, resulting in a risk premium of 7.22%.

2 Incorporating all variables in the respective formulas, indicates a
3 required return of 10.03% for the traditional CAPM approach and 10.37% for
4 the zero-beta CAPM approach, as shown in Exhibit __ (TNN), Schedule 2, page
5 1 and 2 respectively. The average of the two CAPM approaches results in an
6 equity estimate of 10.20% $((10.03\% + 10.37\%)/2)$.

7
8 D. Overall Recommendation

9 Q. What is your estimate of equity cost for Con Edison?

10 A. I estimated the cost of equity by applying the 2/3 DCF – 1/3 CAPM weighting
11 consistently used by the Commission and also recommended by the Judges in
12 the Generic Finance case. My median DCF estimate is 9.76% and my
13 average CAPM estimate is 10.20%. With the DCF estimate given 2/3 weight
14 and the CAPM estimate given 1/3 weight, the resulting return before any
15 adjustment, is 9.91%.

16
17 Q. Did you make any adjustments to the estimated equity return for Con Edison?

18 A. Yes. I adjusted the estimated return of 9.91% for credit quality. Con Edison is
19 rated A- by Standard & Poor's and A2 by Moody's. The median bond ratings
20 of the proxy groups I have used are Baa2 by Moody's and BBB by Standard &
21 Poor's, both in the middle of the "B" rating category. To account for the

1 differences in the bond ratings of the proxy group and Con Edison, I looked at
2 the difference in A-rated and Baa/BBB-rated long term utility bond yields. Over
3 the six-month period from February 2008 to July 2008, A-rated utility bond
4 yields averaged 6.18%, while Baa/BBB-rated utility bond yields over the same
5 period averaged 6.40%. I took 15 basis points or two-thirds of the 22 basis
6 points difference between A-rated and Baa/BBB-rated long-term utility bond
7 yields as the basis of my credit quality adjustment. I did not use the entire
8 difference in bond yields between "A" and "Baa/BBB" rated utility bonds
9 recognizing that the Standard & Poor's rating of Consolidated Edison is on the
10 low end of the "A" rated category. Subtracting 15 basis points from my earlier
11 estimate of 9.91% results in an equity return estimate for Con Edison of 9.76%
12 after applying the credit quality adjustment.

13

14 Q. Are you proposing an issuance adjustment for the costs of equity issuance
15 during the rate year?

16 A. Yes. Company Exhibit_ (AP-13), shows that the company will be issuing \$477
17 million of equity during the rate year. Based on the method approved in the
18 Generic Finance Case and relied upon by the Commission in subsequent
19 proceedings, I estimated an equity issuance allowance of 15 basis points.
20 Based on issuance costs of approximately 3.0% that is consistent with
21 previous company equity financing, I have estimated an issuance cost of \$14.3

1 million. The average common equity balance reported by the Company in
2 Exhibit_ (AP-12), Schedule 1 as updated on July 25, 2008, is approximately
3 \$9.4 billion. The \$14 million issuance cost is approximately 0.15% of the \$9.4
4 billion common equity balance.

5 Adding 15 basis points to my equity return estimate after credit quality
6 adjustment of 9.76% results in a final equity estimate of 9.91%. I recommend
7 that the issuance adjustment be updated at the time of the Commission's
8 Order, based on the approved capital structure and the actual amount of the
9 equity issuance.

10

11 Q. Have you made an adjustment to your equity return recommendation for a
12 multi-year rate plan?

13 A. No, not at this time. I recommend that the Commission establish an equity
14 return for one year. The CPB is not willing to suggest a longer-term return rate
15 based on Con Edison filed plan, which it does not support as presented, and
16 cannot speculate about the duration of any plan that may ultimately result from
17 this proceeding. Should a comprehensive and balanced multi-year rate plan
18 be addressed in negotiations, the CPB would be willing to discuss the
19 appropriateness of an adjustment to its calculated equity return for a multi-year
20 stay out.

21

1 Q. Have you estimated the revenue impact of your 9.91% equity return
2 recommendation as compared to the Company's 11.0% equity allowance
3 request?

4 A. Yes. Based on the Company's response to CPB Interrogatory No. 8, an
5 increase/decrease of 10 basis points in equity return has a revenue
6 requirement impact of approximately \$12 million. Since the difference
7 between my equity return estimate of 9.91% and Con Edison's request of
8 11.0% is 109 basis points, Con Edison's electric customers would save
9 approximately \$131 million if my recommendation is adopted.

10

11 E. Analysis of Consolidated Edison's Equity Return Proposal

12 Q. Please briefly describe how the Company estimated its proposed cost of equity
13 of 11.0%.

14 A. Company Witness Dr. Roger Morin recommends an equity return of 11.0%
15 based on the use of three different methods. The three methods he uses are
16 DCF, CAPM, and Risk Premium. As shown in Exhibits RAM-5, RAM-6, RAM-
17 7 and RAM-8, Dr. Morin estimated four separate DCF equity returns using
18 different combinations of proxy groups and growth rates. Dr. Morin's DCF
19 calculations resulted in equity returns ranging from 10.7 % to 11.4%. He then
20 added 20 to 30 basis points for flotation costs to his DCF estimates resulting in
21 equity return estimates ranging from 11.0% to 11.6%. Second, he used the

1 CAPM approach that produced equity returns of 10.7% and 11.1% for the
2 traditional and zero-beta CAPM, respectively. Dr. Morin then added 30 basis
3 points for flotation costs, bringing his CAPM estimates to 11.0% and 11.4% for
4 the traditional and zero-beta CAPM respectively. Third, Dr. Morin used two
5 Risk Premium analyses, resulting in estimates of 10.1% and 10.5% equity
6 return.

7

8 Q. Do you agree with the Company's approach in estimating its equity return?

9 A. No. Dr. Morin's estimates should not be relied upon. His DCF analysis is not
10 consistent with the Recommended Decision in the Generic Finance Case, as
11 well as the numerous PSC decisions based on that methodology, and results
12 in estimates that are overstated. His CAPM estimate is based on the use of
13 unrealistic market returns and is also overstated. Moreover, Dr. Morin's
14 selection of proxy groups is arbitrary, flawed and inconsistent with the intent of
15 the Generic Finance Case. Finally, the use of the Risk Premium method was
16 rejected by the ALJs in the Generic Finance Case and has been repeatedly
17 rejected by the Commission.

18

19 Q. Please briefly describe how Dr. Morin selected his proxy groups.

20 A. Dr. Morin utilizes two different proxy groups, the first based on companies
21 designated as distribution utilities by S&P and the second based on Moody's

1 Electric Utility Index. The S&P list (Company Exhibit RAM-4, Page 1 of 4)
2 includes all kinds of distribution utility companies, however, only about 20 are
3 electric and combination electric and gas utilities, while the rest are gas only
4 and water companies. The Moody's list also has 20 electric and combination
5 electric and gas utilities. Next, Dr. Morin excludes companies from the lists
6 provided by S&P and Moody's based on the following criteria: foreign
7 companies and those with bond ratings below BBB-; companies without Value
8 line coverage; and companies with less than 50% of revenues from regulated
9 operations. As shown in Company Exhibits RAM-5 and RAM-7, after applying
10 the criteria established by Dr. Morin, the S&P based proxy group is reduced
11 to 12 companies and the Moody's based proxy group is reduced to 15
12 companies.

13

14 Q. Please comment on Dr. Morin's selection of proxy groups.

15 A. Dr. Morin does not explain why he starts the selection of the proxy groups with
16 lists of utilities provided by S&P and the Moody's. Moreover, he does not offer
17 an explanation as to the criteria used by S&P or Moody's for inclusion in their
18 lists. It appears that the selection of companies included in Dr. Morin's proxy
19 groups is completely arbitrary. The proxy groups have included some utilities
20 while excluding others without any proper basis. If Dr. Morin had applied his
21 own criteria to all the electric and combination electric and gas utilities for

1 which Value Line provides data, he would have included an additional 30
2 electric and combination electric and gas utilities to his S&P based proxy group
3 and 27 additional companies to his Moody's based proxy group. All the
4 companies that were left out of his proxy groups meet his own criteria for
5 inclusion in the proxy group; they all have investment grade rating, they all
6 have Value Line coverage and they all have more than 50% revenues from
7 regulated operations.

8

9 Q. Are you suggesting that Dr. Morin should have included all the 30 companies
10 he left out of his S&P based proxy group and all the 27 companies he left out
11 of the Moody's based proxy group?

12 A. Yes. Based on his own criteria, he should have included all these companies
13 in his proxy group. However, some of the companies should not be included
14 based on additional criteria that most analysts use. For instance, as discussed
15 above, I excluded four companies that were either involved in a merger, did not
16 pay a dividend, are a transmission only company or whose debt was not rated
17 by both Moody's and S&P. Additionally, Dr. Morin and I have used different
18 criteria regarding the level of revenues derived from regulated operations for
19 inclusion in the proxy group. I have used at least 70% of revenues from
20 regulated operations as a basis of inclusion in the proxy group, while Dr. Morin
21 has used 50%.

1 Applying the additional criteria I have used in excluding companies from
2 the proxy group (resulting in excluding an additional four companies discussed
3 above) and applying a screen for regulated utility operations, similar to the one
4 I used, i.e., exclude companies with under 70% regulated utility revenues,
5 would still leave 20 companies meeting Dr. Morin's other two criteria and
6 should be included in his S&P based proxy group. Similarly, 17 companies
7 would still meet Dr. Morin's criteria, after applying the additional criteria I used
8 and the 70% screen for regulated utility operations, and should be included in
9 his Moody's based proxy group.

10

11 Q. Going back to Dr. Morin's original proxy groups of 12 S&P based and 15
12 Moody's based companies; did you find other problems with this selection?

13 A. Yes. Both of his proxy groups include Energy East Corporation which is
14 potentially slated to be acquired by Iberdola SA and should be excluded from
15 the proxy groups.

16

17 Q. What is your conclusion regarding Dr. Morin's proxy group selection?

18 A. As shown above, the selection of Dr. Morin's proxy groups is arbitrary. Instead
19 of establishing a selection criteria and then applying it across the electric utility
20 industry, he started with specified lists of companies used by S&P and
21 Moody's that excluded more companies than they included based on his own

1 criteria of being investment grade, having Value Line coverage and meeting a
2 threshold for revenues from regulated operations. In contrast, the process
3 established in the Generic Finance Case and used by the CPB is based on the
4 logic of starting with all electric and combination electric and gas utilities and
5 than applying an agreed upon criteria to all those companies to arrive at a
6 reasonable proxy group. There seems to be no rational basis for excluding
7 certain utilities from Dr. Morin's proxy group. For instance FPL Group, Inc. with
8 a very similar rating as Consolidated Edison ("A2" by Moody's and "A" by S&P
9 for FPL Group, Inc. versus "A2" by Moody's and "A-" by S&P for Consolidated
10 Edison) and a relatively similar percentage of revenues from regulated
11 operations (76.1% for FPL Group, Inc. versus 82.5% for Consolidated Edison)
12 was excluded from both of Dr. Morin's proxy groups. Similarly, NSTAR,
13 another utility with relatively similar bond rating and level of revenues derived
14 from regulated operations as Consolidated Edison, is included in the S&P
15 based proxy group but excluded from the Moody's based proxy group. The
16 only possible explanation for excluding these companies is that they were not
17 included in the initial list provided by S&P and Moody's. This begs the
18 question as to the criteria used by S&P and Moody's for inclusion in their lists.
19 Since the formation of Dr. Morin's proxy groups are completely arbitrary and
20 lacking in logical basis, the application of DCF and CAPM methods to these
21 proxy groups leads to unreliable results.

1 Q. Please briefly describe Dr. Morin's DCF analysis.

2 A. Dr. Morin uses a single-stage model to perform four separate DCF analyses.
3 He uses two different proxy groups and two different estimates of growth rates
4 to perform these analyses. His first proxy group, based on companies
5 designated as distribution utilities by S&P (S&P based proxy group), is
6 composed of 12 electric utilities, while his second proxy group based
7 companies in the Moody's Electric Utility Index (Moody's based proxy group) is
8 composed of 15 companies. For both proxy groups, Dr. Morin estimates the
9 DCF equity return alternatively using Value Line estimates of earnings per
10 share growth and Zack's long-term earnings growth estimates. For the S&P
11 based proxy group he estimates returns of 11.4% and 11.6% for the Value
12 Line and Zack based growth rates respectively. For the Moody's based proxy
13 group, Dr. Morin estimates DCF equity returns of 11.0% and 11.6% for the
14 Value Line and Zack based growth rates, respectively. The average of his four
15 different DCF equity cost estimates is 11.4%.

16

17 Q. Please comment on the Company's DCF analysis.

18 A. Dr. Morin's DCF analysis is similar to the one he presented in the Company's
19 last proceeding (Case 07-E-0523). He relies on analysts' long-term forecasts
20 of earnings growth instead of expected dividend growth. Alternatively applying
21 Value Line and Zack's earnings growth forecasts to S&P and Moody's based

1 proxy groups, Dr. Morin arrives at four different DCF equity cost estimates.
2 The Judge in rejecting Dr. Morin's approach in the Company's last proceeding
3 said the following:

4 We do not find any need in this case to adopt any alternatives or
5 variants for the components [of] the DCF and the CAPM
6 methods. We believe that the Commission should adhere to the
7 calculation of these methods as specified in the Generic
8 Finance Case. (Case 07-E-0523, Recommended Decision,
9 p.134-135.)
10

11 The Commission in upholding the Recommended Decision said the
12 following:

13 We find no merit in Con Edison's claim that the DCF method
14 and the Generic Finance Case approach are flawed and should
15 not be used without an upward adjustment applied to the
16 indicated equity return allowance.
17

18 * * *

19 We are satisfied that the DCF method remains a valid and
20 proper method in these circumstances and we are not inclined
21 to modify it for the reasons presented by Con Edison. (Case
22 07-E-0523, Order Establishing Rates for Electric Service,
23 p.123.)
24
25

26 Q. Is Dr. Morin's DCF analysis consistent with that adopted in the Recommended
27 Decision in the Generic Finance Case?

28 A. No. Dr. Morin's DCF analysis makes a major departure from the methodology
29 specified in the Generic Finance Proceeding. Dr. Morin rejects the use of the
30 two-stage DCF model as recommended in the Generic Finance Case and

1 consistently relied upon by the Commission and instead uses a single-stage,
2 DCF model. He discusses at length why he uses analysts' forecasts of growth
3 contained in Zack's Investment Research, Inc. and Value Line while rejecting
4 other measures of growth like sustainable growth. The question of whether to
5 use a single-stage or two-stage DCF model along with numerous other issues,
6 many of which have been raised by Dr. Morin, were discussed in great detail in
7 the Generic Finance Proceeding and a consensus methodology was agreed
8 upon. After considering other methods, Dr. Stewart Myers of MIT concluded
9 the following:

10 Dr. Myers concluded that if dividend growth is expected to vary
11 in the future, rather than remain constant, then the simplifying
12 assumption that underlies the constant growth DCF model does
13 not work. Hence, the single stage DCF model overestimates the
14 cost of equity if immediate and near term growth is temporarily
15 high, and underestimates the cost of equity if immediate and
16 near term growth is temporarily low.

17 * * *

18
19
20 The Myers Report concluded that for companies that have not
21 settled into steady state, there is no general rule for choosing
22 the most accurate growth rate forecasting method. He did note,
23 however, that the use of a two-stage DCF, or even a long form
24 variable growth dividend discounting model could do a better job
25 of capturing this type of situation than a single-stage model.
26 Therefore, errors in estimated investors' forecasts of future
27 growth are inevitable, and will occur even if all the DCF
28 method's assumptions are satisfied.

29
30 (Return on Equity Consensus Document, issued June 2, 1993,
31 Appendix A at 3, 4.)
32

1 Overall, all of Dr. Morin's DCF estimates are overstated and should be
2 rejected.

3

4 Q. Please comment further on the Company's DCF approach.

5 A. I have previously discussed in detail the problems with the formation of the
6 proxy groups used by the Company to estimate its cost equity. In applying the
7 DCF method to these proxy groups, Con Edison enhances the problem by
8 arbitrarily dropping more companies from its proxy group. The Company starts
9 its DCF analysis based on the S&P based proxy group with 12 companies.
10 While estimating the DCF return using the Value Line earnings growth rate it
11 drops Northeast Utilities from the proxy group results because its growth rate is
12 unsustainable. While using Zack's forecast of growth it drops Public Service
13 Enterprise Group instead of Northeast Utilities from the proxy group because
14 of unsustainable growth projections along with two more companies, CH
15 Energy Group and East Energy Corporation, because of the unavailability of
16 growth projections. Its final DCF estimate using the Zack growth forecast is
17 based on a proxy group of only 9 companies. Similarly, it starts its DCF
18 analysis based on the Moody's based proxy group with 15 companies using
19 the Value Line's projection of earnings growth rate. However, in using the
20 Zack's forecast of growth, it again drops two utilities, CH Energy Group and
21 Energy East Corporation from its proxy group and also Public Service

1 Enterprise Group for an unsustainable growth rate. Its final estimate using the
2 Zack growth forecast for the Moody's based proxy group has only 12
3 companies.

4 As a result of arbitrarily dropping companies, Dr. Morin's four DCF
5 estimates are based on proxy groups of different sizes and composed of
6 different companies. In some cases he drops companies based on
7 unsustainable growth rates only to include them in another proxy group. In
8 setting up his proxy groups, he used the availability of Value Line data as one
9 of the criteria for inclusion. However, in his analysis using the Zack's based
10 growth rates, he drops companies that have Value Line data. In sum, it
11 appears that Dr. Morin's analysis is result driven rather than based on a logical
12 criteria applied uniformly throughout the analysis.

13

14 Q. Please comment on Dr. Morin's flotation cost allowance.

15 A. Company witness Dr. Morin adds 20 and 30 basis points flotation cost
16 adjustment to his four DCF equity cost estimates and 30 basis points to his two
17 CAPM equity cost estimates. There are two problems with this approach.
18 First, there is no reason why Dr. Morin computes two different amounts for
19 issuance costs, i.e., 20 and 30 basis points added to the DCF estimates and
20 30 basis points added to the CAPM estimates. Second, issuance costs should
21 be permitted when they are incurred based on the amount of issuance and not

1 on an on-going basis. The Commission in Cases 02-E-0198 and 02-G-0199
2 said the following:

3 We agree with the Judge's recommendation to exclude a
4 separate adjustment for selling and issuance costs, because our
5 policy has been to allow recovery of such expenses when they
6 are incurred ... (Order issued March 7, 2003, p. 71))
7

8 I recommend that the Commission not allow a flotation cost adjustment
9 in the manner proposed by Dr. Morin.

10

11 Q. Please briefly describe Dr. Morin's CAPM analysis.

12 A. Dr. Morin estimates two sets of equity returns based on the traditional and
13 zero-beta CAPM approaches. For risk premium, he uses 7.6% as an average
14 of an Ibbotson Associates based calculation and a DCF analysis applied to the
15 aggregate equity market using Value Line data. For the risk free rate, Dr.
16 Morin uses the U.S. Treasury 30-year bond yield of 4.5% for April 2008.
17 Finally, for beta he uses .82, the average of the two proxy groups that he has
18 utilized for his DCF analysis. Based on these inputs, Dr. Morin computes a
19 traditional CAPM of 10.70% and an empirical or Zero-Beta CAPM of 11.1%.
20 He adds 30 basis points for flotation to these estimates to arrive at final
21 estimates of 11.0% and 11.4% for the traditional and zero-beta CAPM with an
22 average CAPM estimate of 11.2%.

23

1 Q. Do you agree with Dr. Morin's CAPM analysis?

2 A. No. Dr. Morin's risk premium of 7.6% is the average of a 7.1% Ibbotson
3 Associates and an 8.1% DCF derived risk premium. His first risk premium of
4 7.1% is taken from the Ibbotson Associates study, Stocks, Bonds, Bills and
5 Inflation, 2008 Yearbook, and is based on the spread between common stock
6 returns and the income component of returns on long-term government bonds.
7 Since risk premium is the difference between market return and the risk free
8 rate, Dr. Morin's assumed market return is 11.6% based on the risk free rate of
9 4.5% he used in his CAPM analysis. Although I do not agree with the use of
10 Ibbotson Associates study, the Company's assumed estimate of market return
11 to derive the risk premium is not very different from the 11.4% market return
12 reported by Merrill Lynch in its August 11, issue of Quantitative Profiles –
13 Monthly Insight for Equity Management. In previous cases however, the risk
14 premium derived by using this method has been too high indicating that it is
15 based on an unreasonable assumed market return. For instance, the
16 Company's estimate of market premium in its last proceeding was based on
17 an assumed market return of 11.9% that was 100 basis points above the
18 10.9% market return reported by Merrill Lynch for both the S&P 500 and 1,168
19 firms as reported in its August 10, 2007 issue of Quantitative Profiles –
20 Monthly Insight for Equity Management.

21 I recommend that even though the risk premium derived from the

1 Ibbotson Associates study is relatively close to the market risk premium based
2 on the Merrill Lynch market return in this instance, that it not be relied upon.
3 The Commission in Case 95-G-1034, Central Hudson Gas & Electric
4 Corporation, said the following:

5 ...the Judge's market return calculation based on Merrill Lynch
6 estimate is a reasonable method of deriving a risk premium; and
7 it avoids the problems of stale data in the Ibbotson estimate, or
8 the circularity of the implied risk premium approach in relying on
9 other commissions' return allowances (Opinion No. 96-28,
10 October 3, 1996, p. 14)

11
12 Second, Dr. Morin estimates a risk premium of 8.1% based on a DCF
13 analysis applied to the aggregate equity market using Value Line aggregate
14 stock market index and growth forecasts. The assumed market return
15 underlying Dr. Morin's 8.1% risk premium derivation is completely unrealistic.
16 Given a risk premium of 8.1% and a risk free rate of 4.5%, the underlying
17 market return assumed by Dr. Morin is 12.6%. As stated above, the market
18 return reported by Merrill Lynch for 1,162 firms as reported in its August 11,
19 2008, issue of Quantitative Profiles – Monthly Insight for Equity Management is
20 11.4%. Merrill Lynch's estimate of market return for the S&P 500 is 11.5%. In
21 other words, Dr. Morin's estimate of market return of 12.6% is 120 basis points
22 higher than the estimate of 11.4% provided by Merrill Lynch. The inputs to the
23 CAPM formula are clearly excessive resulting in equity returns that are also
24 excessive and unrealistic.

1 Q. Are there other flaws in Dr. Morin's CAPM analysis?

2 A. Yes. Dr. Morin has not used the approach recommended in the Generic
3 Finance Case and relied upon by the Commission for computing the risk free
4 rate. The Generic Finance Case recommended an average of 10-year and
5 30-year Treasury bond yields over a six-month period as the basis for
6 computing the risk-free rate. Dr. Morin used only the 30-year Treasury bond
7 yield over a single month (April 2008) as the basis of his risk free rate.
8 Although the risk free rate of 4.5% used by Dr. Morin is the same as my six-
9 month estimate of 30-year bond yields, ignoring the 10-year bond yield of
10 3.82% instead of averaging the two estimates, as recommended in the
11 Generic Finance Case, leads to an inflated estimate of the risk free rate. I
12 recommend that the Commission reject his sole reliance on the 30-year bond
13 yield.

14

15 Q. Please comment on the Risk Premium approach used by Dr. Morin.

16 A. The Commission has repeatedly rejected the use of the Risk Premium
17 approach as used by Dr. Morin. In Cases 94-G-0885 and 93-G-0765, the
18 Commission referenced the Recommended Decision and rejected the risk
19 premium approach:

20 ... the Judge rejected two additional methods: the company's
21 risk premium approach (whose results he deemed too volatile),
22 and comparable earnings (presented by staff because it was

1 included in the generic finance case consensus proposal).
2

3 Opinion No. 95-16, National Fuel Gas Distribution Corporation,
4 issued September 15, 1995, page 44.
5
6

7 More recently, in Case 05-E-1222, the Recommended Decision that
8 was adopted by the Commission said the following:

9 To begin, we find that, to the extent that the Company had
10 departed from the generally accepted approach produced by the
11 Generic Finance Case, it has not advanced the consideration of
12 such matters in this proceeding. We recommend that very little
13 weight, if any, be given to NYSEG's risk premium analyses and
14 comparable earnings analysis that clearly depart from the
15 Generic Financing Case approach. We also recommend that the
16 Commission continue to use the DCF and CAPM methods as its
17 principal means to determine the allowed equity returns for the
18 utility companies it regulates.
19

20 (Recommended Decision at 62, 63.)
21

22 PART II – RATE DESIGN

23 Q. Please briefly describe the Company's proposal regarding the customer
24 charge for Service Classification ("SC") 1 – Residential & Religious Electric
25 Service and SC 7 – Residential & Religious – Space or Space and Water
26 Heating.

27 A. Con Edison is proposing to increase the SC1 and SC7 customer charge for
28 electric service by approximately 20 percent. Under the Company's proposal,
29 the customer charge for SC 1 and SC7 will increase by \$2.48 per month from
30 the current charge of \$12.42 to a proposed charge of \$14.90. On an annual

1 basis, residential customers will pay an additional \$29.76 for electric service as
2 a result of this customer charge increase under the Company's proposal.

3

4 Q. Do you agree with the Company's proposal?

5 A. No. There is no reason why the customer charge should be increased. The
6 current customer charge of \$12.42 per month is above the customer cost for
7 serving SC1 customers. According to the Company's latest Embedded Cost of
8 Service (ECOS) study, the customer cost for SC1 is \$12.20 per month.

9 If the Commission does not adopt my recommendation, I would
10 alternatively propose that the Commission increase the SC1 and SC7
11 customer charge, other than that of low-income customers, by no more than
12 the overall percentage increase that it grants the Company. This is what the
13 Commission did in the Company's last proceeding.

14

15 Q. Isn't it true that the customer cost for SC7 is higher?

16 A. Based on the Company's ECOS, the customer cost for SC7 is \$17.37 per
17 month. This is higher than the Company's proposed customer charge of
18 \$14.90 per month for SC1 and SC7 customers. Although, there may be good
19 reasons for having the same rates for both SC1 and SC7, since they are both
20 residential customers, one cannot justify an increase to SC1 that has 2.6

21

1 million customers, based on the need for parity with SC7 that has only 16
2 thousand customers.

3

4 Q. What is your proposal regarding the SC1 and SC7 customer charges?

5 A. I propose that the SC1 and SC7 customer charge not be increased since the
6 current charge of \$12.42 is above the SC1 customer cost of \$12.20.

7

8 Q. Does this conclude your testimony?

9 A. Yes.

EXHIBIT __ (TNN)
SCHEDULES 1 and 2

CONSOLIDATED EDISON COMPANY OF NEW YORK

Two-Stage DCF Growth Model

(PROXY GROUP OF COMBINATION ELECTRIC & GAS UTILITIES)

COMPANY NAME	BETA	6 MONTH PRICE *	Dividends Per Share				11-13 (=2012)	08/09	09/10	10/11	11/12
			2008	2009	2010	2011					
		(A)	(B)	(C)	(C')	(C'')	(D)	(D')	(D'')	(D''')	(D''''')
ALLETE, Inc.	0.90	40.75	1.72	1.80	1.86	1.93	2.00	1.76	1.83	1.90	1.97
Alliant Energy	0.80	35.87	1.40	1.53	1.65	1.78	1.92	1.47	1.59	1.72	1.85
Ameren Corporation	0.80	43.78	2.54	2.54	2.54	2.54	2.54	2.54	2.54	2.54	2.54
American Elec Power Co., Inc.	0.85	42.19	1.67	1.80	1.98	2.18	2.40	1.74	1.89	2.08	2.29
Avista Corp.	0.90	20.46	0.69	0.78	0.89	1.01	1.15	0.74	0.83	0.95	1.08
Cleco Corporation	1.00	24.03	0.90	0.90	1.07	1.27	1.50	0.90	0.98	1.17	1.38
Consolidated Edison, Inc.	0.75	40.91	2.34	2.36	2.38	2.40	2.42	2.35	2.37	2.39	2.41
DPL Inc.	0.80	26.90	1.10	1.16	1.22	1.28	1.34	1.13	1.19	1.25	1.31
DTE Energy Company	0.80	41.96	2.12	2.12	2.18	2.24	2.30	2.12	2.15	2.21	2.27
Duke Energy Corporation	NMF	18.01	0.90	0.94	0.98	1.02	1.06	0.92	0.96	1.00	1.04
Edison International	0.90	51.24	1.24	1.34	1.43	1.53	1.64	1.29	1.39	1.48	1.59
Empire District Elec. Co.	0.85	20.56	1.28	1.28	1.32	1.36	1.40	1.28	1.30	1.34	1.38
Energy Corporation	0.85	112.79	3.20	3.60	3.96	4.36	4.80	3.40	3.78	4.16	4.58
FPL Group, Inc.	0.80	64.84	1.78	1.92	2.05	2.19	2.34	1.85	1.99	2.12	2.27
FirstEnergy	0.80	74.87	2.25	2.45	2.64	2.84	3.05	2.35	2.54	2.74	2.94
Hawaiian Elec. Industries, Inc.	0.75	24.47	1.24	1.24	1.26	1.28	1.30	1.24	1.25	1.27	1.29
IDACORP, Inc.	0.90	31.06	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20	1.20
MGE Energy, Inc.	0.95	33.81	1.43	1.45	1.47	1.48	1.50	1.44	1.46	1.47	1.49
NiSource Inc.	0.90	17.81	0.92	0.92	0.95	0.97	1.00	0.92	0.93	0.96	0.99
Northeast Utilities	0.75	26.07	0.83	0.88	0.93	0.98	1.03	0.86	0.90	0.95	1.00
NSTAR	0.80	32.32	1.43	1.53	1.63	1.74	1.85	1.48	1.58	1.68	1.79
PG&E Corporation	0.85	39.11	1.56	1.68	1.79	1.91	2.04	1.62	1.74	1.85	1.98
Pinnacle West Capital Corp.	0.80	34.47	2.10	2.12	2.18	2.24	2.30	2.11	2.15	2.21	2.27
Portland General Electric Co.	0.80	23.46	0.97	1.01	1.07	1.13	1.20	0.99	1.04	1.10	1.17
Progress Energy	0.80	42.50	2.47	2.49	2.51	2.53	2.55	2.48	2.50	2.52	2.54
P.S. Enterprise GP.	0.90	46.86	1.29	1.41	1.49	1.57	1.65	1.35	1.45	1.53	1.61
Southern Company	0.70	35.83	1.66	1.73	1.82	1.91	2.00	1.70	1.77	1.86	1.95
Teco Energy, Inc.	0.95	17.93	0.80	0.82	0.85	0.87	0.90	0.81	0.83	0.86	0.89
Vectren Corporation	0.90	28.33	1.31	1.35	1.39	1.43	1.47	1.33	1.37	1.41	1.45
Wisconsin Energy Corp.	0.80	45.65	1.08	1.24	1.35	1.47	1.60	1.16	1.29	1.41	1.53
Xcel Energy	0.80	20.55	0.94	0.97	1.00	1.03	1.06	0.96	0.98	1.01	1.04

PROXY GROUP
SUMMARY STATISTICS

# of Companies	31	31	31	31	31	31	31	31	31	31	31
AVERAGE	0.81	37.40	1.50	1.57	1.65	1.73	1.82	1.53	1.61	1.69	1.78
STANDARD DEVIATION	0.16	19.07	0.60	0.64	0.72	0.77	0.78	0.66	0.70	0.74	0.80
MINIMUM	0.00	17.81	0.69	0.78	0.00	0.00	0.90	0.00	0.00	0.00	0.00
MAXIMUM	1.00	112.79	3.20	3.60	3.96	4.36	4.80	3.40	3.78	4.16	4.58

SOURCE: Value Line Investment Survey
May 30, 2008
June 27, 2008
August 8, 2008

* February 2008 to July 2008

COMPANY NAME	Earnings Per Share			BVPS			SHARES			DPS	2012
	2008	2009	11-13	2008	2009	11-13	2008	2009	11-13	GROWTH	RET
	(E)	(F)	(G)	(H)	(I)	(J)	(K)	(L)	(M)	(N)	(O)
ALLETE, Inc.	2.85	2.95	3.25	25.60	27.10	32.50	32.30	33.60	36.50	3.84%	38.46%
Alliant Energy	2.75	2.90	3.30	25.75	27.15	31.95	111.00	112.00	119.00	8.22%	41.82%
Ameren Corporation	3.10	3.25	3.55	33.20	34.05	37.40	210.00	212.00	222.00	0.00%	28.45%
American Elec Power Co., Inc.	3.30	3.50	4.25	27.35	29.20	35.00	404.00	407.00	415.00	9.49%	43.53%
Avista Corp.	1.45	1.55	1.75	18.20	19.00	21.25	54.00	55.00	56.50	13.62%	34.29%
Cleco Corporation	1.65	1.80	2.50	17.75	18.75	21.75	61.00	62.00	65.00	13.62%	40.00%
Consolidated Edison, Inc.	3.05	3.20	3.55	34.35	35.30	38.65	280.00	282.00	288.00	0.84%	31.83%
DPL Inc.	2.10	2.20	2.35	8.40	9.45	12.50	112.00	112.00	112.00	5.06%	42.98%
DTE Energy Company	2.65	3.20	3.75	36.70	37.80	41.75	163.25	163.25	163.25	2.06%	38.67%
Duke Energy Corporation	1.30	1.35	1.50	17.20	17.65	19.00	1262.00	1267.00	1285.00	4.18%	29.33%
Edison International	3.80	4.00	4.50	28.45	31.10	39.45	326.00	326.00	326.00	7.24%	63.56%
Empire District Elec. Co.	1.50	1.60	2.00	16.70	16.95	18.25	37.00	37.50	37.50	2.27%	30.00%
Entergy Corporation	6.60	7.20	9.00	42.20	48.00	62.25	187.00	193.00	199.00	10.67%	46.67%
FPL Group, Inc.	3.85	4.20	5.10	28.30	30.95	39.65	412.00	416.00	428.00	7.08%	54.12%
FirstEnergy	4.30	5.10	6.75	31.50	34.15	44.25	304.85	304.85	304.85	7.90%	54.81%
Hawaiian Elec. Industries, Inc.	1.10	1.65	2.00	15.10	15.40	17.00	85.50	87.50	89.00	1.19%	35.00%
IDACORP, Inc.	2.05	2.15	2.25	27.05	27.50	28.90	46.40	47.70	51.60	0.00%	46.67%
MGE Energy, Inc.	2.45	2.50	2.75	19.80	20.65	21.05	23.00	23.00	25.00	1.20%	45.45%
NiSource Inc.	1.25	1.25	1.50	18.45	18.80	20.25	275.50	276.00	277.50	2.11%	33.33%
Northeast Utilities	1.80	1.95	2.40	19.75	21.55	25.80	158.20	178.00	192.00	5.55%	57.08%
NSTAR	2.25	2.35	3.00	16.80	17.60	20.75	106.81	106.81	106.81	6.65%	38.33%
PG&E Corporation	2.95	3.20	3.50	24.10	25.70	28.95	381.00	384.00	393.00	6.94%	41.71%
Pinnacle West Capital Corp.	2.80	2.90	3.15	35.85	36.60	39.10	100.70	100.90	101.50	2.30%	26.98%
Portland General Electric Co.	1.80	2.00	2.25	21.90	23.05	26.00	62.60	71.00	76.00	5.46%	46.67%
Progress Energy	3.00	3.10	3.40	33.05	33.30	35.75	264.00	268.00	280.00	0.80%	25.00%
P.S. Enterprise GP.	2.90	3.15	3.45	16.10	18.00	23.75	510.00	512.00	518.00	6.35%	52.17%
Southern Company	2.35	2.50	3.00	17.30	18.45	21.75	777.00	793.00	815.00	4.77%	33.33%
Teco Energy, Inc.	0.95	1.25	1.50	9.75	10.20	12.00	212.00	213.00	216.00	2.99%	40.00%
Vectren Corporation	1.85	1.95	2.05	17.45	18.00	19.30	81.00	81.20	81.80	2.92%	28.29%
Wisconsin Energy Corp.	2.80	3.25	4.25	27.95	29.65	36.00	117.00	117.00	117.00	10.33%	62.35%
Xcel Energy	1.50	1.55	2.00	15.25	15.90	18.50	430.00	432.00	438.00	3.05%	47.00%
PROXY GROUP											
SUMMARY STATISTICS											
# of Companies	32	31	31	31	31	31	31	31	31	31	31
AVERAGE	2.44	2.73	3.21	23.46	24.74	28.72	244.75	247.56	252.77	5.12%	41.22%
STANDARD DEVIATION	1.19	1.23	1.55	8.19	8.78	10.90	250.88	252.33	256.36	3.75%	10.17%
MINIMUM	0.00	1.25	1.50	8.40	9.45	12.00	23.00	23.00	25.00	0.00%	25.00%
MAXIMUM	6.60	7.20	9.00	42.20	48.00	62.25	1262.00	1267.00	1285.00	13.62%	63.56%

COMPANY NAME	2012							SUSTAINABLE		LONG FORM	
	AVE	B*R	IN	CURRENT	S	V	SV	GROWTH	ROE	SORTED	
	ROE		SHARES	MBR	FACTOR	FACTOR	FACTOR	RATE			
	(P)	(Q)	(R)	(S)	(T)	(U)	(V)	(W)	(X)	(Y)	
ALLETE, Inc.	10.30%	3.96%	3.10%	159.18%	4.94%	37.18%	1.84%	5.80%	9.89%	7.51%	
Alliant Energy	10.61%	4.44%	1.76%	139.30%	2.44%	28.21%	0.69%	5.13%	9.54%	7.64%	
Ameren Corporation	9.64%	2.74%	1.40%	131.87%	1.84%	24.17%	0.45%	3.19%	8.52%	7.72%	
American Elec Power Co., Inc.	12.51%	5.45%	0.67%	154.26%	1.04%	35.17%	0.37%	5.81%	10.35%	7.74%	
Avista Corp.	8.39%	2.88%	1.14%	112.42%	1.28%	11.05%	0.14%	3.02%	7.74%	7.85%	
Cleco Corporation	11.78%	4.71%	1.60%	135.38%	2.17%	26.13%	0.57%	5.28%	10.09%	8.35%	
Consolidated Edison, Inc.	9.32%	2.97%	0.71%	119.10%	0.84%	16.04%	0.13%	3.10%	8.51%	8.36%	
DPL Inc.	19.68%	8.46%	0.00%	320.24%	0.00%	68.77%	0.00%	8.46%	12.29%	8.42%	
DTE Energy Company	9.13%	3.53%	0.00%	114.33%	0.00%	12.54%	0.00%	3.53%	8.42%	8.51%	
Duke Energy Corporation	7.99%	2.34%	0.45%	104.71%	0.47%	4.50%	0.02%	2.37%	7.72%	8.52%	
Edison International	11.86%	7.54%	0.00%	180.11%	0.00%	44.48%	0.00%	7.54%	10.00%	8.82%	
Empire District Elec. Co.	11.09%	3.33%	0.34%	123.11%	0.41%	18.77%	0.08%	3.41%	9.49%	9.43%	
Entergy Corporation	15.08%	7.04%	1.57%	267.27%	4.19%	62.59%	2.62%	9.66%	12.72%	9.49%	
FPL Group, Inc.	13.39%	7.25%	0.96%	229.12%	2.19%	56.35%	1.24%	8.48%	11.21%	9.54%	
FirstEnergy	15.91%	8.72%	0.00%	237.68%	0.00%	57.93%	0.00%	8.72%	11.77%	9.74%	
Hawaiian Elec. Industries, Inc.	11.96%	4.19%	1.01%	162.05%	1.63%	38.29%	0.63%	4.81%	9.43%	9.76%	
IDACORP, Inc.	7.85%	3.66%	2.69%	114.82%	3.09%	12.91%	0.40%	4.06%	7.51%	9.89%	
MGE Energy, Inc.	13.11%	5.96%	2.11%	170.76%	3.60%	41.44%	1.49%	7.45%	11.04%	9.90%	
NiSource Inc.	7.50%	2.50%	0.18%	96.53%	0.17%	-3.59%	-0.01%	2.49%	7.64%	10.00%	
Northeast Utilities	9.58%	5.47%	4.96%	132.00%	6.55%	24.24%	1.59%	7.06%	10.19%	10.09%	
NSTAR	14.85%	5.69%	0.00%	192.38%	0.00%	48.02%	0.00%	5.69%	10.38%	10.19%	
PG&E Corporation	12.33%	5.14%	0.78%	162.28%	1.26%	38.38%	0.48%	5.63%	9.90%	10.27%	
Pinnacle West Capital Corp.	8.14%	2.20%	0.20%	96.15%	0.19%	-4.00%	-0.01%	2.19%	8.35%	10.35%	
Portland General Electric Co.	8.83%	4.12%	4.97%	107.12%	5.32%	6.65%	0.35%	4.47%	8.82%	10.38%	
Progress Energy	9.62%	2.41%	1.48%	128.59%	1.91%	22.24%	0.42%	2.83%	8.36%	10.60%	
P.S. Enterprise GP.	15.20%	7.93%	0.39%	291.06%	1.13%	65.64%	0.74%	8.67%	11.34%	11.04%	
Southern Company	14.17%	4.72%	1.20%	207.11%	2.49%	51.72%	1.29%	6.01%	10.60%	11.21%	
Teco Energy, Inc.	12.84%	5.14%	0.47%	183.90%	0.86%	45.62%	0.39%	5.53%	9.76%	11.34%	
Vectren Corporation	10.75%	3.04%	0.25%	162.35%	0.40%	38.40%	0.15%	3.19%	7.85%	11.77%	
Wisconsin Energy Corp.	12.19%	7.60%	0.00%	163.33%	0.00%	38.77%	0.00%	7.60%	10.27%	12.29%	
Xcel Energy	11.08%	5.21%	0.46%	134.75%	0.62%	25.79%	0.16%	5.37%	9.74%	12.72%	
									MEDIAN	9.76%	
PROXY GROUP											
SUMMARY STATISTICS											
# of Companies	31	31	31	31	31	31	31	31	31	31	
AVERAGE	11.51%	4.85%	1.12%	162.36%	1.65%	32.08%	0.52%	5.37%	9.66%	9.66%	
STANDARD DEVIATION	2.76%	1.91%	1.28%	55.95%	1.71%	19.55%	0.64%	2.14%	1.38%	1.38%	
MINIMUM	7.50%	2.20%	0.00%	96.15%	0.00%	-4.00%	-0.01%	2.19%	7.51%	7.51%	
MAXIMUM	19.68%	8.72%	4.97%	320.24%	6.55%	68.77%	2.62%	9.66%	12.72%	12.72%	

CONSOLIDATED EDISON COMPANY OF NEW YORK

TRADITIONAL CAPM

Formula: $R_c = R_f + b (R_m - R_f)$

Where:

R_c = Required Return for the Company.

R_f = Risk Free Return = 4.18, six-month average ending July 2008 of 30-Year and 10-Year Treasury Bond Yields, Federal Reserve Statistical Release, (Historical Data).

R_m = Market Return = 11.4%, Quantitative Profiles-Monthly Insights for Equity Management, Merrill Lynch, (August 11, 2008).

b = Beta = .81, Proxy Group Average Beta for Combination Electric and Gas Utilities (The Value Line Investment Survey, Ratings and Reports, (May 30, 2008; June 27, 2008; August 8, 2008).

Required Return:

$$10.03\% = 4.18 + .81(11.4 - 4.18)$$

CONSOLIDATED EDISON COMPANY OF NEW YORK

ZERO-BETA CAPM

Formula: $R_c = R_f + 3/4(b) (R_p) + 1/4(R_p)$

Where:

R_c = Required Return for the Company.

R_f = Risk Free Return = 4.18%, six-month average ending July 2008 of 30-Year and 10-Year Treasury Bond Yields, Federal Reserve Statistical Release, (Historical Data).

R_m = Market Return = 11.4%, Quantitative Profiles-Monthly Insights for Equity Management, Merrill Lynch, (August 11, 2008).

b = Beta = .81, Proxy Group Average Beta for Combination Electric & Gas Utilities. (The Value Line Investment Survey, Ratings and Reports, (May 30, 2008; June 27, 2008; August 8, 2008).

R_p = Risk Premium = 7.22 Market Return minus Risk free rate.

Required Return:

$$10.37\% = 4.18 + .75(.81) (7.22) + .25(7.22)$$