STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Joint Petition of Iberdrola, S.A., Energy East Corporation, RGS Energy Group, Inc., Green Acquisition Capital, Inc., New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation for Approval of the Acquisition of Energy East Corporation by Iberdrola, S.A.	Case 07-M-0906

REPLY BRIEF

OF THE

NEW YORK STATE CONSUMER PROTECTION BOARD

Mindy A. Bockstein
Chairperson and Executive Director

Douglas W. Elfner
Director of Utility Intervention

David L. Prestemon
Intervenor Attorney

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Albany, New York

NYS CONSUMER PROTECTION BOARD
5 EMPIRE STATE PLAZA
SUITE 2101
ALBANY, NEW YORK 12223-1556
http://www.nysconsumer.gov

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As stated in our Initial Brief, the Consumer Protection Board ("CPB") believes that the evidence presented in this proceeding demonstrates that Iberdrola, S.A. ("Iberdrola") has the experience and expertise necessary to ensure that New York State Electric & Gas Corporation ("NYSEG") and Rochester Gas & Electric Corporation ("RG&E") will continue to provide safe and reliable service to New York consumers if Iberdrola's acquisition of Energy East Corporation (the "Proposed Transaction") is authorized by the Public Service Commission ("PSC" or "Commission").[1] Iberdrola also has the potential to contribute significantly to the State's efforts to develop renewable energy resources.

We also demonstrated in our Initial Brief that the concessions made by Joint Petitioners in their Partial Acceptance Document[2] were sufficient to resolve

[1] "Initial Brief of the New York State Consumer Protection Board," April 18, 2008, ("CPB Initial Brief").

[2] Exhibit 50.

any legitimate concerns with respect to the potential for the exercise of vertical market power by the combined companies. We concluded that approval of the Proposed Transaction need not be subject to conditions imposing restrictions on the development of wind generation by Iberdrola's affiliates that would be different from those applicable to any other transmission-owning utility.

In balancing the risks and benefits of the Proposed Transaction, however, we concluded that approval should be subject to specific conditions. Those conditions should ensure that ratepayers receive positive monetary benefits sufficient to compensate them for the risks posed by the merger, and should provide the full range of financial protections recommended by the Department of Public Service Staff ("DPS Staff").

Nothing in the initial briefs submitted by others has convinced us that our position should be modified. Accordingly, with the adoption of the conditions we recommended in our Initial Brief, the CPB recommends that the Proposed Transaction be deemed to be in the public interest pursuant to Section 70 of the Public Service Law.

SUMMARY

In this Reply Brief, we address a number of issues raised in the initial briefs of other parties that bear on the nature and scope of the conditions required for approval of the Proposed Transaction. Specifically, we argue that:

- The assertion that Iberdrola's active involvement in the development of wind generation would be a detriment to New York is completely unfounded.
- The character of the specific Positive Benefit Adjustments ("PBAs") identified by the DPS Staff is irrelevant to a determination of the overall level of benefits necessary to compensate ratepayers for the risks presented by the Proposed Transaction.
- Neither uncertainty associated with the receipt by Iberdrola of production tax credits, nor their underlying function as a stimulus for wind generation development justifies ignoring their value as a benefit of the Proposed Transaction.
- Any order approving the Proposed Transaction should require NYSEG and RG&E to file both gas and electric rate cases, and to show cause why rates should not be temporarily reset to capture the rate effect of approved PBAs and to address over-earning situations. The rate cases should not be unduly expedited either by shortening the normal schedule or by the Commission's adoption of significant rate plan elements based on the record in this proceeding.
- Revenue Decoupling Mechanisms ("RDM") for NYSEG and RG&E should not be adopted in this proceeding, but rather should be considered in conjunction with rate cases for both utilities.

ARGUMENT

A. Iberdrola's ownership and development of wind generation will be a benefit for New York.

DPS Staff contends that "Iberdrola's ownership and development of wind generation is a detriment, and not a benefit of this transaction."[3] The problem, it says, is that the company's operation of generating facilities will give Iberdrola the incentive to use its control over the transmission and distribution facilities of NYSEG and RG&E to favor its plants and disadvantage those of its competitors. In response, the competitors will either scale back their development efforts or pack their bags and leave the State.[4] The Commission, in the meantime, will be helpless to prevent the exodus because the exercise of vertical market power will be too subtle to detect and remedy.[5] In other words, the danger is that Iberdrola will engage in anticompetitive activity so notorious and disruptive that other wind generators will be dissuaded from doing business in New York, but so subtle that the NYISO, FERC and the Commission will all be incapable of addressing it.

The unreasonableness of this position is amply demonstrated by the fact that no other party to this case has taken such an extreme view of the risk of vertical market power. The only party in this case that directly represents the interests of wind generation developers, the Independent Power Producers of New York ("IPPNY"), does not ask that the Proposed Transaction be conditioned upon Iberdrola's divestiture of its existing wind generation, or a ban on further

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3 "Staff Initial Brief," April 11, 2008, p. 24 ("DPS Staff Initial Brief").

4 Id.

5 Id. pp. 94, 95, 102.

wind development by the company.[6] Both Multiple Intervenors, representing large customers, and the CPB, representing consumers, support the adoption by the Commission of vertical market power mitigation measures that will not inhibit further development of wind generation in New York by Iberdrola.[7]

B. Positive benefit adjustments need not be tied to specific accounting items.

Joint Petitioners berate DPS Staff for attempting to achieve tangible, positive benefits for ratepayers by proposing PBAs that "are unrelated to any claimed synergy savings resulting from the Proposed Transaction" and "would not be adopted if presented in a rate case."[8] The argument is completely irrelevant to the underlying issue, which is the amount of quantifiable benefit to be received by ratepayers that will be sufficient to compensate consumers for accepting the risks of the Proposed Transaction.

As it explained in its testimony, DPS Staff estimated the required benefit at $800 million based on its evaluation of the total benefits of the transaction accruing to all other parties.[9] The purpose of its effort to identify specific PBAs was to come up with a means of obtaining that amount through adjustments that would cause the fewest ratemaking issues for the utilities. Joint Petitioners seem

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6 IPPNY does seek a ban on development by Iberdrola within the service territories of NYSEG and RG&E, where the company currently has no wind facilities.

7 "Initial Brief of Multiple Intervenors," April 18, 2008, p. 58-59 ("MI Initial Brief"); CPB Initial Brief, p. 15.

8 "Initial Brief of Joint Petitioners Iberdrola, S.A. and Energy East Corporation," April 18, 2008, p. 33 ("Initial Brief of Joint Petitioners").

9 DPS Staff Initial Brief, p. 115.

to have no problem with that general approach, as they used the same methodology to select the line items necessary to fund the $201 million in PBAs they offered in their Partial Acceptance Document.[10]

If Joint Petitioners disagree with the PBAs chosen by DPS Staff, then they should simply offer a rate reduction that is tied either to other accounts or functions, or to nothing specific. There is precedent for the latter approach in the National Grid/KeySpan merger. In the Joint Proposal approved by the Commission in that case with modifications, there are line items in the enumeration of merger adjustments to the revenue requirements for both KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island that are labeled simply "Additional Margin Adjustment."[11] The adjustments on these lines total over $111 million.[12] They do not purport to be related to any specific accounts. Their sole purpose is to achieve the total agreed-upon rate benefits for consumers.

Positive benefits for ratepayers beyond those proposed by Joint Petitioners need to be identified in order to justify the Proposed Transaction in this case. Whether those come from the PBAs proposed by DPS Staff, or some other source identified by Joint Petitioners is not important. What matters is the amount. The CPB considers the $800 million recommended by DPS Staff to be

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10 CPB Initial Brief, p. 32.

11 Case 06-M-0878, et al., Joint Petition of National Grid PLC and KeySpan Corporation for Approval of Stack Acquisition and Other Regulatory Authorizations, "Merger & Gas Revenue Requirement Joint Proposal," July 6, 2007, Appendix 2, p. 8 and Appendix 3, p. 8 ("NG/KS Merger JP").

12 Id.

sufficient, but as we explained in our Initial Brief, the $201 million offered by Joint Petitioners in their Partial Acceptance Document is not.

C. Production tax credits for wind generation may properly be considered a synergistic benefit of the Proposed Transaction.

The evidence is overwhelming in this record that Iberdrola stands to benefit very substantially from the ability to make full use of wind power production tax credits that it will gain through the acquisition of Energy East.[13] Iberdrola itself touted this benefit of the Proposed Transaction in presentations to the press and financial analysts.[14] It is also an obvious consequence of the fact that, after the acquisition, Iberdrola's subsidiaries will be able to construct wind generation facilities without having to arrange to share the value of the credits with "tax equity partners."[15]

Synergy savings arise from "a mutually advantageous conjunction or compatibility of distinct business participants or elements (as resources or efforts)."[16] That is precisely what will happen here when the taxable earnings of NYSEG and RG&E are combined with the underutilized tax credits of Iberdrola's subsidiaries.

Joint Petitioners decry the fact that crediting some portion of the value of these credits to ratepayers ignores their underlying function, which is to promote

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13 CPB Initial Brief, pp. 22-23.

14 DPS Staff Initial Brief, p. 128 (citing Tr. 1553).

15 CPB Initial Brief, p. 22.

16 Definition of "synergy" from Merriam-Webster Online (http://www.m-w.com).

the development of wind generation.[17] At the same time, they deprecate the value of these credits by claiming that they have no trouble financing their projects currently, using tax equity partnerships as part of the funding package.[18] The simple fact is that after the Proposed Transaction, they will receive a greater portion of the total credit available than they previously did, even if ratepayers are compensated for a share of the savings realized. The production tax credits will, therefore, provide more, not less, of an incentive for wind power development than they currently do.

D. RG&E and NYSEG should be required to file both gas and electric rate cases immediately following any order approving the Proposed Transaction, and should be ordered to show cause why temporary rates should not be set to bridge the period between the expiration of existing rate plans and the setting of new rates.

The CPB fully agrees with the concern of the DPS Staff that new rates be established for NYSEG and RG&E, both to assure that any monetized benefits realized by ratepayers as a result of the Proposed Transaction are translated into lower bills for consumers, and to address over earning by the utilities.[19] Accordingly, we recommend that an order in this case approving the Proposed Transaction include a directive that NYSEG and RG&E file both electric and gas rate cases within 90 days. We disagree, however, with DPS Staff's suggestion that these rate cases be significantly expedited, either by accelerating the normal

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[17] Joint Petitioners Initial Brief, p. 39.

[18] CPB Initial Brief, p. 22.

[19] DPS Staff Initial Brief, p. 170, 176-177. It should be noted that the most recent earnings calculated by Staff for NYSEG electric and RG&E electric – 17.18% and 13.05% -- are far in excess of any ROE authorized by the Commission in recent years.

schedule for the conduct of such proceedings, or by carving out rate case issues for decision on the basis of the limited record in this case.

Handling four rate cases simultaneously will be a very difficult task for the DPS Staff. For intervening parties with more limited resources, it will require a very intense effort just to contribute effectively to the development of multiple records. Consequently, completing the cases in time to have new rates effective on expiration of the existing NYSEG and RG&E rate plans should not be a priority. As DPS Staff suggests, any gap between the expiration of the plans and the establishment of new rates could be filled through the adoption of temporary rates.[20] Indeed, the CPB would take that a step further. We recommend that a decision approving the Proposed Transaction include an order directed to each of NYSEG electric, NYSEG gas, RG&E electric and RG&E gas, to show cause why temporary rates should not be set to include the rate effect of any PBAs adopted, and to ameliorate the over earnings reflected in DPS Staff's analysis.[21]

The CPB also disagrees with the recommendation that the Commission should decide significant rate plan issues on the basis of the record in this case. DPS Staff points out that this is what the Commission did in the National Grid/KeySpan merger proceeding.[22] In that case, however, full rate cases were filed for both of KeySpan's New York utilities in conjunction with the Section 70

[20] DPS Staff Initial Brief, p. 172.

[21] As a corollary of this recommendation, the requests of NYSEG and RG&E to continue their existing rate plans beyond their December 31, 2008, expiration dates should be denied. See DPS Staff Initial Brief, p. 171.

[22] Id., p. 170.

petition. Rate plan issues were central to the proceeding from the beginning and were addressed by the CPB and other intervenors in direct testimony.

Here, no rate cases are pending, and rate-related issues such as gas cost incentive mechanisms, ESCO referral programs, advanced metering, outreach and education, low-income programs, and the like, first appeared in DPS Staff's testimony. All of these issues have an impact on both the level and design of rates, but they have never been central to this case, and have not received adequate analysis and development in the record through rebuttal testimony and cross-examination alone. These issues should be deferred for consideration to the post-transaction rate cases where they belong.

E. Revenue Decoupling Mechanisms for NYSEG and RG&E should not be adopted in this proceeding.

DPS Staff, Joint Petitioners and MI have all recommended that the Commission not attempt to adopt RDMs for NYSEG and RG&E in its order in this proceeding.[23] The CPB concurs fully with this recommendation. Proper design of these mechanisms is essential to assure that they operate fairly and do not cause major rate fluctuations for consumers. The development of these programs can be complex, requiring, as DPS Staff notes, rate case quality data.[24] In the National Grid/KeySpan merger proceeding, despite extensive negotiations that produced detailed multi-year rate plans, the development of RDMs for the

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[23] DPS Staff Initial Brief, p. 193-194; Initial Brief of Joint Petitioners, p.112; MI Initial Brief, p. 59-63.

[24] DPS Staff Initial Brief, p. 194.

KeySpan utilities was deferred to a separate collaborative.[25] Months later, that collaborative is still in progress.

Despite their agreement on deferring the RDM issue to subsequent proceedings, the parties differ somewhat on how the matter should be handled following a decision in this case. DPS Staff and Joint Petitioners would have RG&E and NYSEG file separate proposals to be considered in the latter half of this year.[26] MI urges that the Commission reaffirm its previous determination that RDMs should be considered within the context of rate proceedings, rather than separately.[27] The CPB believes that MI's view is the better one in this case.

As MI notes, the development of an RDM is inextricably entwined with both the setting and design of rates.[28] The data required for this effort is, as DPS Staff also points out, exactly that which the parties can expect to have available in a rate case. DPS Staff has called for the filing of rate cases for both RG&E and NYSEG promptly after a decision in this case, and the CPB supports that call. Incorporating RDM issues in those cases would not, therefore, delay their resolution at all. There is absolutely nothing to be gained by decoupling RDM from the underlying rate cases.

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25 NG/KS Merger JP, p. 3.

26 Id.; Initial Brief of Joint Petitioners, p. 112.

27 MI Initial Brief, p. 61-62.

28 Id.

CONCLUSION

The CPB recommends that the Proposed Transaction be approved by the Commission in an order that incorporates the conditions we have described in this filing and in our Initial Brief.

Respectfully submitted,

Mindy A. Bockstein

Mindy A. Bockstein
Chairperson and Executive Director

Douglas W. Elfner
Director of Utility Intervention

David L. Prestemon
Intervenor Attorney

Dated: Albany, New York
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