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

REPLY BRIEF OF THE NEW YORK STATE

CONSUMER PROTECTION BOARD

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CONSUMER PROTECTION BOARD

The initial brief filed by the Consumer Protection Board ("CPB") in this proceeding anticipated the majority of issues raised by other parties concerning the positions we have taken on the rate filing of New York State Electric & Gas Corporation ("NYSEG"). The arguments we made there will not be repeated here. In this reply brief, we will address only new information, or new interpretations of existing information, presented in the parties' briefs, and we will clarify or expand upon matters which may have been unclearly or incompletely covered in our initial brief.[1] For convenience, the issues are presented in the same order, and generally with the same categories, as the table of contents used by the parties for their initial briefs.

THRESHOLD ISSUES

Asset Sale Gain Account ("ASGA")

The CPB agrees generally with the comments of NUCOR, MI and others supporting the prompt return to customers of the balance in the ASGA, as contemplated

[1] For simplicity, all initial briefs are cited throughout this document using the submitting party's name in abbreviated form, followed by the page number, for example: NYSEG 165, NUCOR 15, Staff 302, CPB 12, etc.

by the terms of the current rate plan.[2] To be equitable, however, any proposal for the return of this money should allocate the funds to the customers who provided them in the first place.

The current balance in the ASGA is not, as MI suggests, “money resulting from the utility’s sale of generation facilities.” (MI 12) Although the ASGA was originally funded from that source, most of the balance now is attributable to excess earnings realized by NYSEG from commodity sales. Virtually all of those excess earnings came from the Company’s fixed price offerings.[3] To the extent that the relative contributions of the various service classes to those commodity earnings differ, equity requires that the return of the funds reflect such differences proportionally.[4]

REVENUE REQUIREMENT

As we stated in our initial brief, the CPB’s witnesses did not conduct a comprehensive review of every element of the Company’s proposed revenue requirement. Consequently, we have addressed in detail only those revenue requirement issues on which we submitted testimony.

The CPB also strongly supports the revenue requirement adjustments proposed by DPS Staff and NUCOR. The recommendations of these parties reflect thorough analysis, are well documented, and have not been convincingly rebutted by NYSEG in its testimony or its brief. They should be adopted by the Commission as presented.

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[2] See for example NUCOR 13-14.

[3] See *infra* at p. 11.

[4] We suggest a methodology for this allocation in our section on excess commodity earnings, *infra* at pp. 11-12.

General Matters – Burden of Proof

NYSEG continues to demonstrate in its Initial Brief that it fails to appreciate its fundamental obligation in this proceeding to prove that its rate requests are just and reasonable. Over and over, the Company takes the position, "This is what we say. Prove us wrong." That is not the responsibility of the Staff or the intervening parties in this case.

NYSEG is entitled to an increase in its revenue requirement only when it meets its statutory burden of proving that it will incur incremental expenses during the rate year.[5] For new equipment acquisitions, new programs and operational changes that any rational person would presume to generate benefits as well as costs, the Company does not meet that burden by ignoring the former and addressing only the latter. When a party has presented sufficient information to permit a reasonable inference to be drawn that benefits will be achieved, the Company has the responsibility of negating that inference, and it does not do so by baldly asserting that the party has failed to prove its point.[6]

The Company's unsupported claims are not proof. NYSEG is required to provide a factual basis for its revenue requirement requests. If it has failed to produce a cost-benefit analysis of its proposed expenditures – as was the case with NYSEG's CCS, radio replacement, WMS, IBO and T&D IRP programs – it does not meet its burden of proving its incremental costs simply by pointing out that no other party has produced such an analysis. Where there is a gap in the information needed to calculate the value

[5] PSL § 66(i).

[6] See, for example NYSEG 105 where the Company criticizes the CPB for failing to prove that certain expenses were either non-recurring or not annual, despite the fact that NYSEG presented no evidence to suggest that they were.

of benefits directly, it is entirely appropriate for the Commission to impute that value on some reasonable basis, and to adjust NYSEG's revenue requirement requests accordingly.[7]

O&M Expenses - Apprenticeship Program

NYSEG's attempts at justifying the amount included in its revenue requirement for this program continue to be nothing more than circular reasoning. As both the CPB and Staff pointed out, new hires and departures of employees in the job categories covered by the apprenticeship program appear to have remained in equilibrium for several years, and NYSEG provides absolutely no objective evidence to support the assertion that a major net increase in employment is imminent. (CPB 8-9; Staff 68)

In response, NYSEG says 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 arrived at the need for the 30 additional apprentice employees to achieve a complement of qualified employees to match desired staffing levels. (NYSEG 61-62)

For an explanation of the nature and scope of that management study, the Company directs the parties to a response to an information request in which it says:

> 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 number of apprentice employees to add by position to achieve a complement of qualified employees to match desired staffing levels.[8]

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[7] See, for example, the discussion of a "burden of proof adjustment" in Cases 94-E-0098, et al., Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Niagara Mohawk Power Corporation for Electric Service; Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Niagara Mohawk Power Corporation for Electric Street Lighting Service; Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Niagara Mohawk Power Corporation for Gas Service; Niagara Mohawk Power Corporation - Consolidated Proceedings, Opinion No. 95-21, December 29, 1995.

[8] Exhibit 1, NYSEG Response No. 0116 to DPS-91.

In other words, NYSEG's only answer to the parties' legitimate questions as to why these additional positions are required is, "Because we decided they were." The Company has failed to provide any factual basis for its claim that incremental positions will be required for this ongoing program which has had stable staffing levels for years. (SM 3764-65) The adjustment proposed by the CPB and Staff should be adopted.

O&M Expenses - Stray Voltage

The information provided in NYSEG's Initial Brief conclusively demonstrates that the adjustments to operating expense for stray voltage testing and inspection recommended by the CPB and DPS Staff are fully justified. Even if the Company is given the benefit of the doubt with respect to its estimate of administrative costs for this program, the rate year allowance should be adjusted downward by nearly five million dollars.

In a response to an information request, the Company reports that it inspected 23% of its facilities in 2005, and performed stray voltage testing on 42%.[9] Its incremental expenses attributable to these efforts fell into three categories: administrative, testing and inspection. The added administrative costs of $311,357 are primarily related to outside contractors; testing costs of $1,800,712 are entirely for contractors; and inspection costs of $82,762 are all internal, principally employee overtime.

Based on the Commission's requirement that 100% of facilities be tested for stray voltage annually, CPB witnesses Larkin and DeRonne projected that the $1.8

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9 Exhibit 1, NYSEG Response No. 0711 to DPS-457.

million expended to test 42% in 2005 would grow to $4,287,409 in the 2007 rate year. (SM 3829) NYSEG itself now projects testing expense for the rate year of $4,554,332, only about 6% more than the CPB estimate.[10] (NYSEG 83) This information completely moots the Company's arguments concerning a major urban/rural cost differential. (NYSEG 83) Whatever that difference may be, it is subsumed by the Company's own projections.

With respect to inspection expense, NYSEG's request for a **4388%** increase from 2005 to the 2007 rate year[11] is not only completely unsupported, but also is utterly illogical. The Company inspected 23% of its facilities in 2005, exceeding the Commission's requirement of 20% annual inspections.[12] NYSEG has no greater obligation in the rate year than that which it undertook last year.

Moreover, of the total incremental inspection expense reported for 2005, approximately 74% was attributable to "Overtime."[13] Overtime is expensive and is generally the last resort for any business. As the inspection process matures and becomes better organized and scheduled, it would be reasonable to assume that this expense would decline.

Finally, the Company makes no claim with respect to inspection expense, as it did with testing costs, that its 2005 experience reflected "easy" inspections and that future efforts would be more difficult. Its argument that certain inspections of single-

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[10] This information was first made available in an information request response dated more than two weeks after CPB's direct testimony was submitted. (See Exhibit 1, NYSEG Response No. 0917 to DPS-523)

[11] From $82,762 to $3,632,000. Exhibit 1, NYSEG Response No. 0711 to DPS-457.

[12] Id.

[13] $60,890 out of $82,762. Id.

phase pad mount transformers performed in 2005 will have to be repeated is completely irrelevant, because it also says that it did not count those inspections in coming up with its 23% total. (NYSEG 84) Therefore, the fact remains that NYSEG completed more than the Commission mandated level of inspections in 2005 at an incremental cost of $82,762.

NYSEG projects that its administrative costs for the stray voltage program will increase from $311,357 in 2005 to $892,320 in the 2007 rate year.[14] Even assuming those costs grow in proportion to the increase in testing costs (a generous assumption since administration also covers inspections which will not grow), the projection for 2007 should be revised downward to $741,236.

Thus, the projected total rate year cost for the stray voltage program, using primarily NYSEG's own numbers, would be:[15]

Administration	$ 741,236
Testing	4,554,332
Inspection	82,762
TOTAL	$ 5,378,330

Compared to the Company's request for $10,184,000 (SM 3828), this total would require a downward adjustment to revenue requirement of $4,805,670. Given the very generous assumptions used for administrative and testing expense, however, the calculation, in fact, confirms that the $5,501,472 adjustment proposed by the CPB's witnesses (SM 3829) was soundly based and should be adopted.

14 Exhibit 1, NYSEG Response No. 0917 to DPS-523.

15 Assumes no allowance for inflation, as recommended by the CPB Panel (SM 3829).

O&M Expenses - Pensions

As the CPB demonstrated, the best estimate of the discount rate to be utilized for calculating pension and OPEB expense was 5.75% based on information available in the record at the time we submitted our Initial Brief. (CPB 13) That information is constantly changing, however. Therefore, the CPB fully supports the recommendation of the DPS Staff that this discount rate be updated, and the associated expenses be adjusted, using information available at the time of the Commission's decision in this case. (Staff 73)

The CPB also recommended the removal from pension expense of the electric portion of a projected actuarial loss resulting from the amortization of deferred losses from prior years. The adjustment was $895,000, equal to 62.5% of the $1,431,709 amortized. (SM 3802) NYSEG has revised the amortization amount downward to $199,167. (NYSEG 73) Accordingly, the CPB's adjustment should be reduced to $125,000.

Merger Savings - Imputed Savings

The CPB recommended that $6.4 million in merger savings be imputed in rates based on the difference between the $28.8 million claimed to have been achieved by the Company and the $35.2 million it projected. (CPB 26) Staff stated in its brief that "since NYSEG reduced the realized merger savings to $25 million in its rebuttal case, we assume that CPB's adjustment would be updated to be $10.2 million." (Staff 103) Staff is correct in its assumption.

COMMODITY OPTIONS

Various parties have raised issues directed at specific aspects of the CPB's commodity options proposal, or more generally, at any proposal that would permit NYSEG to provide a fixed price option ("FPO") to its customers. We address some of those issues in this section.

Customer Confusion

Direct Energy describes NYSEG's Voice Your Choice program as presenting a "confusing array of choices" that poses a threat to the competitive process. (Direct Energy 37) SCMC argues that this complexity is overwhelming for consumers given "the average customer's lack of sophistication," and results in most of them doing nothing but accept the default option. (SCMC 24) Staff says "NYSEG's menu of supply options created customer confusion" and cites testimony in which it describes newspaper reports quoting two customers who found the choices somewhere between "really confusing" (SM 1813) and "damn confusing." (SM 1814)

Notwithstanding the newspaper anecdotes, these arguments simply make no sense. Voice Your Choice customers have two straightforward decisions to make. First, they have a choice between utility commodity service and ESCO commodity service. This is neither complex nor new. It has been the case for nearly a decade and has been very heavily publicized through ratepayer funded outreach and education programs.

Next, customers who decide they want to take service from NYSEG must again confront a "bewildering array" of exactly two choices: fixed price or variable price. While this availability of options for utility service is a change for electric customers, it

hardly represents a novel decision for consumers. Hundreds of thousands of families who heat with fuel oil or propane make the fixed vs. variable decision every winter, apparently without feeling the need to complain to their newspapers. They make similar decisions when choosing telephone service plans and mortgage rates.

Change can be disruptive. It is not surprising that there is anecdotal evidence that some customers initially found it confusing to have to make a decision about utility service where none was required before. That does not mean such decisions are inherently too complex for consumers to deal with. The options presented by the Voice Your Choice program, as that program would be modified by the CPB's proposal, most certainly are not. The "confusion" argument is at best a "red herring" and should be ignored.

VPO as Default

NYSEG suggests that the CPB's recommendation that the VPO be the default service was based on the erroneous assumption that the VPO and FPO rates would remain substantially the same. (NYSEG 252) That is not the case. We noted the close correlation in the past, but as indicated below, we view the availability of open enrollment as the primary safeguard for customers who are unhappy with the option they are assigned.

Return of Excess Earnings

NUCOR (NUCOR 30), Multiple Intervenors (MI 44) and the CPB all agree that if NYSEG is permitted to continue to offer an FPO under which it has the potential to make a profit, earnings above some level should be treated as "excess" and should be

promptly returned to ratepayers. NUCOR suggests that this be done through credits to the NBC. MI suggests either using the NBC or imputing some level of commodity earnings as an offset to delivery rates. The CPB suggested that excess earnings be credited to the ASGA "or otherwise used for the benefit of customers." (SM 2001) Any of the suggested methods for returning funds to ratepayers is potentially acceptable. The CPB's primary concern is that the funds be returned in an equitable manner.

NYSEG's Commodity Options Panel testified that virtually all of the Company's commodity profits were attributable to its fixed price option. (SM 1653) Data provided by NYSEG indicate that, as of November 2005, 90% of SC1 residential customers, 83% of SC2 small commercial customers and 73% of larger SC7 customers were served under either the bundled rate option ("BRO") or the BRO with retail access credit.[16] These data indicate that the various classes made differing contributions to NYSEG's excess earnings. The differences should be taken into account in defining the mechanism through which those earnings are passed back to each service class. The CPB recommends that credits be allocated among service classes based on the percentage of the total FPO service provided by the Company that was taken by the members of each class during the applicable accounting period. Given that NYSEG already calculates the NBC on a service class basis, this calculation would add little if any complication to the process.

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[16] Exhibit 1, NYSEG Response No. 0105 to DPS-80.

COST OF SERVICE/NYSEG ECOS STUDY

Lost Revenue Recovery Mechanism

The CPB agrees with MI that the Commission's Unbundling Policy Statement[17] calls for responsibility for recovery of lost revenues attributable to migration to be shared between all customers and full service customers. (MI 50) We strongly disagree, however, with MI's suggestion that the 50-50 sharing proposed in the pending, contested Central Hudson Joint Proposal is an appropriate model. The Unbundling Policy Statement called for an effort to be made to determine "the relative magnitude of unavoidable POLR costs and long-run avoidable costs" which are to be assessed to full service and all customers, respectively.[18] There is no empirical basis on this record for assuming that full service customers should pay 75% of all migration-related lost revenues, which is what the 50-50 sharing proposed by MI would produce. Instead, NYSEG should be directed to perform the necessary analysis and propose an allocation based on its findings.

REVENUE ALLOCATION/RATE DESIGN

Non-Bypassable Wires Charge ("NBC") – Ancillary Services

Under the terms of NYSEG's existing rate plan, the cost of ancillary services for electric supply is recovered through the NBC. If the NBC is continued, this should be changed. Ancillary services costs should be removed from the NBC and included in the Company's supply charges.

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[17] Case 00-M-0504, Proceeding on Motion of the Commission Regarding Provider of Last Resort Responsibilities, the Role of Utilities in Competitive Energy Markets, and Fostering the Development of Retail Competitive Opportunities – Unbundling Track, Statement of Policy on Unbundling and Order Directing Tariff Filings ("Unbundling Policy Statement") (issued August 25, 2004).

[18] Id. at pp. 35-36.

As NYSEG's Commodity Panel noted on cross-examination, "one of the key requirements of a default service is to send a price signal that is appropriate." (SM 1642) Ancillary services are a normal component of electric supply and their cost is should be recovered in the supply charge. Again, NYSEG's Commodity Panel confirmed this point:

> Q. But ordinarily [ancillary services] would be a cost that you would want in the supply charges, if you were sending an accurate price signal.
>
> A. (Witness Segal) Again that is a charge that is incurred of – pretty much volumetrically with usage, so yes. (SM 1643)

Including ancillary services costs in the NBC needlessly distorts the price signal sent by the supply charge portion of NYSEG's bills.

Fixed Non-Bypassable Wires Charge

As we stated in our initial brief, NYSEG should be required to offer ESCOs the ability to use the same fixed NBC that it employs in setting the price for its FPO. (CPB 53-54) However, because our witness, Mr. Niazi, also testified that the CPB considered the elements of its commodity options plan to be interdependent, (SM 1994) there may be a question as to whether we would support the fixed NBC proposal standing alone. We would, therefore, like to clarify that the CPB does support the adoption of this proposal even if the Commission determines, contrary to our recommendation, that NYSEG should no longer offer an FPO.

We had two primary concerns in arguing that our commodity proposal should not be viewed as a menu of choices. First, we would not want to see the Variable Price Option (VPO) be the default for consumers if they do not also have the benefit of open

enrollment to permit them to change options at any time. Second, we would not have supported the current pricing mechanism for the FPO without significant limitations on NYSEG's earnings from the program.

Making a fixed NBC available to ESCOs presents no such problems, even if the Commission chooses to modify the Voice Your Choice program substantially. In fact, the availability of a fixed NBC will be even more important if the Commission decides that NYSEG should not offer an FPO. In that circumstance, ESCOs would become the only source of such an option. If they are hindered in developing FPO offers by having to deal with a constantly changing NBC, consumers may be completely deprived of an option they have overwhelmingly indicated they prefer. Thus, the CPB supports the suggestion of the DPS Staff (Staff 235) that NYSEG be required to make the fixed NBC available to ESCO customers.

RENEWABLES AND DISTRIBUTED GENERATION

NYSEG's Rate Plan Panel proposed that the Company be permitted "to recover any renewable generation investments made by NYSEG consistent with the State's goal of achieving a 25% level of renewable resources." (SM 1093) It also requested that the Company be allowed to "own and operate DG facilities for customers;" that it would "charge such customers a cost for this service;" and that the cost would be "developed in a tariff to be filed 90 days after the approval" of a rate plan by the Commission. (SM 1093) NYSEG's initial brief does nothing more than reiterate these statements. (NYSEG 23)

This is the sum total of the information that NYSEG has provided for a proposal that "would be a step backward from the Commission's long-standing pro-competition

policies" with respect to power generation. (IPPNY 5) The CPB agrees fully with the DPS Staff that the Company "has not provided enough information to allow ... the Commission to make a decision to allow such expenditures." (SM 2974) There is absolutely no substantive basis in this record for a decision permitting the Company to re-enter the generation business. If the Company believes it can supply adequate justification for its proposal in the context of a more detailed filing, it is free to make such a submission in the future. For now, the proposal must be rejected.

CONCLUSION

For the reasons set forth in its testimony and briefs in this proceeding, the recommendations of the Consumer Protection Board with respect to the rate plan filed by New York State Electric and Gas Corporation should be adopted by the Commission.

Respectfully submitted,

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