BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

In the Matter of

Iberdrola SA, New York State Electric & Gas Corporation,
Rochester Gas & Electric Corporation

Case 07-M-0906

January 2008

Prepared Testimony of:

GAS RATES PANEL

Michael Salony
Utility Supervisor (Rates)

Michael W. Wayand
Utility Engineer 3 (Policy)

Office of Electric, Gas and
Water

State of New York
Department of Public Service
Three Empire State Plaza
Albany, New York 12223-1350

Q. Please state your full name and business address.

A. Michael Salony, Three Empire State Plaza, Albany, New York 12223.

Q. By whom are you employed and in what capacity?

A. I am employed by the New York State Department of Public Service. I am an engineer and supervisor in the Gas Rates Section of the Office of Electric, Gas & Water.

Q. Would you please state your educational background and professional experience?

A. I received a Bachelor of Science degree in Electrical Engineering from Pratt Institute in 1974. I joined the Department of Public Service in May 1976. My responsibilities have included analysis of various rate and regulatory issues, including rate design, gas sales and revenue forecasts, operating and maintenance expenses, depreciation and rate base, and I have testified on these topics in several proceedings before the Commission.

Q. Please state your full name and business address.

A. Michael W. Wayand, Three Empire State Plaza, Albany, NY 12223.

Q. Mr. Wayand, by whom are you employed and in what capacity?

A. I am employed by the Department of Public Service of the State of New York. I am a Utility Engineer 3 on the staff of the Office of Electric, Gas & Water, Policy Section.

Q. Please state your educational background and professional experience.

A. I received a Bachelor of Science degree in Mechanical Engineering from Union College in Schenectady, New York in 1977. I have been employed continuously since that time in the Department of Public Service as an engineer in the Office of Electric, Gas & Water. My duties in the Policy Section relate to gas utility matters, including the review of rate filings. I have previously testified before the Commission.

Q. What is the purpose of your testimony in this proceeding?

A. Although we do not find the proposal as filed to be in the public interest and therefore do not recommend its approval, we here offer some recommendations that should be instituted if the Commission were to allow the Iberdrola merger to proceed. More specifically, we recommend certain gas measures that are needed to protect ratepayers, and could provide gas customer benefits, should Iberdrola acquire Energy East and its affiliated local distribution companies (LDCs) NYSEG and RG&E. Specifically, the Commission should adopt capital expenditure (CAPEX) accountability measures, and eliminate the current Energy East LDCs Gas Cost Incentive Mechanisms (GCIM-2), which we believe are no longer necessary and therefore should be discontinued. Also, regardless of the resolution of merger issues, we recommend that NYSEG implement a gas revenue decoupling mechanism (RDM) in compliance with Commission Order issued August 29, 2007 and Notice Consolidating Proceedings, issued October 22, 2007 in Case 07-M-0996. A similar RDM should also be implemented for RG&E as a condition to any merger.

<u>GAS CAPEX ACCOUNTABLITY PROPOSAL</u>

Q. Why are you making a proposal to hold NYSEG and RG&E accountable for capital expenditures?

A. We believe it necessary to ensure there are no reductions in gas infrastructure work that may compromise system reliability, if the acquisition of Energy East by Iberdrola is allowed.

Q. What type of work is included in each company's capital programs?

A. Work includes the installation of new transmission and distribution gas mains, gas services, meters and improvements to gate stations that are necessary to maintain system integrity, safety and support customer growth.

Q. What has been the gas capital budget and actual expenditure history for NYSEG?

A. NYSEG's gas capital budgets on average approximated $15.5 million per year for the calendar years 2004 through 2006. Annual actual capital expenditures on average approximated $16.8 million.

Q. What has been the gas capital budget and expenditure experience history for RG&E?

A. RG&E's gas capital budgets on average approximated $24.4 million per year for the calendar years 2004 through 2006. Annual actual capital expenditures on average approximated $17.6 million, or 28 percent below budget.

Q. What are the companies' gas capital program expectations for the next three years?

A. According to NYSEG's most recent financing case (07-M-0891) average annual gas capital requirements for 2008 through 2010 are forecast at $20.8 million, or $62.8 million in total for the three year period. According to RG&E's finance case filing (07-M-1194) average annual gas capital requirements for 2008 through 2010 are approximately $19.3 million, or $57.9 million for the three year period.

Q. Are the companies' forecasts for 2008 through 2010 reasonable with respect to their historic experience?

A. Yes. The forecasts appear to recognize inflationary impacts and historic actual budget variance experience and therefore should accommodate system needs. That said, it should be noted that staff has not completed a full review of either the company's recent capital spending or going foreword budgeting process as part of this instant proceeding.

Q. Please explain your proposal to hold NYSEG and RG&E accountable for future capital expenditures?

A. We propose that if the actual annual amount expended is less than the annual average amount budgeted for the three years (2008-2010), that the companies defer the carrying costs on the budgeted shortfalls for the future benefit of customers. The revenue requirement impact will be calculated by applying the respective company pre-tax annual carrying charge of 9.1% for NYSEG and 10.1% for RG&E to the actual annual variance from the forecasted annual average budget amount. In addition, the companies should be required to provide staff with their approved annual gas budgets detailed by project for each of the next three years within one month of the date of the decision in this proceeding, and to file associated end year actual expenditures explaining any variances within two months of the end of each year.

GAS COST INCENTIVE MECHANISM

Q. Please describe the Energy East LDCs current Gas Cost Incentive Mechanisms (GCIM-2)?

A. The mechanisms provide for a sharing between customers and shareholders of gas cost savings attained through the joint optimization of the gas supply portfolios of the Energy East LDCs. The optimization activities include gas storage, transportation, and joint optimization of demand and variable savings associated with turnback of pipeline capacity.

Q. Why is the GCIM-2 no longer necessary?

A. They unnecessarily over-compensate the companies for taking measures facilitating the procurement and management of gas supply on a least cost basis. All New York State utilities are already required to procure gas on a least cost basis by law, §§PSL 66(e) and 66(f), and Commission regulations, 16 NYCRR - Part 61.3.6 (gas purchasing policies and load management practices), or be at risk for denial of recovery of imprudent costs. Therefore, no further incentives like the GCIM-2 are necessary for the companies to perform their duties, and elimination of this redundant incentive would provide a benefit to ratepayers.

GAS REVENUE DECOUPLING MECHANISM (RDM)

Q. Please comment on the Commission's August 29, 2007 Order Instituting Proceeding in Case 07-M-0996 on the development and implementation of a RDM for NYSEG?

A. The Commission has examined potential disincentives to utilities to engage in energy efficiency programs and is now requiring utilities to develop and implement mechanisms that true-up forecast and actual delivery service revenues. An October 22, 2007 Notice Consolidating Proceedings remands the development of a RDM for both electric and gas for NYSEG to this merger proceeding.

Q. What are your recommendations regarding a gas RDM?

A. NYSEG, and RG&E as well, should each implement a gas RDM as a precondition of approval of any merger, to facilitate the development of energy efficiency efforts and achieve the resulting customer savings in the NYSEG and RG&E service territories.

Q. How would the Panel structure a gas RDM?

A. We recommend the development of a RDM structured on an average pure base delivery revenue per customer (RPC) basis premised on rate case quality sales forecasts. We contemplate the establishment of annual RPC factors for residential and commercial customer classes excluding cooking and large industrial customer groups who typically are not the focus of customer energy efficiency programs. RPC factors would be derived by dividing the rate case quality sales forecast pure base revenues for each customer group by the average number of customers forecast for that customer group for a defined time period. Each company's allowed pure base revenue for each customer group will equal the RPC factor for the group times the actual average number of customers in the defined period. An accurate accounting of customers within each service class or group is a critical element of the RDM and will require a reliable and transparent data source (e.g., the number of open active gas meters may be a reliable proxy).

Q. How do you define pure base revenues?

A. Pure base revenues are revenues from tariff delivery rates and charges, excluding gross receipts taxes, merchant function charges

(MFCs), billing and payment processing charges, and all other applicable credits or surcharges other than the weather normalization adjustment (WNA) credits or surcharges. The inclusion of the WNA is necessary to offset the impact of weather related sales revenue captured in the RDM.

Q. How would you reconcile allowed and actual pure base revenues?

A. At the end of each period, for each group, actual pure base revenue will be reconciled to allowed pure base revenue. If actual revenues are greater than the allowed revenues, the difference should be refunded to customers. If actual revenues are less than allowed revenues, the shortfall should be surcharged to customers. The excess or shortfall should be refunded or surcharged to each customer group on a volumetric basis over the next 12 month period. Finally, procedures should be put in place to ensure that the RDMs are developed and in place by January 2009.

Q. Does this conclude your panel testimony at this time?

A. Yes.