

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Proceeding on Motion of the Commission as to
the Rates, Charges, Rules and Regulations of
New York State Electric & Gas Corporation for
Electric Service

Case 05-E-1222

BRIEF ON EXCEPTIONS OF THE NEW YORK STATE
CONSUMER PROTECTION BOARD

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I. Statement of the Case

This case was initiated by a filing dated September 30, 2005, in which New York State Electric and Gas Corporation (“NYSEG” or “the Company”) requested permission to extend its existing rate plan for an additional six years with only minor substantive changes in most areas, but with a substantial increase electric delivery rates. The extension would permit continuation of NYSEG’s Voice Your Choice program under which consumers have the option of purchasing electricity from the Company, or from an energy service company (“ESCO”), on either a fixed or variable price basis. That program would otherwise expire at the end of this year.

NYSEG also proposed to mitigate the impact of the delivery rate increase by using previously collected funds and accelerating the benefits resulting from the expiration of contracts with certain non-utility generators (“NUGs”). As a result, the overall effect of the Company’s filing would be a reduction in delivery service bills.

On February 6, 2006, various parties, including the New York State Consumer Protection Board (“CPB”) submitted testimony recommending substantial downward

adjustments to the Company's proposed revenue requirement, and suggesting changes to the Voice Your Choice program ranging from minor modifications to complete elimination. NYSEG filed rebuttal testimony on February 21, 2006, in which it adopted a number of adjustments proposed by the parties and revised its delivery rate increase request downward to \$58.3 million.¹

Twelve days of evidentiary hearings were held in March and April before Administrative Law Judges William Bouteiller and Elizabeth H. Liebschutz ("ALJs"), following which some 14 parties, including the CPB, submitted briefs. Most of those parties also filed reply briefs.

On June 9, 2006, the Recommended Decision of the ALJs ("RD") was issued for exceptions by the Secretary to the Commission pursuant to 16 NYCRR § 4.10. The RD concludes that NYSEG's delivery rates should be reduced, rather than increased, by \$37.168 million, and that the Company's Voice Your Choice commodity program should be continued, but with significant modifications that will reduce the cost of the program to consumers and promote the Commission's policies on retail access.

II. Summary of Basic Position

The CPB commends the ALJs for what we consider to be an exceptionally thorough and thoughtful analysis of difficult, hotly contested and often complexly interrelated issues. Their conclusions reflect a fair and comprehensive analysis of the record evidence in this case. Particularly noteworthy is their recommendation regarding commodity options which is solidly based on the real world facts regarding retail competition in NYSEG's service territory. The resolution of the issues they have

¹ The original request was for an increase of \$91.2 million, subsequently updated to \$103.6 million.

addressed will have a very significant impact on the quality and cost of service received by customers in NYSEG's service territory in 2007 and beyond.

In general, the RD produces a result that, given the record developed in this case, is clearly within the range of outcomes that can be considered fair to both the Company and consumers. Our exceptions are directed at a handful of issues where we believe the RD is mistaken or unclear. Adoption of the recommendations we make here will, we believe, make an already sound decision better.

Specifically, we address the following issues:

- Apprenticeship Program. The RD improperly shifted the burden of proof to intervenors to show that increased funding of this program was not required, after the Company failed to present any evidence whatsoever to corroborate its claim that test year expenditures for the program should be adjusted upward.
- Hydroelectric Plant. The RD improperly included a rate allowance for the full amount of projected rate year expenses for certain hydroelectric plant repair and maintenance projects which were shown to be non-recurring. The expenses should be recovered ratably over the life of the projects.
- Productivity Adjustment. Although the productivity adjustment adopted by the RD reflects a reasonable methodology for including an allowance in rates for additional savings likely to be realized from merger-related programs, the size of the adjustment is clearly inadequate in light of the evidence presented by the CPB and the Department of Public Service staff ("Staff"), and the admissions of the Company.

- Asset Sale Gain Account (“ASGA”). Because the ASGA has become very large as a result of revenue sharing under NYSEG’s existing rate plan, the RD should have provided for a more rapid return of these funds to ratepayers than will be achieved by the recommended rate base offset. The Commission should direct the parties to collaborate on development of a fair and equitable methodology for allocating these funds among consumers of all rate classes. Funds allocable to residential customers should be retained to be utilized, as recommended by NYSEG, to mitigate the rate impact of a possible loss of low-cost NYPA power, given the currently scheduled termination NYPA power allocations in 2007.
- Fixed Price Commodity Offer. The recommendations of the RD should be clarified to assure that a fixed price commodity offer is available from the Company for all small, non-demand metered customers, whether residential or commercial.

III. Exceptions

A. Apprenticeship Program

The RD improperly shifts the burden of proof on this issue to intervenors when it states that, “Absent a clear demonstration that the ‘redundant staff’ is not needed for the specific purposes for which NYSEG plans to use them, a rate allowance should be provided.”² The Commission’s regulations, quite to the contrary, clearly impose upon the Company the obligation to make a “clear demonstration” that additional staff are needed before any rate allowance can be provided.³ That obligation cannot be met by

² RD, p. 16.

³ 16 NYCRR § 61.1.

“speculative or conjectural data” and any estimates or projections of future needs made by the Company “must be explained in detail.”⁴ In this case, NYSEG has not provided, and the RD is unable to cite, any detail whatsoever to support the Company’s conjecture that it will experience an abrupt increase in staffing requirements for its heretofore stable apprenticeship program.

The RD opines that, “It is not clear from the DPS Staff and CPB presentations that they have considered, as thoroughly as NYSEG, the Company’s need for a larger, current class of apprentices.”⁵ In fact, the CPB’s panel of witnesses performed a detailed analysis of the limited information available from NYSEG. They demonstrated that the level of employment in the positions for which the apprentices would be trained by the Company has been very stable (Tr. 3766), and that the apprenticeship positions that formed the basis for the proposed payroll adjustment had not been filled as scheduled in November 2005 (Tr. 3765). The RD, itself, acknowledged that the proposed increase in apprentice staffing for the rate year appeared “aberrational.”⁶

The CPB could not analyze the specific basis for the increased rate year apprentice staffing because the Company never provided any. DPS Staff asked NYSEG to “describe how the company derived the number of additional employees,” but all it received in response was a conclusory, wholly subjective statement that:

Management reviewed the current and projected staffing levels for each of the referenced positions in consideration of potential retirements. Based on the information, management determined the need for the identified

⁴ 16 NYCRR § 61.4.

⁵ RD, p. 16.

⁶ Id. Staff witness Haslinger testified that he, too, had found that employment levels for the positions to be filled by the apprentices had remained stable for several years. (Tr. 2362-2364)

number of apprentice employees to add by position to achieve a complement of qualified employees to match desired staffing levels.⁷

The “information” allegedly relied upon by “management” was never provided. The unnamed management decision-makers did not sponsor testimony describing or explaining the basis for their determination that an “aberrational” requirement for additional employees was imminent, and intervenor parties had no opportunity to cross-examine them.

The CPB fully understands the need for apprenticeship programs and the relationship between adequate staffing of those programs currently and the quality of service that consumers will receive in the future. Given a clear demonstration that such staffing was inadequate, we would not hesitate in supporting an increase in funding. On the record in this case, however, NYSEG has utterly failed to meet its burden of proof under the Commission’s regulations and the RD erred in concluding that the burden of disproving the need for a rate allowance had shifted to intervenors. The adjustment to revenue requirement of \$1,175,000 recommended by the CPB and Staff should be accepted.

B. Hydroelectric Plant

The RD erred in providing the full rate allowance requested by NYSEG for certain hydroelectric plant repair and maintenance projects when the uncontradicted evidence demonstrated that these projects were not recurring and were unlikely to be repeated for five, ten or more years. The allowance of \$675,000 covered projects which NYSEG stated were scheduled for the 2007 rate year and which included items such as repair

⁷ Hearing Exhibit 1, NYSEG Response No. 0116 to DPS-91.

and overhaul of turbines, concrete repairs to spillways and dams, and painting of exposed steel.⁸

The CPB's panel of witnesses testified that the description of these projects provided by NYSEG showed that the work to be performed was normal, routine maintenance that should have been performed historically by the Company and could not be considered a new obligation imposed by more stringent regulatory requirements. It was also clearly not of a type that would be recurring annually so as to justify a continuing allowance in rates. NYSEG's witnesses confirmed the CPB panel's assessment. On cross-examination, they acknowledged that the enumerated projects represented maintenance that NYSEG would normally perform (Tr. 441) and that some of those projects would be performed "on a ten-year cycle." (Id.)

No one has questioned the need for the repair and maintenance work proposed by NYSEG or the fact that it is scheduled to take place during the 2007 rate year. What the evidence demonstrates unequivocally, however, is that these projects will not be repeated in 2008, 2009 or, in some cases, any other year in the next decade.

Commission policy clearly requires that legitimately incurred, but non-recurring expenses be normalized for the rate year.⁹ This can be accomplished by recovering the cost ratably over the life of the project generating the expenditures.¹⁰ Most of the

⁸ Hearing Exhibit 1, NYSEG Response 0759 to information request CPB-4.

⁹ Case, 88-W-080, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of the Jamaica Water Supply Company for Water Service, Opinion No. 89-3, March 8, 1989, p. 27.

¹⁰ See, for example, Case 89-C-008, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of AuSable Valley Telephone Company for Telephone Service, Opinion No. 90-3, January 11, 1990, at p. 21, where the Commission found that in the absence of company evidence that a training expense would be recurring, the judge properly accepted Staff's recommendation that it be recovered over two years.

hydroelectric plant maintenance and repair projects for which NYSEG seeks a rate allowance were identified through inspections made every five years pursuant to FERC requirements or every ten years under Company procedures.¹¹ Accordingly, it would be reasonable to include an allowance in rates of one-fifth of the projected rate year expense of \$675,000, or \$135,000. Therefore, revenue requirement attributable to this line item should be adjusted downward by \$540,000.

C. Productivity Adjustment

The CPB recommended revenue requirement adjustments in four areas that can be characterized as efficiency savings derived from projects related to the NYSEG merger with Rochester Gas & Electric Corporation. First, in response to NYSEG's own representations that it had achieved an additional \$20 million in merger-related synergy savings in 2005, and expected further integration savings in 2006 through 2008 (Tr. 1984), we recommended that \$6.4 million in additional efficiency gains be imputed in rates. This number represented the difference between NYSEG's original estimate of merger savings and its most recent projection of actual savings. (Tr. 1985) Subsequently, when NYSEG reduced its savings projection, we increased our recommended adjustment to \$10.2 million.¹² Staff, using a similarly "holistic" approach, estimated additional savings of \$8.7 million.¹³

In addition, CPB witnesses attempted to assess efficiency savings not reflected in NYSEG's proposed revenue requirement by examining the impact of specific projects. As a result, they recommended adjustments related to the Work Management

¹¹ Hearing Exhibit 1, NYSEG Response 0759 to information request CPB-4.

¹² Reply Brief of the New York State Consumer Protection Board, p. 8.

¹³ RD, p. 36.

System, Integrated Back Office and Customer Care System projects totaling approximately \$7.5 million.

The RD agrees substantively with the positions of the CPB and Staff. It finds that NYSEG “provided a conservative quantification of savings” and “that it is reasonable to expect the Company to achieve more cost savings and greater efficiencies than were reflected in the September 2005 rate filing.”¹⁴ Consequently, it says, there is “ample basis” for applying a higher productivity factor than normal in setting NYSEG’s rates.¹⁵ It recommends a factor of 3%.

The CPB has no objection to using the productivity factor as the means for adjusting the Company’s revenue requirement to reflect projected efficiency savings, but based on extensive record evidence, the 3% factor chosen by the ALJs here is clearly inadequate. According to Appendix B, Schedule B, page 2, of the RD, this translates to an adjustment of just \$2.3 million, less than a third of even the lower of CPB’s estimates.

Such a minimal adjustment effectively, and unfairly, rewards NYSEG for its nearly complete failure to provide the types of cost-benefit analyses or studies of its merger-related projects that would have enabled the parties to more readily and accurately assess the potential efficiency gains related to their implementation. Both the CPB and the Staff requested such studies repeatedly to no avail. Despite the testimony of CPB witness Larkin that in his 36 years of experience he has found that such studies are always performed for projects of this magnitude (Tr. 3804), NYSEG

¹⁴ RD, p. 39

¹⁵ Id.

apparently did none.

Accordingly, the productivity factor must be increased further. We recommend a minimum of 6%, which would produce a total revenue requirement adjustment of approximately \$5.8 million. This recommendation is less than those of CPB and Staff witnesses, and less than NYSEG's own representations as cited above. Given that the difficulty in estimating a number for efficiency savings was clearly not the fault of the intervening parties in this case, we believe our recommendation is reasonable.

D. Asset Sale Gain Account

The projected balance in this account, according to the RD, is \$87.7 million,¹⁶ and it is highly likely that this number will grow still further when the results of revenue sharing for 2006, the last year of NYSEG's current rate plan, are calculated.¹⁷ This money belongs to ratepayers and there is no question that, sooner or later, it will be used for their benefit. By recommending that the ASGA balance simply be taken as an offset to rate base, the RD has avoided the need to make any decision as to how and when that should occur. The Commission should take this opportunity to do just that.

First, the Commission should recognize that the funds in the ASGA belong to all consumers, large and small, and that any distribution from the account should be allocated among customer classes in a fair and equitable manner that takes into account, among other things, the indirect contributions to the ASGA made by customers who took service under NYSEG's fixed rate commodity option. Based on preliminary discussions we have had, the CPB believes that such a methodology can be worked out

¹⁶ RD, p. 52

¹⁷ The CPB did not address the ASGA in its testimony, but the results of revenue sharing for 2005 have now made it imperative that plans for distribution of these funds be developed.

among the parties to this case. Accordingly, we recommend that the Commission direct NYSEG to convene a collaborative proceeding within thirty days of an order in this case in which interested parties will attempt to agree upon an appropriate allocation method.

Funds allocable to residential customers should be retained by the Company to mitigate any rate increases these classes may experience as a result of the loss of low-cost NYPA power allocations that are currently scheduled to expire on August 31, 2007. NYSEG has estimated that elimination of these allocations would result in a 14.5% increase in residential rates. (Tr. 1093) This increase would occur just eight months after any decrease resulting from this case would have taken effect, and before customers would have begun to see substantial benefits from reductions in the non-bypassable wires charge resulting from the expiration on some legacy NUG contracts. Smoothing this “bump” for residential customers is exactly the type of rate mitigation for which these funds should be used.¹⁸

E. Availability of Fixed Price Option for Small Commercial Customers

Although the principal factual and policy questions addressed in the RD with respect to the offering of a fixed price commodity option (“FPO”) by NYSEG are discussed without reference to any specific class or classes of customers,¹⁹ the stated bases for the recommendations adopted in the decision rely heavily on the “unique facts and circumstances” of the residential market.²⁰ Accordingly, there is some ambiguity as to what the ALJs intended to be the scope of their finding that maintaining the

¹⁸ In the event that the NYPA allocations are continued, disposition of the ASGA balance allocable to residential customers would be subject to further Commission order.

¹⁹ RD, p. 92.

²⁰ Id., at p. 122.

availability of a fixed price offer from the utility is a necessary transition measure until competitive markets are more fully developed. The Commission should clarify this uncertainty by requiring NYSEG to provide an FPO for all small, non-demand metered customers whether residential or commercial.

In terms of usage, there is little distinction between small commercial customers and residential customers. As of November 2005, NYSEG had approximately 68,500 non-residential customers taking service under its SC-6 rate classification.²¹ To be eligible for this service, a customer must use less than 2,000 kilowatt-hours per month. At the same time, nearly 140,000 residential customers were taking service under SC-8, which requires monthly usage greater than 1,000 kilowatt-hours.²² Clearly, the size overlap between residential and small commercial classes is considerable.

The overlap in commodity service preferences is equally great. Again, as of November 2005, 88% of SC-1 and SC-8 residential customers were receiving fixed price commodity service from NYSEG, as were 78% of non-residential customers under SC-6.²³ These similarities in preferences and in usage characteristics demonstrate clearly that all small customers, whether residential or commercial, should have the same commodity options available. The Commission's order in this case should so require.

²¹ Hearing Exhibit 1, NYSEG Response 0105 to information request DPS-80.

²² Id.

²³ Id.

CONCLUSION

With the few modifications and clarifications we recommend herein, the Recommended Decision of the ALJs in this proceeding should be adopted in its entirety by the Commission.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Teresa A. Santiago". The signature is fluid and cursive, with the first name "Teresa" being the most prominent part.

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