BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

In the Matter of

Consolidated Edison Company of New York, Inc.

Case 06-G-1332

March 2007

Prepared Testimony of:
Staff Accounting Panel

Kristee Adkins
Senior Auditor

Claude Daniel
Public Utilities Auditor II

Jeffrey Hogan
Principal Utility Financial
Analyst

John Scherer
Supervisor

Jane Wang
Senior Auditor

Office of Accounting, Finance
and Economics
State of New York
Department of Public Service
Three Empire State Plaza
Albany, New York 12223-1350

1 Q. Please state your names, employer, and business
2 addresses.
3 A. Kristee Adkins, Claude Daniel, Jeffrey Hogan,
4 John Scherer, and Jane Wang. We are employed by
5 the New York State Department of Public Service
6 (Department). Our business addresses are Three
7 Empire State Plaza, Albany, New York 12223 and
8 90 Church Street, New York, New York 10007.
9 Q. Ms. Adkins, what is your position at the
10 Department?
11 A. I am employed as a Senior Auditor in the Office
12 of Accounting, Finance and Economics.
13 Q. Please describe your educational background and
14 professional experience.
15 A. I graduated from the State University of New
16 York Institute of Technology in Marcy, New York
17 in 2002 with a Bachelor of Science degree in
18 Accounting and Finance. I have been employed
19 with the Department since June 2005. I examine
20 accounts, records, documentation, policies and
21 procedures of regulated utilities. I have
22 participated in the rate proceedings of Adrian's
23 Acres West Water Company, Inc., Case 05-W-0802,
24 and Orange and Rockland Utilities, Inc. (Orange

1 and Rockland), Case 05-G-1494. I have also
2 worked on asset transfer filings for
3 Consolidated Edison Company of New York, Inc.
4 (Con Edison).
5 Q. Ms. Adkins, have you previously testified before
6 the New York State Public Service Commission
7 (the Commission)?
8 A. Yes, I have submitted testimony on various other
9 operating revenues and operation and maintenance
10 (O&M) expense forecasts in the most recent gas
11 case for Orange and Rockland, Case 05-G-1494.
12 Q. Mr. Daniel, what is your position at the
13 Department?
14 A. I am employed as a Public Utilities Auditor II
15 in the Office of Accounting, Finance and
16 Economics.
17 Q. Please describe your educational background and
18 professional experience.
19 A. I graduated from Hunter College of the City
20 University of New York with a Bachelor degree in
21 Accounting and joined the Department in 1986.
22 Q. Please describe your responsibilities with the
23 Department.
24 A. I routinely examine accounts, records,

1 documentation, policies, and procedures of
2 regulated utilities.
3 Q. Mr. Daniel, have you previously testified before
4 the Commission?
5 A. Yes, I have prepared cost of service exhibits
6 and offered testimony on various O&M expense
7 adjustments in previous Con Edison electric, gas
8 and steam rate cases. I also testified in a New
9 York Telephone Company rate case regarding its
10 earnings base versus capitalization (EBCAP).
11 Q. Mr. Hogan, what is your position at the
12 Department?
13 A. I am employed as a Principal Utility Financial
14 Analyst in the Office of Accounting, Finance and
15 Economics.
16 Q. Please describe your educational background and
17 professional experience.
18 A. I received a Bachelor of Arts Degree in
19 Economics and Political Science from Syracuse
20 University in 1991. In 1993 I received a
21 Master's Degree in Business Administration with
22 a concentration in finance from the State
23 University of New York at Albany. I joined the
24 Department in February 1994 and subsequently

1 took additional college courses in accounting.
2 Q. Please briefly describe your responsibilities
3 with the Department?
4 A. My areas of responsibility include analyzing
5 rate of return and O&M expense levels. I also
6 work on financing requests from utilities and
7 regulatory review of the formation of utility
8 holding corporations. In addition, I assist in
9 analyzing legislative proposals affecting the
10 utility industry.
11 Q. Mr. Hogan, have you previously testified before
12 the Commission?
13 A. Yes, I testified on the appropriate capital
14 structure and cost of capital in the following
15 cases: Case 05-S-1376 - Con Edison Steam Rates,
16 Case 04-E-0572 - Con Edison Electric Rates, and
17 Cases 03-G-1671 and 03-S-1672 - Con Edison Gas
18 and Steam Rates. In Case 02-W-1564, Sea Cliff
19 Water Company, I testified on the capital
20 structure and cost of capital, as well as on
21 certain O&M expenses. In Case 01-M-0075,
22 Niagara Mohawk/National Grid Merger, I analyzed
23 the capital structure and cost of equity. In
24 Case 94-W-0157, New Rochelle Water Company, I

1 assisted in the development of Staff's
2 recommended capital structure and cost rates.
3 In Case 94-G-0885, National Fuel Gas
4 Distribution Corporation, I analyzed the capital
5 structure and assisted in the calculation of
6 Staff's recommended return on common equity. In
7 Case 95-G-0761, Brooklyn Union Gas, I assisted
8 in the formation of the capital structure as it
9 formed a holding Company, as well as assisted in
10 the calculation of Staff's recommended return on
11 equity.
12 Q. Mr. Scherer, what is your position at the
13 Department?
14 A. I am employed as a Supervisor in the Office of
15 Accounting, Finance and Economics.
16 Q. Please describe your educational background and
17 professional experience.
18 A. I graduated from Siena College, Loudonville, New
19 York in 1988 and have a B.B.A. degree with an
20 Accounting major. I have been employed by the
21 Department since 1988.
22 Q. Please briefly describe your responsibilities
23 with the Department.
24 A. My responsibilities include examination of

1 accounts, records, documentation, policies and
2 procedures of regulated utilities. I have been
3 involved in numerous rate and accounting
4 examinations including Con Edison's last three
5 electric rate proceedings, the Company's
6 electric and gas rate unbundling proceeding and
7 the Company's last gas and steam rate cases. I
8 have general responsibility for accounting and
9 ratemaking matters related to Con Edison.
10 Q. Mr. Scherer, have you previously testified
11 before the Commission?
12 A. Yes, I have testified in numerous Commission
13 proceedings on a variety of accounting and
14 regulatory issues including property taxes,
15 pensions and other post employment benefit
16 (OPEBs), EBCAP adjustments, O&M expense
17 forecasts, federal income taxes, various rate
18 base components, and tax refunds. With specific
19 reference to Con Edison, I submitted testimony
20 in the Company's last electric, gas, and steam
21 rate cases, the Unbundling Track of the
22 Competitive Markets Proceeding and in two income
23 tax proceedings.
24 Q. Ms. Wang, what is your position at the

1 Department?
2 A. I am employed as a Senior Auditor in the Office
3 of Accounting, Finance and Economics.
4 Q. Please describe your educational background and
5 professional experience.
6 A. I graduated from Tsinghua University, Beijing,
7 China in 1985 with a BS degree in Electric Power
8 Engineering. I also received a Master's degree
9 in Electric Power Engineering from Tsinghua
10 University in 1988. I received a Master's in
11 Business Administration from Union College,
12 Schenectady, New York in 1997. I have
13 experience working as a cost engineer with
14 General Electric and a Staff Accountant with
15 Time Warner Cable. I have been employed by the
16 Department since April 2005. I have worked on
17 municipal rate proceedings and general
18 accounting examinations.
19 Q. Ms. Wang, have you previously testified before
20 the Commission?
21 A. Yes, I have testified in Con Edison Steam Case
22 05-S-1376 for other operating revenues, items in
23 rate base and other miscellaneous adjustments.
24 Q. Panel, what is the purpose of your testimony?

1 A. Our testimony addresses accounting aspects of
2 Con Edison's gas rate filing. We will discuss
3 and recommend adjustments in the following
4 areas:
5 - Late payment charges (LPC) revenues
6 - Unbundled retail choice service
7 revenues
8 - Pensions and OPEBs expenses
9 - Injuries and damages
10 - Materials and supplies
11 - Other operations and maintenance
12 - Property taxes
13 - World Trade Center costs
14 - Manufactured gas plant (MGP)/Superfund
15 - Accumulated deferred taxes
16 - Deferred accounting
17 We also summarize Staff's overall revenue
18 requirement position.
19 Q. What is the effect of Staff's adjustments on
20 rate of return?
21 A. The adjustments as shown on Exhibit__(AP-2),
22 Schedule 1, increase the gas rate of return
23 before any proposed rates from 4.10% to 5.92%.
24 Q. What is the rate of return recommended by the

1 Staff Financial Panel?
2 A. The Staff Financial Panel recommends a 7.16%
3 rate of return based on an 8.8% return on
4 equity. As a result, the indicated rate change
5 in gas base rates is a $32.2 million increase
6 for the rate year ending September 30, 2008.
7 Q. What are the major areas where Staff is
8 proposing adjustments?
9 A. The adjustments fall into eight major
10 categories: sales, other operating revenues,
11 O&M expenses, depreciation, property taxes, rate
12 base, income taxes, and working capital.
13 Q. Please highlight the amount of the adjustments
14 for each of categories.
15 A. The Gas Rates Panel has proposed $27.2 million
16 of additional sales revenues. $22.3 million of
17 this is related to New York City Housing
18 Authority customers moving from interruptible
19 service to firm service.
20 Our Panel proposes $5.7 million of
21 adjustments to the Company's other operating
22 revenues. Of this amount, $4.5 million is
23 related to Staff's proposal that the Company
24 recover the under-collection of pension and OPEB

1 expenses over a five-year period instead of the
2 three-year period proposed by the Company.
3 Staff is proposing $32.0 million of
4 adjustments to O&M expenses. Over half of this
5 amount is from adjustments related to contract
6 labor costs, pension and OPEB expense, and
7 outreach and education expense.
8 The Gas Rate Panel and the Gas Capital
9 Construction O&M Program Panel is proposing $5.5
10 million of adjustments to depreciation costs,
11 primarily the elimination of the Company's
12 proposed depreciation rate changes.
13 This Panel is proposing an adjustment of
14 $2.4 million to the Company's property tax
15 expense.
16 Staff is proposing to decrease the
17 Company's proposed rate year rate base by $192.8
18 million. This is primarily driven by
19 adjustments to the Company's treatment of its
20 prepaid pension expense, a reduction to the
21 Company's capital construction forecast, and a
22 correction of a Company error in their EBCAP
23 calculation.
24 Staff's adjustments have impacts on the

1 income taxes, primarily due to lower income
2 resulting from our recommended return on equity.
3 Staff's adjustments also affect the Company's
4 working capital needs.
5 Q. Will the Panel refer to, or otherwise rely upon,
6 any information produced during the discovery
7 phase of this proceeding in its testimony?
8 A. Yes, the Panel will refer to, and have relied
9 upon, several responses to Staff Information
10 Requests (IR). They are designated as Exhibit
11 __ (AP-1).
12 Q. Is the Panel sponsoring any other Exhibits?
13 A. Yes, the Panel is sponsoring Exhibit __ (AP-2),
14 which is Staff's cost of service presentation.
15 Q. Please describe Exhibit __ (AP-2).
16 A. Exhibit __ (AP-2) contains eight schedules.
17 Schedule 1 is the Staff's projection of gas
18 operating income, rate base and rate of return
19 for the 12 months ending September 30, 2008, and
20 includes the Staff's proposed revenue
21 requirement. Schedule 1 is supported by
22 Schedules 2 through 8.
23 Q. Please describe the format of Schedule 1.

1 A. Column 1 of Schedule 1 contains income
2 statement, rate base and rate of return figures
3 as filed by the Company for the rate year,
4 before a revenue increase. Column 2 contains
5 the Company's revised filing as of December 8,
6 2006. Column 3 contains the Company's updates
7 to its revised filing. Column 4 reflects the
8 income statement, rate base and rate of return
9 figures as updated by the Company. Column 5
10 contains references to the supporting schedules
11 that present Staff's adjustments set forth in
12 Column 6. Column 7 presents Staff's projected
13 rate year figures before a revenue increase.
14 Column 8 contains Staff's proposed changes in
15 revenues, and Column 9 is Staff's projected rate
16 year income, rate base and rate of return after
17 this revenue increase.
18 Q. What information is shown on Schedules 2 and 3?
19 A. Schedule 2 projects O&M expense cost elements
20 for the rate year. Schedule 3 projects taxes
21 other than income taxes.
22 Q. What information is shown on the remaining
23 schedules?

1 A. Schedules 4 and 5 project New York State and
2 federal income tax expenses, respectively. The
3 adjustments in these schedules correspond
4 primarily to adjustments set forth in other
5 schedules. Schedule 6 projects the rate base
6 for the rate year ending September 30, 2008.
7 Schedule 7 projects an allowance for working
8 capital, which is a component of rate base.
9 Schedule 8 lists Staff's adjustments with their
10 supporting witnesses.
11 **Other Operating Revenues**
12 Q. Please explain your adjustment to LPC revenues.
13 A. The Company's Accounting Panel forecasted LPC
14 revenues at $3,292,000 for the rate year using a
15 historic three-year average ratio of LPC
16 revenues to total sales revenues. Staff
17 forecasts the rate year level of LPC revenues at
18 $3,787,000. In the response to Staff IR #83
19 Revised, the Company provided corrected levels
20 of LPC revenues and sales which caused the
21 historic three-year average ratio to increase
22 from .1997 to .2291. Use of the corrected ratio
23 resulted in an increase of $484,000 in
24 forecasted LPC revenues. Also, Staff proposes

1 an increase to rate year sales revenues which
2 results in an additional increase of $11,000 in
3 rate year LPC revenues. Staff's total rate year
4 forecast of LPC revenues is $3,787,000; an
5 increase of $495,000 over the Company's
6 forecast.
7 Q. Please continue with the next group, unbundled
8 retail choice service revenues.
9 A. The Company's unbundled retail choice service
10 revenues are comprised of two items:
11 ESCOs/Marketers - Bill Charges (CUBS) revenues
12 and Purchase of Receivables (POR) discount
13 revenues.
14 Q. Please explain your adjustment to CUBS revenues.
15 A. The Company's Accounting Panel forecasted CUBS
16 revenues at the rate year level of $297,000.
17 The forecast was developed by annualizing six
18 months of CUBS revenues realized by Con Edison
19 from January 2006 through June 2006. Applying
20 the same methodology to the most recent six
21 months of data from July 2006 through December
22 2006, Staff proposes an increase of $138,000 to
23 the rate year level of CUBS revenues. Staff's

1 rate year level forecast of CUBS revenues is
2 $435,000.
3 Q. Please explain the adjustment to POR discount
4 revenues.
5 A. The Company's Accounting Panel indicated that
6 the Company intends to continue with the POR
7 programs established in the current rate plan,
8 with some modifications. The Company's rate
9 year level of POR discount revenues was
10 projected based on the historic level of
11 $1,199,000. Staff forecasts an increase of
12 $91,000 to the rate year level by applying the
13 Company's forecast methodology to the most
14 recent 12 months of data from January 2006
15 through December 2006. Staff's rate year level
16 of POR discount forecast is $1,290,000.
17 Q. Does Staff recommend any other adjustment to the
18 Company's forecast of other operating revenues?
19 A. Staff recommends a $4.9 million increase in
20 other operating revenues to reflect lower
21 deferred pension and OPEB costs as well as a
22 five-year amortization of the costs. We discuss
23 the basis for this recommendation in the pension
24 and OPEB expense section of our testimony.

1 Q. The Company proposes to pass back gas customers'
2 share of an Investment Tax Credit (ITC) refund
3 over three years. Do you agree with the
4 Company's proposal?
5 A. Yes. However, we found that the Company's
6 proposal does not include interest on the
7 deferred balance that customers are entitled to
8 pursuant to the Commission's Order in Case 05-M-
9 0407. The Commission's Order required the
10 Company to defer the customers' share of the
11 refund, with interest at the unadjusted customer
12 deposits rate, until disposition of the
13 customers' share was determined.
14 Q. Do you have a calculation of the interest
15 amount?
16 A. We calculated interest on gas customers' share
17 of the ITC refund from the date the Company
18 received it to the start of the rate year. Our
19 calculation produced $88,078.
20 Q. Do you have a recommendation as to the treatment
21 of the interest?
22 A. Yes. Consistent with the Company's pass-back of
23 the refund, we recommend a three-year pass-back
24 of the interest. We therefore adjust other

1 operating revenues by $29,259, representing one-
2 third of the accrued interest. We also decrease
3 rate base by $44,130, representing the
4 unamortized net-of-tax interest balance in the
5 rate year.

6 **Gas O&M Expenses**

7 **Administrative & General Expenses Capitalized**

8 Q. How did Con Edison forecast rate year
9 administrative and general (A&G) expenses
10 capitalized?

11 A. Con Edison applied a general inflation factor to
12 its historic year level of A&G capitalized to
13 forecast the rate year amount.

14 Q. Do you think Con Edison's approach is
15 unreasonable?

16 A. No. The Company's forecast understates the
17 level of A&G costs that will be capitalized in
18 the rate year. The Company projects that major
19 components of its A&G costs will grow at rates
20 well in excess of general inflation. In
21 addition, the 2007 labor capitalization (labor
22 cap) rate has also increased over rates used
23 during the historic year. The combination of
24 these facts indicates that capitalized A&G costs

1 will increase at a rate greater than the general
2 inflation rate.
3 Q. What are the major components that determine A&G
4 capitalized?
5 A. A&G capitalized are administrative and
6 supervisory (A&S) costs that are associated with
7 capital construction projects. These costs
8 include company labor and labor-related
9 functions, such as human resource and labor
10 relations, injuries and damages, and employee
11 welfare expenses. The amount of these labor-
12 related costs that are capitalized is mainly
13 determined by the labor cap rate, which is
14 established on an annual basis. A&S costs also
15 include other functions, such as corporate
16 accounting, property records, purchasing,
17 information resources, and electronic
18 information administration. The level of costs
19 capitalized for these functions is determined
20 based on time studies. In a period of
21 increasing capital construction activities, the
22 labor cap rate increases, and therefore the
23 level of A&G costs that are capitalized will by
24 default increase. This effect will occur even

1 if the underlying A&S costs do not increase.
2 Changes in the level of A&S costs also will
3 affect the future level of A&G costs that are
4 capitalized. Staff's adjustment to A&G
5 capitalized reflects the increases in both the
6 labor cap rate and the Company's forecast of A&G
7 costs.
8 Q. How has Con Edison's labor cap rate changed
9 since the historic year?
10 A. The Company recently approved its 2007 labor cap
11 rate of 34.5%. The labor cap rate is the
12 percentage of total Company payroll expected to
13 be capitalized as part of construction projects
14 during a calendar year. The effective historic
15 year labor cap rate was 33.38%, which is the
16 average of the 2005 and 2006 rates of 33% and
17 33.75%, respectively.
18 Q. How will the A&G expenses change over the test
19 period?
20 A. Rate year A&G expenses, excluding A&G
21 capitalized, net employee pension/OPEB expenses,
22 employee welfare expenses, and shared services,
23 are forecasted by the Company to increase from
24 the historic year level of $31,254,000 to

1 $58,842,000 in the rate year (Company Exhibit__
2 (AP-6), Schedule 4). The change, $27,588,000,
3 represents an 88.3% increase. In addition, A&G
4 labor is forecasted by the Company to grow from
5 $14.8 million in the historic year to $16.4
6 million in the rate year, an increase of
7 approximately 11%. These growth rates are
8 substantially higher than the Company's general
9 inflation rate of 5.0%.
10 Q. How does Staff forecast rate year A&G
11 capitalized?
12 A. We started with Con Edison's recently approved
13 2007 authority letter which estimates the level
14 of A&G expenditures to be transferred to
15 construction. Staff then applied the general
16 inflation rate to the 2007 estimate to forecast
17 the 2008 level. Staff's forecast of rate year
18 A&G capitalized is $8.266 million, which is
19 $705,379 higher than the Company's forecast.
20 Q. Did you consider the impact of Staff's proposed
21 adjustments to the rate year capital projects?
22 A. Yes. In developing our forecast, we reflected
23 Staff's proposed $8.147 million reduction in gas
24 capital spending for the rate year. This

1 adjustment was recommended by the Gas Capital
2 Construction and O&M Program Panel (GCCOP).
3 **Company Labor**
4 Q. How did you adjust the company labor?
5 A. Staff's adjustments to company labor reflects
6 reductions to the payroll expense associated
7 with 12 new positions in the Company's tax
8 department and 13 employees in the Company's new
9 shared service organization.
10 Q. Please explain the incremental labor costs
11 related to the tax department.
12 A. Con Edison included $196,000 in labor costs
13 representing the gas department's allocation of
14 $1.2 million labor expense for 12 new positions
15 in the tax department. Con Edison stated that
16 it plans to fill all of these positions by July
17 2007.
18 Q. How many of these positions have Con Edison
19 filled to date?
20 A. Con Edison has filled six of these positions to
21 date. Prior to September 2006, the Company had
22 filled two of these positions. In September
23 2006, the Company hired three staff at salary
24 levels of $55,100, $61,000, and $65,000.

1 Recently, the Company announced that it hired a
2 Vice President in charge of all tax-related
3 matters.
4 Q. What are Staff's concerns with the Company's
5 forecasted labor costs associated with these
6 positions in the tax department?
7 A. Based on Con Edison's hiring pattern to date, we
8 do not believe that the Company will fill the
9 remaining positions by the rate year in this
10 case. Moreover, the actual salary levels of the
11 new tax department employees suggest that the
12 Company's average forecasted salary is
13 significantly overstated. Staff estimates that
14 Con Edison will hire four additional tax
15 department employees by the end of the rate
16 year. Staff's forecast includes the salaries of
17 the six positions filled to date, a secretary
18 for the Vice President, and four additional new
19 hires with an average salary level of $60,367.
20 This average salary level is based on the actual
21 salary of the three employees hired in September
22 2006. Staff's adjustment to company labor
23 related to the tax department employees is a
24 $58,737 reduction to the Company's request.

1 Q. Please explain your adjustment to company labor
2 associated with the 13 positions in the new
3 shared service organization.
4 A. Con Edison included a $256,000 increase to
5 company labor expense associated with its new
6 shared service organization. The increase
7 represents the gas portion of the payroll cost
8 for 13 new positions. Con Edison has already
9 filled 11 of the 13 new management positions.
10 However, the Company filled nine of the 11
11 positions from within the Company and no salary
12 increases were granted. Since the Company
13 filled these positions internally, there are no
14 incremental payroll costs being incurred by the
15 Company. In addition, Con Edison hired two
16 employees from Orange and Rockland. The payroll
17 costs of these two employees represent
18 incremental costs to Con Edison. The Company
19 plans to fill the remaining two positions,
20 either from Con Edison, Orange and Rockland, or
21 from outside sources, during 2007 at an
22 estimated salary of $91,000 each. Based on its
23 pattern in hiring the shared service employees
24 to date, Staff has assumed that only one of the

1 two remaining positions will be filled from
2 outside Con Edison and result in incremental
3 payroll costs. Therefore, Staff's adjustment to
4 company labor related to the new shared service
5 organization only includes incremental payroll
6 costs for the two employees hired from Orange
7 and Rockland and an estimated one additional
8 employee that will be hired from outside Con
9 Edison. Staff's adjustment reduces the gas
10 portion of the shared services organization
11 costs by $199,575.
12 Q. Are there other costs associated with the
13 reduction of the number of positions in the tax
14 and shared services organizations?
15 A. Yes. Staff also adjusted the employee fringe
16 benefits associated with Staff's reduction in
17 the number of new positions in the two
18 departments.
19 **Contract Labor**
20 Q. Does this Panel have any adjustments regarding
21 contract labor?
22 A. Yes. In response to CPB IR #34, the Company
23 indicated that there are $1.8 million of savings
24 related to the Company's advanced meter reading

1 (AMR) efforts which were not reflected in the
2 Company's filing and would be upon update. We
3 are assuming that these savings would result
4 from lower contract labor costs.
5 Q. Please explain.
6 A. AMR efforts will allow company labor currently
7 involved in meter reading to work on other
8 tasks. It is our understanding that much of
9 these tasks would otherwise be completed by
10 contract labor. Therefore, the AMR efforts
11 should lead to a reduction in contract labor
12 expenses.
13 **Consultants and Shared Service**
14 Q. Does Staff have any adjustments to consultant
15 and shared service expenses?
16 A. Yes. Staff adjusted rate year consultant
17 expense down by $27,000 and shared service
18 expense down by $115,544. Our adjustments
19 reflect normalizations of the historic year
20 costs and a known change related to consultant
21 fees.
22 Q. Please explain.
23 A. Con Edison included a $188,000 program change to
24 the rate year consultant expenses. The

1 Company's forecast was based on expected 2007
2 fee schedules for its consultants. However,
3 during the historic year the Company expensed
4 six months of certain consulting fees in the
5 amount of $110,000 as shared services expenses.
6 It will book all 12 months of the same fees to
7 consultant expense in the rate year. Staff
8 reclassified this amount to consultant expenses.
9 The reclassification reduced the Company's base
10 for forecasting shared services expense.
11 Therefore, the Company's forecast of rate year
12 shared services expense is overstated by
13 $110,000 plus inflation, or $ 115,544.
14 Q. Please explain your adjustment to the rate year
15 consultant expense.
16 A. Con Edison's board recently approved its 2007
17 fee schedule for its outside accounting and
18 auditing services. We relied upon this fee
19 schedule to produce our rate year forecast. Our
20 rate year forecast results in a $27,000
21 reduction to the Company's rate year consultant
22 expense.
23 **Duplicate Miscellaneous Charges**
24 Q. What is Staff's adjustment to duplicate

1 miscellaneous charges?
2 A. Our adjustment reduces the duplicate
3 miscellaneous charges, a credit to O&M expenses,
4 by $46,000.
5 Q. How did Con Edison estimate the duplicate
6 miscellaneous charges for the rate year?
7 A. Each year, Con Edison develops a rate for gas
8 used for internal purposes. The Company's
9 forecast was developed based on its 2007 rate.
10 The Company applied a 5.0% general inflation
11 factor to forecast the rate year. This
12 inflation factor represents expected inflation
13 for the period between the historic year and the
14 rate year.
15 Q. How does Staff adjust the rate year duplicate
16 miscellaneous charges?
17 A. Because an expense for the calendar year 2007 is
18 being used as the historic year amount, Staff
19 applies a general inflation factor from the 12-
20 month period ending December 31, 2007 to the
21 rate year, rather than from the 12-month period
22 ended June 30, 2006. The inflation factor is
23 1.57% for this period, according to the indexes
24 provided by the Company.

1 **Electric and Gas Used**

2 Q. What is the Staff adjustment to electric and gas
3 used?

4 A. Similar to the duplicate miscellaneous charges,
5 Staff's adjustment to electric and gas used
6 represents the same inflation adjustment. Staff
7 applies 1.57% to adjusted test year amount,
8 instead of the 5.0%, to forecast the rate year
9 amount. The Staff adjustment reduces the rate
10 year electric and gas used forecast by $8,300.

11 **Pension/OPEB Expense**

12 Q. Are there adjustments to Con Edison's rate year
13 forecast of gas net pension and OPEB expense?

14 A. Yes. To develop our rate year pension and OPEB
15 forecast, we used the latest available actuarial
16 information, provided by the Company in response
17 to Staff IR #273. In addition, we made three
18 specific adjustments to the Company's forecast
19 model. Our first adjustment eliminated the
20 effect of an amortization of a special 1993
21 early retirement incentive. Our second
22 adjustment was a change to the Company's labor
23 cap rate assumption. Our final adjustment was a
24 change to the Company's forecast of pension

1 costs to be billed to Orange and Rockland.
2 Q. Why do you propose to eliminate the early
3 retirement incentive from the Company's
4 forecast?
5 A. The amortization of the 1993 incentive cost will
6 expire in December 2007 for gas operations. The
7 Company's forecast, however, reflected the
8 amortization continuing through March 2008. Our
9 adjustment eliminates this expense after
10 December 2007.
11 Q. Why do you propose a change in the
12 capitalization assumption?
13 A. As previously stated, the Company recently
14 approved its labor cap rate of 34.5% for 2007.
15 The 2007 rate represents a small increase from
16 the 2006 rate of 33.75%, which was used by the
17 Company to develop its forecast. The updated
18 rate represents the actual rate the Company will
19 use for a portion of the rate year in this case.
20 As such, we recommend use of the 2007 rate for
21 developing the rate year forecast of pension and
22 OPEB expenses.
23 Q. Why do you propose a change to the Company's
24 forecast of pension costs billed to Orange and

1 Rockland?
2 A. Con Edison's gas pension cost was $3.7 million
3 for the historic test year ending June 2006.
4 The Company billed $395,000, or about 10.7% of
5 gas pension cost, to its affiliate Orange and
6 Rockland. For the rate year, the Company
7 forecasts gas pension costs of $14 million but
8 billings to Orange and Rockland of $176,000,
9 which represent only 1.3% of the total. The
10 Company offered no basis for the forecasted
11 decline in billings to its affiliate,
12 particularly given the significant forecasted
13 increases in pension costs. We forecast rate
14 year pension cost billings to Orange and
15 Rockland in the same proportion to the actual
16 billings for the period July 2005 through
17 December 2006.
18 Q. Please summarize the impact of your adjustments
19 to rate year pension and OPEB expense.
20 A. In total, our adjustments reduce the Company's
21 original rate year pension and OPEB expense
22 forecast of $13,953,000 by $2,969,500, to
23 $10,983,500.
24

1 **Pension and OPEB Reconciliation**

2 Q. Does the latest available actuarial information
3 have any other impact on the Company's rate case
4 filing?

5 A. Yes. Con Edison is seeking recovery of
6 estimated under-recovered pension and OPEB
7 costs, which are deferred pursuant to the
8 Commission's Pension Policy Statement. The
9 under-recovered costs represent the difference
10 between the rate allowances for the term of the
11 2004 Rate Plan and the Company's actual and
12 expected costs. Con Edison seeks recovery of
13 these deferred costs over a three-year period.
14 Based on the updated actuarial information and
15 our other proposed adjustments, we forecast a
16 slight reduction in this under-recovery from
17 $34.4 million to $32.6 million.

18 Q. Do you support the Company's request to recover
19 these deferred pension and OPEB cost over three
20 years?

21 A. No. We recommend that the Commission consider a
22 recovery period of five years or more. A five-
23 year amortization period would reduce the
24 resultant revenue requirement impact by $4.5

1 million, from $11.2 million to $6.7 million.
2 Q. Why do you think a longer recovery period is
3 appropriate?
4 A. The rate increase sought by Con Edison in this
5 case is significant. The three-year recovery
6 period proposed by Con Edison has a revenue
7 requirement impact of over $11 million, or
8 approximately 2% of delivery revenues. A longer
9 amortization period will mitigate the rate
10 impact. Moreover, the majority of the projected
11 $32.6 million under-recovery did not represent a
12 cash outlay for Con Edison. As such, extending
13 the recovery period should not have any
14 significant effect on the Company's cash flow
15 position.
16 Q. Please explain why a portion of the deferred
17 under-recovery balance does not represent a cash
18 outlay for Con Edison.
19 A. Case 03-G-1671 provided Con Edison rate
20 allowances for the recovery of forecasted
21 pension and OPEB expenses for the three years of
22 the 2004 Rate Plan. Pursuant to the
23 Commission's Policy Statement, the Company is
24 authorized to defer for future rate disposition

1 the difference between the rate allowances and
2 its actual Statement of Financial Accounting
3 Standards (SFAS) No. 87 Pension and SFAS No. 106
4 OPEB expense accruals. The accrual of pension
5 and OPEB costs on the Company's books does not
6 represent a cash outlay. It is simply an
7 accounting entry based on an actuarial analysis.
8 As a result, differences between the actual
9 expense accruals and the levels provided in
10 rates do not represent cash expenditures.
11 Q. When do pension and OPEB benefit costs become
12 cash expenditures for the Company?
13 A. Pension and OPEB employee benefits become cash
14 expenditures when the utility funds its benefit
15 plans.
16 Q. Has Con Edison funded its pension and OPEB
17 benefit fund plans during the term of the 2004
18 rate plan?
19 A. While Con Edison has funded, and projects to
20 fund, its OPEB plans with cash roughly equal to
21 its SFAS 106 accrual during the term of 2004
22 rate plan, it has only funded its pension plan
23 once since 1997. That was done in September
24 2006.

1 Q. Why is it important to consider the non-cash
2 nature of deferred under-recovered pension costs
3 in this case?
4 A. The Company includes $34.4 million of projected
5 deferred pension and OPEB under-recoveries in
6 rate base. Rate base should include cash
7 expenditures which created an internal or
8 external financing need for the Company. A
9 significant portion of these under-recoveries
10 included in rate base, however, were never
11 funded and as such have not created a financing
12 need for the Company. Since, there is limited
13 cash outlay related to the pension under-
14 recovery, there is a limited financing
15 requirement. Therefore, only the cash portion
16 of the pension under-recovery is properly
17 included in the Company's rate base.
18 Q. What do you propose?
19 A. We will reduce the $34.4 million rate base
20 amount to reflect only the cash outlays related
21 to pension and OPEB funding above and beyond the
22 amounts included in rates.
23 Q. Do you know the level of cash Con Edison
24 expended to fund its pension and OPEB plans that

1 was in excess of rate allowances?
2 A. No. While the Company indicates in response to
3 Staff IR #275, Part C, that it will update rate
4 base to reflect the non-cash amount of the
5 pension and OPEB expenses, it has not yet
6 provided the update. Until a better estimate
7 becomes available, we recommend the use of a
8 placeholder for both the OPEB and pension
9 amounts. For OPEBs, the placeholder would
10 assume that the Company funded its OPEB plans at
11 a level equivalent to its SFAS 106 expense
12 levels. For pensions, we allocated the
13 September 2006 total Company cash outlay to gas
14 operations in a manner consistent with the
15 Company's pension expense forecast methodology.
16 We estimate that Con Edison's cash outlay
17 related to under-recovered pension and OPEBS
18 costs are $11.2 million ($5.2 million for
19 pensions and $6 million for OPEBs). Reflecting
20 a five-year amortization period of the under-
21 recovery, we recommend that the Company's $17.2
22 million net-of-tax unamortized balance included
23 in rate base be reduced by $11.2 million, to $6
24 million.

1 Q. Are there any other issues with respect to the
2 pension and OPEB under-recovery?
3 A. Yes. While the Company included the pension and
4 OPEB under-recovery in rate base, it did not
5 include these deferred costs in the
6 determination of its EBCAP adjustment.
7 Q. Is this proper?
8 A. No, it is not. The EBCAP should include all
9 rate base elements. Therefore, we recommend
10 adjusting the Company's EBCAP measurement to
11 reflect deferred OPEB under-recoveries. We
12 estimate that the average net-of-tax balance of
13 under-recovered OPEB costs was $1 million for
14 the historic test year.
15 **Pension Policy Statement**
16 Q. Has the Pension Policy Statement always applied
17 to Con Edison's gas operations?
18 A. No. Con Edison's gas operations returned to the
19 provisions of the Pension Policy Statement
20 effective October 1, 2004. The Company had gone
21 off the Pension Policy Statement, effective
22 April 1, 1997, consistent with the terms of the
23 rate plan adopted in Case 96-E-0897.
24 Q. Why is it a significant event that the Company

1 returned to the provisions of the Pension Policy
2 Statement?
3 A. As discussed previously, the Pension Policy
4 Statement permits the reconciliation of the
5 difference between the rate allowances for
6 pension and OPEBs and the actual accrued pension
7 and OPEB expenses. In addition, the Pension
8 Policy Statement contains numerous other
9 technical provisions. The present rate case is
10 Staff's first opportunity to test the quality of
11 Con Edison's compliance with the Pension Policy
12 Statement.
13 Q. Is Con Edison in full compliance with the
14 Pension Policy Statement?
15 A. No. We identified a number of issues with
16 respect to the Company's current and proposed
17 treatment of its internal reserves for OPEBs,
18 also known as OPEB liability, and for pensions,
19 also known as prepaid pensions.
20 Q. Please explain the concern with Con Edison's
21 treatment of its OPEB liability.
22 A. The Commission's Policy Statement on pension and
23 OPEBs requires companies following the Statement
24 to accrue interest on the unfunded OPEB

1 obligation or OPEB liability at the Company's
2 pre-tax overall rate of return. We found that
3 Con Edison has not recorded any interest on its
4 OPEB liability since its return to the Policy
5 Statement on October 1, 2004.
6 Q. Do you have an interest calculation to offer?
7 A. Yes. We calculate that for the period October
8 1, 2004 through June 30, 2006, Con Edison should
9 have accrued $125,000 of interest on its
10 unfunded OPEB liability related to gas
11 operations.
12 Q. What do you recommend?
13 A. To rectify the non-compliance with the
14 provisions of the Pension Policy Statement, the
15 Commission should require Con Edison to record
16 the interest that should have been accrued on
17 the Company's unfunded OPEB liability through
18 the date of the Commission's Order in this case.
19 Prospective application of such interest, in
20 compliance with the Policy Statement, should
21 also be required. Otherwise customers will be
22 denied this benefit and as a result will likely
23 bear higher OPEB costs in the future.
24

1 **Prepaid Pension - EBCAP**
2 Q. Did Con Edison include its prepaid pension
3 expense in its rate base request?
4 A. Yes. The Company's Accounting Panel, on page
5 59, acknowledges that the Company has included
6 its prepaid pension expense in its rate base
7 compilation as part of its EBCAP measure.
8 Q. Does Staff have any concerns with Con Edison's
9 proposed treatment?
10 A. Yes, the majority of the prepaid pension balance
11 was amassed while the Company was off the Policy
12 Statement. Moreover, a significant portion of
13 the so-called prepaid pension expense does not
14 represent a cash investment for Con Edison.
15 Q. How large is the prepaid pension expense?
16 A. Con Edison has accumulated a significant prepaid
17 pension expense balance. As noted by the
18 Company's Accounting Panel, the average balance
19 of the gas prepaid pension expense was $232
20 million for the historic year ended June 2006.
21 Q. How do prepaid pension expense balances arise?
22 A. There are two ways a prepaid pension balance can
23 occur. It can occur when management, at its
24 discretion, makes contributions to, or funds,

1 its pension plan with cash in excess of the rate
2 allowances. A prepaid pension balance can also
3 occur when a negative pension expense is accrued
4 on the company's books. Con Edison's prepaid
5 pension balance developed as the result of this
6 latter situation rather than the Company
7 actually making cash contributions to the
8 pension fund in excess of its rate allowances.
9 Thus, Con Edison's prepaid pension expense
10 balance is not a cash prepaid expense, but
11 rather the balance sheet effect that results
12 from the accrual of negative pension expense.
13 Q. Were negative pension expenses reflected in Con
14 Edison's gas rates?
15 A. Partially. Con Edison's gas operations started
16 recording negative pension expense accruals in
17 1998. However, negative pension expense
18 allowances were not reflected in gas rates until
19 2002.
20 Q. Were differences between rate allowances and
21 actual pension accruals reconciled and deferred
22 for the benefit of ratepayers?
23 A. No. Effective April 1, 1997, Con Edison went
24 off the Pension Policy Statement and suspended

1 the reconciliation of rate allowances to actual
2 pension and OPEB accruals. As noted previously,
3 the Company returned to this Policy Statement
4 requirement effective October 1, 2004 for its
5 gas operations.
6 Q. How did Con Edison's actual pension accruals
7 compare to its rate allowances while the Company
8 was off the Pension Policy Statement?
9 A. Based on information provided by the Company, we
10 determined that Con Edison's actual gas pension
11 expenses were negative $152 million for the
12 period it was off the Policy Statement. During
13 this period rate allowances for gas pensions
14 totaled negative $98 million. Therefore, the
15 Company's actual pension expenses were $54
16 million lower than the level set in rates.
17 Since the Company was off the Policy Statement
18 at that time, the benefits of these savings
19 flowed to shareholders, not ratepayers.
20 Q. Why is the inclusion of the prepaid pension
21 expense balance in rate base problematic?
22 A. The inclusion of the prepaid pension expense
23 will provide the Company a cash return on the
24 prepaid pension expense balance. A significant

1 portion of the Company's prepaid pension expense
2 is not associated with any cash outlay. As
3 such, the request to include the non-cash
4 component in rate base has no merit. Moreover,
5 the non-cash component of the prepaid pension
6 expense is not associated with any benefits
7 realized by customers. Customers received a
8 benefit only to the extent that pension credits
9 were reflected in the rates they paid. Con
10 Edison retained pension credits in excess of
11 those reflected in rates since it was not on the
12 Pension Policy Statement and now is attempting
13 to earn a return on the resultant profits it
14 earned while off the Pension Policy Statement.
15 To require customers to pay carrying costs on
16 the portion of a benefit they never received
17 (because it flowed to shareholders) is
18 inequitable and inappropriate.
19 Q. The Company's Accounting Panel, starting on page
20 59, suggests that negative pension costs
21 resulted in a cash financing requirement for the
22 Company. Do you agree?
23 A. No. While the Company's Accounting Panel
24 properly states that negative pension expenses

1 or credits were non-cash, they also suggest that
2 these non-cash credits were used to reduce the
3 Company's operating costs. As a result, the
4 revenue requirement was reduced and cash flow
5 was reduced. The Company's argument misses the
6 point, however, because it fails to focus on the
7 fact that the prepaid balances were also derived
8 from differences between the negative pension
9 credits reflected in rates and the even greater
10 negative pension expenses actually booked by the
11 Company. While the Company is correct that cash
12 flow was reduced by the credits reflected in
13 rates, its position does not consider the fact
14 that cash flow was in no way affected by the
15 prepaid balances generated by the even greater
16 negative pension expenses booked by the Company.
17 Put another way, the Company's position is true
18 only to the extent the pension credits were
19 reflected in rates. Credits in excess of those
20 reflected in rates resulted in non-cash earnings
21 on which the Company now inappropriately seeks
22 to earn a return.
23 Q. How do you propose to remedy this situation?
24 A. We propose that the Commission consider the

1 portion of the prepaid pension balance that is
2 equivalent to the pension credits that were not
3 reflected in rates as a non-regulated asset. We
4 propose to adjust the Company's capitalization
5 to eliminate the capital supporting this non-
6 regulated asset. We reflected our adjustment in
7 the EBCAP adjustment to the Company's rate base.
8 Q. What is the amount of your proposed adjustment?
9 A. We calculated that for the period April 1997
10 through September 2004, Con Edison's actual gas
11 pension expense was $54 million less than the
12 amounts provided in rates. We recommend that
13 the net-of-tax amount of this difference, $32.4
14 million, be reflected as an adjustment to the
15 Company's capitalization supporting gas
16 operations.
17 **Employee Welfare Expenses**
18 Q. Please explain Staff adjustments to employee
19 welfare expenses.
20 A. Staff's first adjustment to employee welfare
21 expenses relates to the Company's program change
22 for the work home wellness programs.
23 Q. What is the basis of Staff's adjustment?
24 A. The $134,998 program change to employee welfare

1 expenses represents the gas allocation of the
2 costs for a new work home wellness program,
3 Active Health. The program was introduced to
4 help control health care costs and manage
5 employee absences, according to the testimony of
6 Con Edison witness Hector Reyes. However, the
7 Company did not reflect any cost savings from
8 this program in its rate year revenue
9 requirement. Staff's adjustment of $134,998
10 reflects elimination of the cost for the new
11 program under the assumption that the program
12 will produce savings at least equal to the
13 program costs. The Company bears the burden of
14 justifying costs associated with any new
15 program. The Company failed to quantify the
16 cost benefits of the program in its rate filing.
17 Q. What is Staff's next adjustment to employee
18 welfare expenses?
19 A. The next adjustment is to the health insurance
20 cost.
21 Q. Please explain.
22 A. The Company's forecast of health insurance costs
23 in the rate year was developed based on contract
24 rates and the number of participants as of July

1 1, 2006. The historic year dental insurance
2 costs were then escalated by 8.75% to arrive at
3 the rate year estimates. Test year prescription
4 drug costs were escalated by 9.5%. The hospital
5 and medical insurance costs were escalated by an
6 effective rate of 12.18%, as indicated in
7 Company Exhibit__(HJR-1). Staff starts with the
8 latest available information, the updated 2007
9 contract rates and number of participants, to
10 determine the Company's costs for the calendar
11 year 2007. Staff then escalates the 2007 health
12 insurance costs by the general inflation factor,
13 2.10%, calculated from the inflation indexes
14 provided by the Company, to forecast health
15 insurance costs for calendar year 2008. Our
16 rate year health insurance forecast represents
17 the combination of three months of 2007 costs
18 and nine months of 2008 costs. Staff's approach
19 results in a $711,168 reduction to the Company's
20 rate year employee welfare expenses.
21 Q. Why does Staff disagree with Con Edison's
22 forecasts?
23 A. The gross domestic product inflation indexes
24 reflect a basket of goods and services,

1 including health care. The use of a separate
2 escalation factor in projecting health care
3 costs, other than the general inflation factor,
4 is inconsistent with the Commission's practice,
5 as stated in Commission Opinion No. 84-27,
6 issued October 12, 1985 in Case 28695. Staff's
7 adjustment reflects the latest known costs plus
8 general inflation.
9 Q. Do you have any other adjustment to employee
10 welfare expenses?
11 A. Yes. Staff's last adjustment tracks reductions
12 in rate year company labor resulting from our
13 adjustments to the tax department and shared
14 services organization program changes.
15 Q. Please continue.
16 A. Con Edison included $138,000 of employee welfare
17 expenses related to the gas allocation of fringe
18 benefits for its new employees. Since ten of
19 the management personnel in the new shared
20 service organization do not represent new hires,
21 the Company did not and will not incur
22 additional costs for employee fringe benefits.
23 Staff's estimate of 11 new hires (ten tax
24 employees and one additional secretary) in the

1 tax department instead of the 12 proposed by Con
2 Edison also reduces the forecasted cost of
3 employee fringe benefits. Staff applies the
4 fringe benefit rate per employee developed by
5 Con Edison to the total 13 employee reduction to
6 reduce the forecast of new employee fringe
7 benefit costs. The $27,820 staff adjustment
8 represents gas allocation of the expected
9 reduction.

10 **Injuries and Damages**

11 Q. Please describe your adjustment to injuries and
12 damages.
13 A. Our forecast of rate year injuries and damages
14 expense is based on net claims disbursements
15 payments, whereas the Company's was based on
16 gross disbursements. We discovered that the
17 Company has consistently recovered from various
18 sources a portion of its injuries and damages
19 disbursements. We reflected the recoveries in
20 our forecast and it results in a $1,258,000
21 reduction to the Company's rate year estimate.
22 Q. How has the Company estimated the rate year
23 injuries and damages expense?
24 A. On page 44 of its testimony, the Company's

1 Accounting Panel states that, "[I]n accordance
2 with prior Commission practice, the rate year
3 level of injuries and damages is equivalent to
4 the annual average of all claim disbursements
5 for the three-year period July 2003 through June
6 2006."
7 Q. Do you agree with this method?
8 A. It is customary to use average disbursements to
9 forecast this expense item. However, while the
10 Company uses the total of all claim
11 disbursements as the basis for the forecast,
12 this computation should instead take into
13 account the net payments associated with claims
14 related to injuries and damages. Indeed, a
15 review of the Company's accounts shows that the
16 Company recovers portions of these disbursements
17 every year. The recoveries reduce the Company's
18 cost and therefore should be factored in to
19 arrive at the forecasted level of expense.
20 Q. Please indicate the effects of using the
21 disbursements net of recoveries.
22 A. Staff has computed the amounts recovered during
23 the relevant three-year period and has
24 determined the average allocated to gas to be

1 $1,258,000, with inflation. Staff has therefore
2 reduced the rate year injuries and damages
3 expense accordingly.
4 **Materials and Supplies**
5 Q. Please explain the adjustment to materials and
6 supplies expense.
7 A. The Company's forecasted rate year level of
8 materials and supplies expense is $2,541,000.
9 The Company's forecast included a number of
10 program changes. Staff's GCCOP recommends a
11 decrease of $116,000 related to two of the
12 Company's program changes: tunnel programs and
13 cast iron maintenance programs. The Company's
14 forecast of these program changes included an
15 inflation factor. Our adjustment eliminates the
16 $6,000 of inflation related to the disallowed
17 program changes. Staff's rate year level
18 forecast of materials and supplies is
19 $2,419,000, $122,000 less than the Company's
20 forecast.
21 **MGP/Superfund**
22 Q. Please explain the Company's proposal for the
23 treatment and recovery of MGP/Superfund costs.
24 A. The Company proposes to continue the expense

1 true-up mechanism for MGP/Superfund costs
2 allowed in the existing rate plan but proposes
3 that the target level of $800,000 in its
4 proposed rate plan be updated. The Company
5 testimony notes that funds available for
6 remediation efforts from insurance recoveries,
7 divestiture of Con Edison generating assets and
8 prior collections from ratepayers at the time
9 the allowance was set have been used up. As of
10 September 30, 2006, gas operations disbursements
11 exceeded recoveries by almost $4 million.
12 Exhibit__(EJR-1), Schedule 4, page 3 of 3, also
13 shows that the projected spending from October
14 1, 2006 through the end of the first rate year
15 ending September 30, 2008 will be $128 million,
16 of which gas operations will be responsible for
17 $20.8 million. The Company proposes a three-
18 year amortization of this combined requirement
19 of $24.5 million, or $8.179 million per year.
20 This amount, plus the existing rate allowance,
21 results in the Company's requested rate target
22 of $8.932 million.
23 Q. Do you agree with the Company's proposal?
24 A. We do concur with the Company that the existing

1 expense true-up mechanism allowed in the
2 existing rate plan should continue, but we do
3 not agree that an annual rate allowance of
4 $8.932 million is required at this time.
5 Q. Please explain.
6 A. Our first difference is with the quantification
7 of the program change necessary to reflect the
8 Company's three-year amortization. As
9 acknowledged by the Company in their responses
10 to Staff IR #22 and Staff IR #23, the Company's
11 requested program change of $8.179 million
12 should have reflected the current rate allowance
13 of $753,000 per year as a partial recovery of
14 environmental spending from October 1, 2006
15 through September 30, 2007. Furthermore, the
16 existing rate allowance of $753,000 should have
17 been deducted, rather than added to the
18 Company's resulting three-year expense of $8.179
19 million per year. Correcting for these two
20 items decreases the Company's requested rate
21 allowance by $1.004 million to $7.928 million.
22 Q. Please continue.
23 A. Our remaining difference relates to the
24 Company's three-year recovery period. When

1 considering the size of the rate increase sought
2 by the Company, we believe that a three-year
3 recovery of a little over two years of largely
4 projected spending for MGP costs is
5 unreasonable. We recommend that the MGP rate
6 allowance reflect a five-year amortization of
7 the September 30, 2006 deferred balance plus the
8 projected spending from October 1, 2006 through
9 September 30, 2008. This change further reduces
10 the MGP/Superfund environmental rate allowance
11 by $3.171 million to an allowance of $4.757
12 million. Staff's total adjustment to this cost
13 is $4.175 million.
14 **Postage**
15 Q. The Company has proposed an increase in its
16 postage expense related to a pending increase in
17 postage rates. Do you agree with the Company's
18 forecast?
19 A. At this time, the Postal Rate Commission has not
20 yet decided on a request of the U.S. Postal
21 Service (USPS) to increase postage rates. We
22 have not provided an adjustment to this expense.
23 However, should new postage rates which differ
24 from the amounts requested by the USPS become

1 known prior to the Commission deciding this
2 proceeding; we recommend that the amount be
3 updated.

4 **Other O&M**

5 Q. Please continue with your next group, other O&M
6 expense.
7 A. The Company's proposed rate year level of other
8 O&M expense is $13,640,000. The Company's
9 forecast included a number of program changes.
10 Of these programs changes, the Company
11 acknowledges changes to gas survey and
12 facilities programs. This Panel proposes an
13 adjustment regarding the program change related
14 to the law imaging project. In addition, Staff
15 witness Rosenthal has proposed an adjustment
16 related to the Company's bill redesign project.
17 Q. Please explain the adjustments that the Company
18 acknowledges for gas surveys and facilities
19 programs.
20 A. In response to Staff IR #252, the Company
21 acknowledges a decrease of $75,000 relating to
22 program changes for its gas surveys. In
23 response Staff IR #250, the Company acknowledges
24 a decrease of $280,000 relating to a program

1 change for its facilities programs. The
2 Company's forecast of these program changes
3 included an inflation factor. Our adjustment
4 eliminates the $18,000 of inflation related to
5 the reduction of expenses for these program
6 changes.
7 Q. Please explain your adjustment related to the
8 Company's proposed law imaging projects.
9 A. Con Edison included a $61,000 program change to
10 other O&M expense for its rate year law imaging
11 projects: $26,000 for scanning of historic
12 regulatory documents, $26,500 for purchase of
13 software to more efficiently manage electronic
14 discovery in major litigation matters, and
15 $8,000 for the design and implementation of an
16 online catalog for easy access from desktop
17 computers. However, these costs are rate year
18 only expenditures according to the Company's
19 response to Staff IR #263. Staff proposes to
20 amortize these costs over a three-year period,
21 i.e. $20,333 per year. Staff's adjustment
22 reduces rate year other O&M expense by $40,667.
23 The Company's forecast of this program change
24 included an inflation factor. Our adjustment

1 eliminates the $2,000 of inflation related to
2 the reduction of expenses for this program
3 change. Offsetting the Staff adjustment to the
4 law imaging projects are the on-going software
5 maintenance costs in the amount of $2,708 per
6 year, which represent the gas allocation of the
7 total estimated annual cost of $20,500 (Staff IR
8 #290).
9 Q. What is Staff's net adjustment to other O&M
10 expense related to the law imaging projects?
11 A. Staff's net adjustment reduces other O&M expense
12 related to the law imaging projects by $39,959.
13 Q. Please explain the adjustment related to the Con
14 Edison's bill redesign project.
15 A. Staff witness Rosenthal has proposed to remove
16 the gas portion of the costs associated with a
17 bill redesign project out of other O&M expense
18 and into the Company's general outreach and
19 education budget. Other O&M expense has been
20 adjusted by $42,000 to reflect this
21 recommendation. The Company's forecast of this
22 bill design project included an inflation
23 factor. Our adjustment eliminates the $2,000 of
24 inflation related to the reduction of expenses

1 for this project.

2 Q. Please explain your adjustment to other O&M
3 expense as it relates to general inflation.

4 A. The Company utilized a general inflation factor
5 of 5% to forecast expected increases from
6 historic year levels for many of its cost
7 elements. However, for other O&M expense the
8 Company used a 5.33% inflation factor without
9 any justification for the discrepancy.
10 Adjusting the forecast to reflect the Company's
11 general inflation factor reduces the Company's
12 rate year forecast of other O&M expense by
13 $37,000.

14 Q. Please summarize the total adjustment to other
15 O&M expense.

16 A. Our total adjustment to other O&M expense is
17 comprised of $394,000 related to programs
18 changes, $42,000 related to bill redesign, and
19 $59,000 related to inflation for a total
20 decrease of $495,000. Staff's rate year level
21 for other O&M expense is $13,145,000.

22 **Property Taxes**

23 Q. What is the basis of your adjustment to property
24 tax expense?

1 A. Our adjustment to the Company's rate year
2 property tax expenses reflects Staff's estimated
3 changes in the New York City (NYC) property tax
4 rates and the level of forecasted Westchester
5 property taxes.
6 Q. How did the Company determine its rate year
7 estimate for NYC property taxes?
8 A. The Company forecasted the rate year level based
9 on the forecasted assessed values of the gas
10 properties, including forecasted construction
11 expenditures, and an estimated tax rate for
12 properties that are classified as class 3 and
13 class 4. The Company estimated tax rate was
14 based on a 0% tax rate escalation factor, which
15 was developed "from historical experience and
16 judgment".
17 Q. Do you agree with the Company's escalation rate?
18 A. We do not. In 2003, NYC imposed an 18.5%
19 across-the-board rate increase. This increase,
20 which took effect in the middle of the 2002-2003
21 tax year and outside of the regular assessment
22 period, is unusual and not likely to reoccur.
23 Therefore, the effect of this unusual increase
24 should be removed from the computation of the

1 average escalation rate.

2 Q. Has the Company accounted for that event in its
3 computation?

4 A. On page 19 of his testimony, Company witness
5 Hutcheson indicated that he has not considered
6 that abnormal increase in his analysis to arrive
7 at the 0% escalation factor. To do so, the
8 Company has developed the equivalent of a six-
9 year average historic growth rate for the period
10 2000-2001 to 2006-2007, from which the 2003-2004
11 escalation was ignored.

12 Q. How do you propose to eliminate this abnormal
13 change in the NYC property taxes?

14 A. Since this event occurred during the fiscal tax
15 year 2002-2003, we used the average changes that
16 have occurred for the years since the unusual
17 mid-year increase. A four-year average of the
18 tax rate changes from the rate in effect at the
19 end of the 2002-2003 tax year to the 2006-2007
20 tax year produces annual escalation rates of
21 negative 1.12% and negative 1.27% for class 3
22 and class 4 properties, respectively, as opposed
23 to the 0% developed by the Company.

24 Q. Are you proposing other changes to the property

1 tax expense?
2 A. Yes. We have a change to the Westchester
3 portion of property taxes.
4 Q. Please indicate how the Company accounted for
5 the Westchester portion.
6 A. Mr. Hutcheson indicated on page 19 of his
7 testimony that he has simply escalated 2006
8 taxes by a percentage that he has developed
9 based on actual experience. The Company's
10 growth rate of 2.73% was developed based on
11 actual Westchester tax expense for the period
12 2002 to 2006.
13 Q. Please explain the proposed change to this
14 computation.
15 A. We discovered an error in the Company's
16 development of its growth rate. The Company's
17 forecast model did not properly compute the
18 impact of the 2006 tax change. Correction of
19 the formulaic error results in a growth rate of
20 2.25%.
21 Q. What is the total impact on the rate year
22 property tax expense forecast as determined by
23 Staff?
24 A. For the rate year, the application of the NYC

1 escalation rates and the Westchester growth rate
2 change resulted in a decrease in the level of
3 rate year property taxes of $2.425 million.
4 Q. Do your proposed adjustments have an impact on
5 any other aspect of the rate year revenue
6 requirement?
7 A. Yes. As a result of the changes, the estimated
8 prepayments associated with the property taxes
9 should be reduced by $618,000.
10 Q. Do you propose that the property tax expense
11 forecast be updated during this proceeding?
12 A. Yes. The tax rates for the 2007-2008 tax year
13 should be known by July 2007. That means that
14 the actual property tax expense for the first
15 nine months of the rate year will be known
16 before the Commission established rates in this
17 case. We propose that the actual property tax
18 expense be used to determine property tax
19 expenses for the first nine months of the rate
20 year, and that the five-year average of the tax
21 rate changes from the 2003-2004 tax year to the
22 2007-2008 tax year be used as the escalation
23 rate to determine the 2008-2009 tax rate, which
24 will impact the final three months of the rate

1 year.

2 **Rate Base**

3 **Earnings Base / Capitalization**

4 Q. Please briefly describe the nature of the EBCAP
5 adjustment.

6 A. This adjustment reduces the rate year rate base
7 by $12.703 million to account for an error made
8 by the Company in calculating its EBCAP
9 adjustment.

10 A. What is the purpose of the EBCAP element in rate
11 base?

12 Q. The EBCAP is a computation intended to bring
13 rate base and capitalization into alignment so
14 that the basis upon which a return can be earned
15 reflects only the investor-supplied capital
16 dedicated to public service.

17 Q. What data was used in this computation?

18 A. Traditionally, the EBCAP is based on data from
19 the Company's books and records for the
20 historical year under consideration. In this
21 instance, the data are for the period ended June
22 30, 2006.

23 Q. What is the basis of Staff's adjustment?

24 A. During the discovery phase of this case, Staff

1 found that the equity amount included in the
2 capitalization was different than the amount on
3 the Company's books. The Company has stated
4 that the information in the rate case filing was
5 from an internal report rather than the book
6 record. The Company has indicated that the
7 oversight will be corrected in their update.
8 **World Trade Center Costs**
9 Q. What does the company propose with respect to
10 its World Trade Center (WTC)-related costs?
11 A. Con Edison proposes to recover $22.2 million of
12 deferred O&M expenditures and accrued interest
13 that relate to the WTC incident over a three-
14 year period, or $7.4 million per year. In
15 addition, the Company seeks to recover $12.7
16 million of deferred capital expenditures over a
17 thirty-year period, or $422,000 per year. The
18 unamortized deferred net-of-tax balances have
19 been included in the Company's rate base
20 request. The Company believes it is unlikely
21 that it will be reimbursed for these costs from
22 insurance and/or federal funds.
23 Q. Can you provide any information on the potential
24 for Con Edison to obtain such recovery?

1 A. Yes. The federal government has appropriated
2 $750 million to reimburse utility providers for
3 their losses. A process has been established
4 for the review of utility claims and is
5 underway. Con Edison's WTC-related costs fall
6 into three categories: restoration and
7 emergency response, rebuilding of facilities,
8 and interference. Review of Con Edison's claim
9 for restoration and emergency response costs is
10 complete. The Company was reimbursed for 100%
11 of its qualifying costs in this category. Con
12 Edison appealed the disallowance of accrued
13 interest as an eligible expense and recently
14 Empire State Development Corporation determined
15 that the company should be reimbursed for
16 accrued interest. On February 7, 2006, Con
17 Edison filed its claim for interest on
18 restoration and emergency response costs
19 consistent with Empire State Development
20 Corporation's guidelines.
21 The costs that Con Edison seeks recovery of
22 in this case fall into all three categories plus
23 accrued interest as well as other related costs.
24 The Company seeks recovery of 25% of rebuilding

1 costs incurred since federal reimbursement will
2 be limited to 75% of expenditures. The Company
3 seeks recovery of interference costs incurred to
4 date on the basis that the federal appropriation
5 will be inadequate to cover all of its
6 interference costs. The administrative agencies
7 disbursing the federal funds have commenced
8 review of the Company's permanent restoration
9 costs. Con Edison received a $30 million
10 advance payment shortly after filing its
11 permanent restoration costs application. It is
12 our understanding that the review of the
13 Company's permanent restoration cost application
14 is complete and the Company will soon receive a
15 $70 million payment. The gas portion of these
16 reimbursements is not known at this time.
17 Moreover, the Company has an opportunity to
18 appeal the audit team's findings. The
19 application for interference costs is not yet
20 available to the Company.
21 Q. What concerns do you have with Con Edison's
22 proposed recovery of these costs?
23 A. Much remains unknown regarding the Company's
24 costs and reimbursement levels. The Company is

1 seeking recovery of WTC-related costs from
2 customers when neither the Company nor Staff can
3 definitively state what the Company's net cost
4 will be. Estimates of various costs and
5 expected reimbursement levels are all that can
6 be offered. Costs are still being incurred and
7 the federal review process is still underway.
8 Even at this late date, much remains unknown
9 regarding the federal reimbursement levels.
10 Finally, the Company is seeking recovery of
11 interference costs from customers in advance of
12 seeking federal reimbursements. We do not fault
13 the Company for this since the application is
14 not yet available to the Company. However, the
15 Company's request in this case does not reflect
16 any anticipated reimbursements for interference
17 costs.
18 Q. How is this issue being addressed by the
19 Commission?
20 A. In 2001, Con Edison filed a petition with the
21 Commission in which it seeks authority to defer
22 and recover its WTC-related costs, Case 01-M-
23 1958. The Commission held that it was premature
24 to consider the petition because other avenues

1 of recovery of these costs have not yet been
2 exhausted. We expect that once those
3 reimbursement options are settled, the
4 Commission will address the appropriate
5 treatment of these costs in that proceeding.
6 Q. Does the Panel have any interim recommendations
7 on this issue?
8 A. Yes. We recognize the extraordinary nature of
9 these expenditures and that they could have cash
10 flow consequences for the Company in the short-
11 term. While we have not audited the WTC-related
12 expenditures in any detail, Staff has monitored
13 the Company's restoration and rebuilding
14 activities and Empire State Development
15 Corporation's review of the Company's
16 reimbursement claims. We believe that the
17 majority of the costs can be considered prudent
18 expenditures. Therefore, as an interim measure,
19 until all of the costs are known and all of the
20 reimbursement issues are settled, we recommend
21 that the Commission allow the Company's request
22 to amortize $7.8 million of O&M expenses and
23 deferred capital expenditures per year and to
24 include the unamortized balances of deferred WTC

1 costs in its rate base. The inclusion of
2 deferred costs in the Company's rate base will
3 eliminate the need to accrue interest on them.
4 This treatment should be subject to full
5 reconciliation based upon actual expenditures
6 net of federal and insurance recoveries, the
7 establishment of appropriate amortization
8 periods for the various categories of both
9 capital and O&M expenditures, or other treatment
10 as the Commission may prescribe in Case 01-M-
11 1958.

12 **Other Rate Base Items**

13 Q. Are there other planned revisions to the rate
14 base as filed?
15 A. The Company has also indicated that two items
16 included in the rate base in error will be
17 revised in their update. Deferred Federal
18 Income Taxes (FIT) on Excess Deferred State
19 Income Taxes (SIT) in the amount of $208,000, as
20 well as Deferred FIT on SIT of $8.0 million,
21 should be taken out of rate base.

22 **Accumulated Deferred Taxes -**
23 **Change of Accounting Section 263A**

24 Q. Do you have any concerns that may impact the

1 deferred federal income taxes reflected in the
2 Company's rate base in this case?
3 A. Yes. The Company's rate base includes average
4 accumulated deferred taxes for the rate year of
5 $65.699 million associated with tax accounting
6 changes made under Section 263A of the Internal
7 Revenue Code. Starting in 2002, Con Edison
8 began to use the "simplified service cost
9 method". This permitted the Company to obtain
10 expense deductions for costs and assets that
11 would have otherwise been depreciated over a 15-
12 to 20-year period. As noted in the Company's
13 response to Staff IR #285 Revised, the Internal
14 Revenue Service is disputing the Company's
15 calculation of this deduction claimed for the
16 years 2002 through 2005. The gas rate filing
17 reflects the deduction claimed for tax years
18 2002-2004, but not 2005 as the Company
19 anticipated resolution prior to the rate filing.
20 The Section 263A deduction taken by the Company
21 on its 2005 tax return resulted in $11.253
22 million of deferred taxes that would be
23 applicable to gas operations.
24 Q. Do you propose to adjust rate base to reflect

1 these additional deferred taxes?
2 A. No. Since the resolution of this matter is
3 still pending and there is a potential for a
4 significant disallowance, we propose to reduce
5 deferred taxes by $12.8 million, from $65.7
6 million to $52.9 million. Our proposed deferred
7 taxes level is 60% of the forecasted Section
8 263A balance of claimed deductions for the years
9 2002 through 2006. We further propose that any
10 difference between the Section 263A deduction
11 reflected in rate base and the deferred taxes
12 related to the ultimate deduction allowed by the
13 Treasury Department be deferred subject to
14 interest at the allowed pre-tax rate of return.
15 Any difference between the Section 263A
16 deduction reflected in rate base and the
17 deferred taxes related to the ultimate deduction
18 allowed will consider any related offset to the
19 ADR/ACRS/MACRS rate base balances. Should a
20 resolution with the Treasury Department be
21 reached during the course of this proceeding,
22 the Company should notify the parties and,
23 depending upon the current status of the
24 proceeding, an update should be required of the

1 Company.

2 **Multi-Year Rate Plan**

3 Q. Company witness Rasmussen has sponsored a three-
4 year rate plan proposal. Do you agree with such
5 a proposal?

6 A. No. The Company's proposal does not include
7 sufficient data to evaluate the revenue
8 requirement of the Company in the proposed
9 second and third rate year. Further, the
10 proposal contains numerous reconciliations
11 which, as they are crafted, isolate the Company
12 from nearly all risk. In addition, the
13 Company's proposal contains the right to file
14 for new rates immediately after this rate case
15 concludes should the Company not be satisfied
16 with the result of the Commission decision.
17 Staff's review has been limited to the one year
18 rate case filing supported by the other Company
19 witnesses.

20 **Deferred Accounting**

21 Q. On pages 11 through 18 of his testimony, Company
22 witness Rasmussen seeks to employ the use of
23 deferred accounting to true-up a number of
24 items, even if a one year rate plan is adopted.

1 Do you support the Company's request for
2 reconciliation accounting for these items?
3 A. Staff's recommendations on deferred accounting
4 for pension and OPEB expenses, environmental
5 remediation, and WTC costs have already been
6 addressed in our testimony. Since Staff is
7 advocating a one-year rate plan, we do not
8 support the proposals to reconcile transmission
9 and distribution plant capital expenditures or
10 to reforecast sales in the context of a multi-
11 year rate plan. Staff would agree to
12 reconciliation of interference costs, pipeline
13 integrity costs related to facilities maintained
14 by KeySpan, and the New York facilities
15 agreement, assuming appropriate target levels
16 were set for the rate year.
17 Q. What deferred accounting proposals would you
18 object to?
19 A. We object to the reconciliation of property tax
20 expense and new legislation or regulatory
21 requirement impacts in a one-year rate case.
22 Q. Please explain your objection to reconciling
23 property tax expense.
24 A. The costs for property taxes can be reasonably

1 forecast for the rate year and it is very
2 unlikely that they will vary significantly from
3 their expected levels in the rate year. Given
4 the shortened forecast period and the
5 opportunity, in this proceeding, to submit
6 updates for known changes up to the Brief on
7 Exceptions, such a deferral treatment is
8 unnecessary.
9 Q. Please explain your objection to reconciling
10 expenses incurred due to new legislative and
11 regulatory requirements.
12 A. Should such expenses occur, the Company always
13 has the option to petition the Commission for
14 recovery of such costs.
15 **Disposition of Utility Plant**
16 Q. On page 84 of the Company's Accounting Panel
17 testimony, the use of the new after-tax gain
18 from the sale of Con Edison's First Avenue
19 properties is discussed. Do you agree with this
20 proposal?
21 A. Con Edison is proposing to refund the Company's
22 estimate of the net gain from the sale of the
23 First Properties to customers over a three-year
24 period. While Staff does not object to this

1 proposal, it should be noted that the Commission
2 has not yet acted on the Company's proposed
3 accounting and ratemaking for the net proceeds
4 in that case, and therefore the exact level of
5 proceeds available to be returned to gas
6 customers has not yet been determined. Pending
7 the resolution of that proceeding, the refund
8 amount proposed by the Company for the rate year
9 can be used as a placeholder.
10 Q. Does this conclude your testimony?
11 A. Yes.