

STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

RECOMMENDED DECISION BY  
ADMINISTRATIVE LAW JUDGE JEFFREY E. STOCKHOLM

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.

NOTICE OF SCHEDULE FOR FILING EXCEPTIONS

(Issued March 24, 2003)

Attached is the Recommended Decision of Administrative  
Law Judge Jeffrey E. Stockholm in this proceeding, together with  
a copy of the Commission's rules governing the procedures to be  
followed. Briefs on exceptions will be due in hand to the  
undersigned and all active parties on April 11, 2003 and briefs  
opposing exceptions will be due in hand to the undersigned and  
may be mailed to all active parties on April 25, 2003.

JANET HAND DEIXLER  
Secretary

STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

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APPEARANCES: See Appendix A

JEFFREY E. STOCKHOLM, Administrative Law Judge:

I. INTRODUCTION

A. Procedural Background

On March 21, 2000, the Commission instituted a proceeding to determine, among other issues, the future role regulated utilities should play in providing electricity and natural gas in competitive markets.<sup>1</sup> The proceeding was intended to refine the Commission's concept of mature competitive retail energy markets and to identify and remove obstacles to its achievement.<sup>2</sup> More particularly, the Commission ordered that the proceeding address the future of the competitive natural gas and electricity markets and the role of the regulated utilities in such markets; the identification of obstacles to the development of such markets and recommendations to eliminate them; and various issues regarding provider of last resort (POLR) responsibilities.<sup>3</sup>

During the pendency of the Competitive Markets Proceeding, the Commission concluded that " . . . one prerequisite to fostering market development is the conduct of cost studies, the ensuing assignment of costs to the utilities

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<sup>1</sup> 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, Order Instituting Proceeding (issued March 21, 2000), p. 1 (hereafter the Competitive Markets Proceeding).

<sup>2</sup> Id., p. 2.

<sup>3</sup> Id., p. 6.

various functions and services, and the establishment of fully unbundled, cost-based rates for electricity and gas service."<sup>4</sup> The Commission accordingly instituted this "Unbundling Track" to study and allocate utility costs between competitive and non-competitive functions and to establish cost-based rates that would afford customers accurate price signals as they choose among the providers of services in a competitive market. Recognizing that the required detailed cost studies would entail substantial efforts, the Commission determined that unbundling efforts should commence immediately, notwithstanding the continuing efforts in the Competitive Markets Proceeding.<sup>5</sup> Accordingly, the Commission directed the electric and gas utilities to perform embedded cost of service (ECOS) studies.

In its Order Directing Filing of Embedded Cost Studies,<sup>6</sup> the Commission resolved a number of issues regarding the nature of the cost studies to be performed e.g., ECOS studies rather than marginal cost studies) and directed that those studies be filed by March 15, 2002.<sup>7</sup> In addition, the Commission stated: "Gas and electric retail markets are now open, and we believe it important to establish competitive service unbundled rates, calculated with some degree of statewide uniformity, as soon as possible to replace the variously calculated backout

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<sup>4</sup> 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, Order Directing Expedited Consideration of Rate Unbundling (issued March 20, 2001), p. 1.

<sup>5</sup> A recommended decision was issued in the Competitive Markets Proceeding on July 13, 2001.

<sup>6</sup> Case 00-M-0504, Order Directing Filing of Embedded Cost Studies (issued November 9, 2001)(hereafter November Order).

<sup>7</sup> Id., p. 12. Also, Order on Rehearing Petitions and Motions (issued January 24, 2002).

credits now in use."<sup>8</sup> The November Order also addressed the potential for utility revenue losses as a result of retail migration and stated that the utilities should be accorded "a fair opportunity to recover prudently incurred revenue requirements, subject to the utilities' obligation to productively manage and reasonably mitigate their costs."<sup>9</sup>

On March 21, 2002, the Commission issued an additional order addressing two principal questions: the utilities' recovery of revenues lost due to migration; and the extent to which statewide consistency in establishing rates for competitive utility services could or should be accomplished.<sup>10</sup> This order required the utilities to include within their draft tariffs implementing their ECOS studies a mechanism to allow the recovery of revenue shortfalls, net of avoided costs. The Commission ordered that the mechanism recover the prudent level of any shortfalls, in part from all customers, and in part from utility full service customers.<sup>11</sup> The March Order also directed that the calculation of customer migration and associated revenue losses consider "actual net migration levels," as well as the utilities' realized revenues compared to the revenue forecasts utilized or assumed in establishing current rates.<sup>12</sup> The purpose of this

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<sup>8</sup> November Order, p. 14. Backout credits, or the amount migrating customers no longer pay the utility, are intended to approximate the utilities' costs of providing a competitive service. Generally, the utilities, Staff, and the energy services companies (ESCOs) have agreed upon backout credit levels without litigation and without the aid of detailed cost studies. In the absence of such studies, however, it is not possible to determine whether the backout credits are too high (thereby subsidizing the ESCOs), too low (thereby constraining economic market development), or approximately correct (reasonably reflecting the utility's cost of providing a competitive product or service).

<sup>9</sup> November Order, p. 5.

<sup>10</sup> Case 00-M-0504, Order Establishing Parameters for Lost Revenue Recovery and Incremental Cost Studies (issued March 21, 2002)(hereafter March Order).

<sup>11</sup> Id., p. 24.

<sup>12</sup> Id., p. 24, n. 24.

requirement is to "ensure that the utility neither overrecovers nor underrecovers revenues lost to migration . . . ." <sup>13</sup>

Concerning the issue of statewide consistency, the Commission stated as follows:

. . . , the [ECOS] studies must not be so uniformly constrained that they cannot reflect the real and material differences among the utilities; but neither can they be so disparate that the elements or components of competitive service rates are significantly different from utility to utility. Accordingly, we direct the administrative law judge to address in this generic proceeding [the unbundling phase] any challenges to the studies' methods or any other disputes concerning the studies or the tariffs that raise issues or policy questions of statewide concern. The judge is authorized to determine which of the issues raised by the parties should be determined in this proceeding and which should be reviewed in a separate proceeding where the rates would be implemented. <sup>14</sup>

The above orders also reflect the Commission's intent to implement unbundled rates under a two-part process. The first part (addressed in this recommended decision) is a review of the utilities' ECOS studies and other issues of statewide concern; and the second, to be undertaken in the context of individual utility proceedings, concerns the specific design and implementation of the unbundled rates, calculated in accordance with the Commission's decisions in this phase.

Following two Commission orders addressing scheduling issues <sup>15</sup> and an order on rehearing <sup>16</sup>, evidentiary hearings were held to examine Con Edison and NYSEG filings; they commenced

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<sup>13</sup> Id.

<sup>14</sup> Id., p. 28.

<sup>15</sup> Case 00-M-0504, Order Regarding Schedule (issued April 10, 2002), Confirming Order (issued April 17, 2002); Order Regarding Schedule (issued June 10, 2002), Confirming Order (issued June 19, 2002).

<sup>16</sup> Case 00-M-0504, Order on Rehearing and Clarification Petitions (issued May 30, 2002).

November 6 and November 12, 2002 respectively.<sup>17</sup> Four days of hearings were held (November 6-7 and 12-13), generating 1193 pages of transcript and 50 exhibits. Initial briefs regarding the Con Edison and NYSEG studies were filed on December 6, 2002 by the New York Energy Service Providers Association (NESPA), the National Energy Marketers Association (NEM), and the Small Customer Marketer Coalition (SCMC), jointly (ESCO I<sup>18</sup>); Amerada Hess Corporation (Hess), NEM, NESPA, and SCMC, jointly (ESCO II<sup>19</sup>); Central Hudson Gas and Electric Corporation (Central Hudson); Consolidated Edison Company of New York (Con Edison); the New York State Consumer Protection Board (CPB); Keyspan Energy Supply, LLC (Keyspan Supply); Keyspan Energy Delivery New York and Keyspan Energy Delivery Long Island, jointly (Keyspan Delivery); Multiple Intervenors (MI); NEM; Niagara Mohawk Power Corporation (Niagara Mohawk); Nucor Steel Auburn, Inc. (Nucor); New York State Electric & Gas Corporation (NYSEG); National Fuel Gas Distribution Corporation (NFGDC); and Staff of the Department of Public Service (Staff). On December 20, all of the above parties except MI filed reply briefs.

B. Purpose of the Proceeding

As the Commission has directed in a number of orders, the purpose of this phase of the proceeding is to examine the ECOS studies filed by the utilities for the purpose of identifying appropriate methods and policies to be applied in the performance of the cost studies, the calculation of prices for utility competitive services, and the recovery of competition-induced lost revenue. In addition, the extent to which these methods and policies should be applied on a consistent basis

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<sup>17</sup> Ruling on Schedule, Process, and Discovery (issued July 23, 2002).

<sup>18</sup> For the purpose of this brief, NESPA consists of Constellation NewEnergy, Energy America, LLC, GreenMountain Energy Company, and Strategic Energy, LLC.

<sup>19</sup> For the purposes of this brief, NESPA consists of AES NewEnergy, GreenMountain Energy Company, and Strategic Energy, LLC.

throughout the state will also be examined. Individual rates to be charged by the utilities for competitive or potentially competitive services will not directly result from the decisions made here. Rather, the issues decided here will require the utilities (in this phase, Con Edison and NYSEG) to rerun their studies and to file final tariffs with unbundled prices for competitive products and services, including a mechanism to recover lost revenues.

At its core, the effort here is to establish just and reasonable prices for utility services and products that are or may become competitive as previously determined by the Commission.<sup>20</sup> It is critically important to the development of the retail markets that these prices be set in a manner that is just and reasonable to all parties--consumers, utilities, and ESCOs.

The differing views of the parties, as discussed in more detail below, arise in part from the fact that the introduction of competition in a previously vertically integrated monopoly market will initially result in higher total costs due to the loss of the utilities' economies of scale (as the utilities' services are provided to fewer customers) and loss of economies of scope (as the utilities offer fewer products or services). In other words, as the utilities lose customers who begin purchasing electric or gas commodity, billing services, metering services, etc. from ESCOs, the utility's costs will have to be spread over fewer services and products or over fewer customers.<sup>21</sup> Another way to express the concept is to understand that total societal costs for any previously monopoly function

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<sup>20</sup> November Order.

<sup>21</sup> It is expected that the utilities' costs will marginally decrease in the short-run (by short-run avoided costs), but the utilities' estimates of those avoided costs have been very small. However, the Commission has determined that customers should be able to avoid paying for utility services and products based on utility embedded costs when they secure such services and products from an ESCO. The difference between these short-run avoided costs and the price of the service calculated here may result in the utilities not receiving all of the revenues allowed by the Commission in setting rates.

will increase as competitors duplicate the capabilities of the utilities, so long as the utilities' avoidable costs are less than the ESCOs' marginal costs. Therefore, the issue underlying the majority of the arguments here is who should bear the burden of the added costs in the market, or of the loss of utility economies.

The utilities are concerned that setting the price for competitive services at any level above their short-run avoided costs will result in a reduction in utility revenues (as customers move to other providers) without an equal reduction in costs, leading to reduced earnings. It is therefore understandable that NYSEG and Con Edison calculate the lowest price for competitive services.<sup>22</sup> From the opposite perspective, the ESCOs are concerned that if the utility's price is not set well above the utility short-run avoided costs, retail competition will not be possible. Thus, it comes as no surprise that the ESCO price calculations and policy recommendations are many times higher than the utilities'. Staff's concerns include the Commission's market development policies (which benefit from a higher utility price) and the need to maintain just and reasonable utility rates (which goal benefits from a lower utility price).<sup>23</sup> Staff presents two different cost study methods (i.e., utility regulatory method [URM] and the general allocation method [GAM]), one (GAM) resulting in a higher price and the other (URM) in a lower one, but Staff does not recommend either approach as superior. Like the other parties, Staff

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<sup>22</sup> For example, for residential electric supply procurement, Con Edison calculates a price of 0.025 cents/kwh, and NYSEG calculates a price of 0.04 cents/kwh. Staff's estimates range from 0.11 cents/kwh (NYSEG) to 0.286 cents/kwh (Con Edison), and the ESCO calculations range from 0.27 cents/kwh (NYSEG) to 0.307 cents/kwh (Con Edison). (Staff Initial Brief, App. A, B.) The ESCOs further argue that, for policy reasons, these prices should be set at 0.55 cents/kwh (ESCO I Initial Brief, p. 18.) The ESCO policy-based prices are therefore 20 times as large as the Con Edison studies suggest.

<sup>23</sup> As the utility price for a competitive service is set at a higher level, migration increases the amount of lost revenues, and upward pressure on utility rates results.

concerns are evidenced in its presentation, but Staff's results generally fall between those of the utilities and the ESCOs. From the consumer's perspective and as recognized by the Commission, a competitive market cannot develop if the consumer is required to continue to pay the utility for retail services that the consumer buys from an ESCO and the utility no longer provides.<sup>24</sup>

As can be seen from the above, the utilities and ESCOs alike recommend what appears to be in their own financial best interest. Staff offers two options for Commission consideration that lie between the utility and the ESCO recommendations. As Staff notes, the higher the retail price, the greater the utility revenue erosion and, potentially, the larger the impacts on utility rates needed to recoup those losses. Setting higher utility rates for competitive services should also have a positive impact on migration and the development of retail markets.<sup>25</sup> On the other hand, lower backout credits should minimize upward pressure on utility rates, but may also limit the rate of growth of the retail markets. Therefore, we are faced in this proceeding with balancing potentially competing objectives, at least in the short-run, of promoting competition and setting least-cost utility rates.

In this recommended decision I first address the general methodological arguments raised by the parties and then turn to a discussion of issues concerning the functionalization and allocation of specific costs. Policy and other concerns regarding net loss revenue recovery are considered next, followed by discussion of the competitive and other ratemaking impacts of implementing the results of the studies.

## II. SETTING COMPETITIVE PRICES

The arguments raised by the parties generally fall in two categories: the proper conceptual approach to the cost studies; and the method that should be used to assign specific

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<sup>24</sup> March Order, p. 24.

<sup>25</sup> Setting prices at too high a level risks encouraging uneconomic entry and unsustainable markets.

activity costs. The conceptual arguments mostly invoke negative characterizations of one's opponents' studies (e.g., the utilities' approach is utility-centric and improperly based on avoided cost principles; the Staff and ESCO studies are result-oriented) or posit a general rationale to be applied to individual activity costs (e.g., Staff's URM and GAM justifications).

Historically, specific types of utility costs have been assigned using one of three different methods: direct assignment; special studies; and pro-rata assignments based on the assignment of other costs (e.g., labor) or revenues. The direct assignment of costs, where there is a clear cost-causation link, is the usual first approach in an ECOS study.<sup>26</sup> For example, the cost of poles and wires is obviously related to the delivery function, and, therefore, the costs of the poles and wires would be assigned to non-competitive services. If principles of cost causation do not clearly support the direct assignment of costs to a particular service, special studies can be performed to determine where it is most reasonable to assign the costs. For example, the nature of calls to a company's call center could be tracked and the costs of the call center could be allocated based on the percentages of received calls that concerned competitive and non-competitive services. Finally, in cases where neither direct assignments nor special studies are practicable, costs may be allocated to the various services pro-rata, based on the direct assignment of other costs or revenues. For example, some administrative and general (A&G) costs tend to vary with total labor costs and therefore might be reasonably assigned to the various services pro-rata based on the relative levels of labor costs directly assigned to each service.

Staff and other non-utility parties caution that some judgment must be exercised to avoid allowing the foregoing traditional method to lead to irrational results and that a

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<sup>26</sup> Staff's GAM approach implicitly challenges the reasonableness of first using the direct assignment of costs based on principles of cost-causation, at least for the purpose of deriving prices for competitive services.

hierarchy of methods cannot be blindly followed, especially considering that the unbundling effort is employing ECOS studies in a unique way.<sup>27</sup> In addition, Staff and the ESCOs question the reasonableness of the utility special studies. Staff contends that these extremely detailed studies are very difficult and costly to verify or reproduce, thereby giving the utility "a huge advantage" related to its greater knowledge of the studies compared to the knowledge possessed by any other party.<sup>28</sup> The ESCOs contend that the utilities use special studies only where it best suits their purposes, thereby suggesting that the utility studies were result-oriented.<sup>29</sup>

The utilities argue generally that the judgment exercised by the other parties violates principles of cost-causation, resulting in an over-allocation of costs to competitive services. Regarding special studies, the utilities argue that their analyses more accurately assign costs to those activities that cause them, as required by the Commission.<sup>30</sup> Ignoring principles of cost-causation will, according to the utilities, provide uneconomic subsidies to ESCOs and result in unjustified and unnecessary increases in utility rates.

Set forth below are the conceptual arguments raised by each of the parties, followed by specific cost allocation issues.

A. Conceptual Issues

1. Parties' Positions

a. Staff

Staff begins by quoting Bob Dylan - "the times they are a-changin'."<sup>31</sup> Its point is two-fold. First, ECOS studies, historically used to determine and adjust inter-class returns and rate designs for bundled utility service, are now being used for the first time to establish unbundled rates for competitive

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<sup>27</sup> November Order, p. 11.

<sup>28</sup> Staff Initial Brief, p. 24.

<sup>29</sup> ESCO I Initial Brief, p. 8.

<sup>30</sup> March Order, p. 24.

<sup>31</sup> Staff Initial Brief, p. 5.

services. Staff's second point is that the utilities have conducted their studies with a "utility-centric" focus, based on their historical way of doing business, and have thereby missed the point of the cost study exercise. Staff contends that the utilities' approach necessarily assumes that utilities are not competitors and are not suppliers of competitive services. It is from this perspective, Staff contends, that the utilities use avoided cost principles to functionalize and assign costs, an approach previously rejected by the Commission. Staff also challenges the use of special studies, arguing that verifying them is burdensome and that "regulators and customers should not bear the burden that their lack of knowledge causes."<sup>32</sup>

For its part, Staff offers the URM and the GAM. The URM is described a method that treats delivery service as a base service and competitive offerings as incremental. The GAM is described as a method that treats each utility service (competitive and non-competitive) as benefiting equally from the utility's expenditures, resulting in a greater degree of revenue-based cost assignments than is reflected in the URM process, which makes more direct cost assignments. While there are a number of differences between these approaches in the assignment of various activity costs, the GAM's results for Con Edison differ most significantly from those of the URM in the assignment of information resources (IR) and call center costs, where GAM assigns approximately \$25 million more to the competitive services than does the URM.<sup>33</sup> For NYSEG, the majority of the difference between the URM and the GAM is in the allocation of A&G expense, where the GAM doubles the assignment to competitive functions.<sup>34</sup>

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<sup>32</sup> Staff Initial Brief, p. 24.

<sup>33</sup> Con Edison's study and the Staff URM assign approximately \$12 million to competitive services from these costs, while the GAM assigns approximately \$37 million (Exhibit 44, Schedule SP10-C).

<sup>34</sup> NYSEG's study and the Staff URM assign \$8.4 million of A&G costs to the competitive function, while the GAM assigns \$16.6 million (Exhibit 78, schedule SP-2R).

b. Con Edison

Con Edison generally defends its studies, arguing that it properly functionalized, assigned, and allocated its costs based on a method that appropriately considered principles of cost-causation. Where a direct causal link was not clear but was potentially indicated, Con Edison performed special studies. Where no causal connection could be identified, costs were allocated on a basis that related to the nature of the underlying costs. Staff (especially in its GAM approach), the CPB, and the ESCOs, according to Con Edison, did not assign costs based on the factors that cause them, but on the basis of the results that different means of assignment would produce, i.e., the non-utility parties were "result-oriented." Because they "continually compared the Company's" study results to its current competitive prices (i.e., backout credits) "as a means of discrediting the Company's studies," Con Edison concludes, the non-utility parties began their analyses with desired results, and then proposed methods that would get them there.<sup>35</sup>

Con Edison also challenges Staff's loss of economies of scope theory. Staff's rationale lacks merit, according to Con Edison, because "competitive services neither contributed to the economics of scope reflected in the Company's rates nor are they the cause of the Company's past or ongoing incurrence of those costs."<sup>36</sup> According to Con Edison, the only economies of scope arise from its position as a supplier of two services-- electricity and gas.<sup>37</sup>

c. NYSEG

Like Con Edison, NYSEG defends its studies as consistent with the Commission's orders and with the principles of cost causation. NYSEG argues that a four-tier hierarchy of

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<sup>35</sup> Con Edison Initial Brief, p. 6, n. 14.

<sup>36</sup> Con Edison Initial Brief, p. 5.

<sup>37</sup> In my opinion, Niagara Mohawk's more expansive view of "a myriad of products and services" being provided by the utility and contributing to economies of scope, is the better perspective.

cost allocation methods should be used (direct assignment, special studies, functional allocations (e.g., labor, rate base) and general allocations (revenues)); it alleges the first three steps were bypassed, in most cases, by Staff and the remaining parties.

According to NYSEG, use of the Staff URM or GAM "drastically overstates" the allocation of costs to competitive functions, resulting in high retail prices that subsidize the ESCOs.<sup>38</sup> Regarding the URM, NYSEG states that the only open issues are the functionalization of Credit and Collection and Customer Contact costs on the basis of revenues. The GAM assigns all retail-service-related costs to all functions on the basis of revenues, an approach, NYSEG contends, that could assign large amounts of unrelated and unintended dollars to a specific function, yielding a result-oriented ECOS study. The NYSEG studies avoided this problem, the company suggests, by examining its costs and applying reasonable and fair allocators based on the activity that caused the underlying costs.

d. Other Utilities

Niagara Mohawk submitted responsive testimony, and Central Hudson, Niagara Mohawk, Keyspan Delivery, and NFGDC filed initial and reply briefs.

Niagara Mohawk argues that the fundamental purpose of a cost of service study is to establish links between the utility's incurred costs and the factors that cause them to be incurred. It supports the hierarchy of cost assignment methods recommended by NYSEG and Con Edison and criticizes Staff for using functional allocators without first considering assignments based on cost causation principles, i.e., direct assignments or assignments via special studies.<sup>39</sup> Regarding Staff's concern that special studies are unfairly difficult to verify or challenge, Niagara

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<sup>38</sup> NYSEG Initial Brief, p. 12.

<sup>39</sup> Keyspan Delivery (Initial Brief, pp. 5-7) contends that the use of functional allocators by Staff and the ESCOs abandons principles of cost-causation and adopts revenue allocators that have no cost basis.

Mohawk states that ". . . if we throw all special studies out the window because they are difficult to review," the unbundling of rates will not be accomplished.<sup>40</sup> Niagara Mohawk also argues that Staff improperly designed its proposals by considering the level of unbundled utility prices as compared to ESCO cost structures (which costs are not contained in the record).<sup>41</sup> Niagara Mohawk also criticizes the ESCOs' study for limiting its review to the PSC account level and for not breaking down those costs for further analysis.

Finally, Niagara Mohawk, Central Hudson, and NFGDC all express concerns that the decisions here on the Con Edison and NYSEG studies will establish binding precedents: Niagara Mohawk expresses the concern that the results ". . . may have a binding or precedential effect in Niagara Mohawk's proceeding"; Central Hudson argues that the results here ". . . should not have a precedential consequence for Central Hudson or prejudice consideration of Central Hudson's ECOS studies"; and NFGDC states that "National Fuel's principle objective . . . is to insure that matters addressed . . . [here] . . . not be deemed to have 'generic' applicability that would bind Distribution before it is afforded its opportunity for hearings."<sup>42</sup> Niagara Mohawk argues, like Central Hudson and NFGDC, that its territory, costs, rates, and retail access programs differ in most respects from Con Edison's and NYSEG's, and, therefore, that none of the issues raised in these proceedings is "generic" in nature such that it could be binding on the other utilities.

Central Hudson argues that the Commission's objective of establishing competitive retail markets ". . . implies a bias

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<sup>40</sup> Niagara Mohawk Initial Brief, p. 8. NFGDC (Reply Brief, p. 6) also attacks the Staff position on special studies claiming that it ". . . bespeaks a frivolity that should not be countenanced."

<sup>41</sup> Niagara Mohawk Initial Brief, p. 18. Niagara Mohawk quotes the Commission's March Order and November Order for the proposition that the purpose of the case is to establish fully unbundled rates based on utility costs.

<sup>42</sup> Niagara Mohawk Initial Brief, p. 33; Central Hudson Initial Brief, p. 21; NFGDC Initial Brief, p. 1.

in favor of high utility prices . . . to create maximal incentive for customers to choose a third party supplier."<sup>43</sup> Concerned about this alleged bias, Central Hudson argues that pricing competitive services too high (and, accordingly, non-competitive services too low) will create uneconomic synergy, uneconomic migration incentives, uneconomic market entry, uneconomic subsidies, wealth transfer from customers to ESCOs, and, potentially, unrecovered revenue requirements. Citing the State's experience with the six-cent law which set wholesale prices well above costs, Central Hudson urges that the Commission avoid the imposition of uneconomic subsidies intended to jump start specific competitive retail markets.<sup>44</sup>

Central Hudson also challenges the appropriateness of using Con Edison's ECOS study for setting competitive prices, arguing that the Commission has not based rates on historical costs since it adopted a projected rate year.<sup>45</sup> Further, Central Hudson contends that the existence of only one normalizing adjustment to Con Edison's study suggests that the study does not fulfill the Commission's directive that normalizing adjustments be made if required to reflect anticipated changes.<sup>46</sup> The unreliability of Con Edison's study is further demonstrated,

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<sup>43</sup> Central Hudson Initial Brief, p. 3. In my view, there is no implied bias in the Unbundling Track of this proceeding. The purpose here is to determine just and reasonable utility prices for competitive services that are neither too high (promoting uneconomic competition) nor too low (subsidizing competitive prices with monopoly revenues and preventing the development of retail competition).

<sup>44</sup> Central Hudson Initial Brief, p. 15. Central Hudson argues that the only appropriate method to set competitive prices is based on marginal costs, a position contradicted by the Commission's previous decisions in this proceeding (Order on Rehearing Petitions and Motions (issued January 24, 2002), p. 6; March Order, pp. 15-17).

<sup>45</sup> Central Hudson Initial Brief, pp. 6-10, citing the Commission's Statement of Policy on Test Periods in Major Rate Proceedings (issued November 23, 1977).

<sup>46</sup> Because all of the studies (Staff, CPB, ESCO, and Nucor) are largely based on Con Edison's costs, Central Hudson argues that none of the studies meet the Commission's requirements (Central Hudson Initial Brief, p. 10).

according to Central Hudson, by the fact that Con Edison's existing rates are not based on calendar year 2000 costs (the ECOS studies are) and by the fact that ". . . no Staff investigations into the prudence of Con Edison's actual expenditures have been reported . . . ".<sup>47</sup>

Central Hudson also challenges Staff's GAM method.<sup>48</sup> While Staff claimed the method allocated economies of scale, Central Hudson maintains it merely functionalized retailing costs by revenues, without any showing that economies of scale are related in any way to revenues. Central Hudson argues that Staff offered no objective basis for the GAM, and that the suggestions in Staff's testimony that the GAM may more accurately reflect the stand-alone costs of a utility competitor or that the retail prices that result from the GAM may be necessary for the ESCOs to compete were shown to lack any factual basis.

After reviewing the various orders in this proceeding, Keyspan Delivery concludes that the Con Edison and NYSEG studies have met the Commission's requirements for calculating embedded cost-based unbundled rates. Consistent with the positions taken by Central Hudson and Niagara Mohawk, Keyspan Delivery objects to the Staff approach (especially the GAM) and the ESCO study on the grounds that they depart from concepts of cost-causation without any supporting rationale. The company also notes that the Commission has been sensitive to the required balance between setting prices high enough to sustain a competitive market, but not so high as to encourage inefficient competitors.<sup>49</sup> It argues that setting utility competitive prices higher will result in higher utility lost revenues (thereby sending utility rates even higher), and, in all likelihood, higher ESCO prices as well.

NFGDC states that its ". . . principal objective in participating . . . is to insure that matters addressed . . . [here] . . . not be deemed to have 'generic' applicability that

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<sup>47</sup> Id.

<sup>48</sup> Id., pp. 11-14. While CH also opposes the URM, most of its arguments focus on Staff's GAM.

<sup>49</sup> Keyspan Delivery Initial Brief, p. 15.

would bind Distribution before it is afforded its opportunity for hearings." <sup>50</sup>

e. ESCOs

Mr. Richard Hornby submitted testimony on behalf of Amerada Hess Corporation (Hess), NESPA, NEM, and SCMC. The ESCO I initial and reply briefs were filed on behalf of NESPA, NEM, and SCMC, while the ESCO II briefs were submitted on behalf of Hess, NEM, NESPA, and SCMC. In addition, NEM filed separate initial and reply briefs, as did Keyspan Supply.

As a general matter, the ESCOs challenge the adequacy of the Con Edison and NYSEG filings, urging that they be rejected. ESCO I argues that the utilities want to offer inexpensive competitive products and to subsidize that offering with inflated prices for monopoly services.<sup>51</sup> Unverifiable special studies and improper avoided cost methods, according to ESCO I, have been used by the utilities to inflate the costs of monopoly services and minimize the costs of competitive services. In addition, ESCO I contends that the utilities have violated cost-causation principles in a number of areas. It concludes that the utilities have not presented a prima facie case.

ESCO II argues that the utilities have ignored the new competitive environment by "severely" understating the level of uncollectibles, customer care, and A&G costs to be assigned to competitive service offerings.<sup>52</sup> Applying traditional ECOS principles is appropriate regarding the direct allocation of costs, according to ESCO II, but, in light of the new competitive environment, the use of traditional approaches for the allocation of certain indirect and overhead costs may not be reasonable.<sup>53</sup>

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<sup>50</sup> NFGDC Initial Brief, p. 1.

<sup>51</sup> ESCO I Initial Brief, p. 2.

<sup>52</sup> ESCO II Initial Brief, p. 4.

<sup>53</sup> ESCO II cites the November Order (p. 11), where the Commission stated: "Finally, the functionalized unbundling of competitive services envisioned here has not been attempted previously, and, therefore, past methodologies may not provide much useful guidance for the current effort."

Regarding the Con Edison study, ESCO II argues that the utility focused on functionalizing the vast majority of clearing account and A&G costs as being related to the utility's regulated service, thereby rendering the presentation unreasonable on its face. The study produces irrational results, argues ESCO II, as shown by its allocation to regulated services of 95% of uncollectible costs, 79% of customer care costs, and 97% of A&G costs even though regulated services are allocated only 39% of the company's direct costs.<sup>54</sup>

Keyspan Supply argues that Con Edison's study allocates a "higher-than-appropriate" share of costs to its monopoly service by focusing on the costs Con Edison would avoid if it no longer offered competitive services.<sup>55</sup> This is not the type of study the Commission required, according to Keyspan Supply, and the competitive prices that result are not cost-based and would stifle the development of competition. Keyspan Supply generally supports the ESCO and Staff studies (especially Staff's GAM methodology), finding them more representative of Con Edison's costs of providing competitive services.

NEM urges that Con Edison's study be rejected for failing to comply with the Commission's order, or, at a minimum, that the ESCO adjustments to Con Edison's study be adopted.<sup>56</sup> According to NEM, Con Edison filed an avoided cost study rather than the required embedded cost study, resulting in an "enormously disproportionate share" of costs being assigned to the monopoly service. NEM contends that the assignment in Con Edison's study of only 2% of the company's revenue requirement to contestable services while 39% of its revenues are generated by those services supports the conclusion that Con Edison's approach is unreasonable.

NEM also challenges Staff's URM method. It suggests that a "fundamental economic imperative" to the design of

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<sup>54</sup> ESCO II Initial Brief, p. 10. ESCO II Initial Brief, p. 29 also characterizes the Staff and CPB presentations as consistent with the presentations of the ESCO witness.

<sup>55</sup> Keyspan Supply Initial Brief, p. 3.

<sup>56</sup> NEM Initial Brief, p. 1.

unbundled prices is a determination of whether ESCOs would find it difficult to compete against the utility's retail price.<sup>57</sup> According to NEM, the URM adopts the utilities' avoided cost approach, and even Staff's GAM yields artificially low rates. It would accept the Staff GAM as modified by witness Hornby until a proper study can be completed.<sup>58</sup>

As a final matter, ESCO I and II offer another conceptual approach for the Commission to consider--establishing a uniform state-wide price for utility retail electric commodity sales of 5.5 mills/kWh for residential service and 5.0 mills/kWh for large commercial and industrial service. Current rates (2 mills/4 mills for Con Edison), according to these ESCOs, have not led to robust retail competition and have not created appropriate incentives for the utilities to control their costs. Nor are the studies as adjusted by Staff, CPB, Nucor, or, one assumes, by the ESCOs themselves adequate to produce reasonable results. Accordingly, the ESCOs begin with the results of Staff's GAM method, which assigned \$105 million of retailing costs (out of \$201 million) to competitive services. The ESCOs then allocate the balance of retail costs also to competitive services. A 100% allocation of retailing costs to the competitive function results in Con Edison electric retail supply rates per kWh of 5.68 mills (residential) and 5.08 mills (commercial & industrial) and NYSEG supply rates of 4.6 mills (residential) and 3.4 mills (commercial & industrial).<sup>59</sup> Based on the Commission's desire for some level of statewide consistency, the ESCOs recommend a single statewide rate for retail electric supply of 5.0/5.5 mills. According to the ESCOs, "[t]he positive impact of a single state-wide number more than outweighs any 'imprecision' that may result."<sup>60</sup> The inadequate

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<sup>57</sup> Id., pp. 14-15.

<sup>58</sup> For Con Edison electric supply, Staff's GAM results are roughly 7% lower than witness Hornby's, whereas for gas supply, Staff's GAM results are roughly 8% higher than witness Hornby's (Staff Initial Brief, Appendix A).

<sup>59</sup> ESCO I Initial Brief, p. 17, Appendix A, B, C.

<sup>60</sup> Id., p. 18.

cost studies, the need to enhance the development of retail markets, and the requirement to develop rates that reflect a realistic appraisal of all of the issues and concerns all lead to the conclusion, say the ESCOs, that these uniform statewide rates should be adopted.<sup>61</sup>

f. Customer Representatives

CPB and Nucor filed testimony and initial and reply briefs, and MI filed an initial brief. Each of these parties generally opposes the utilities' studies and warns that adopting such studies will adversely affect the development of competitive markets.

CPB recommends that the Con Edison and NYSEG studies be rejected for assigning excessive levels of costs to the monopoly function and thereby setting competitive prices "far below" actual costs.<sup>62</sup> The results recommended by CPB coincide with the Staff URM, and it recommends, in addition, that the Commission consider the Staff GAM and the ESCO approaches, while also considering potential impacts on utility rates.<sup>63</sup>

Nucor focuses on NYSEG's presentation, noting at the outset that, unlike Con Edison, NYSEG has the potential to generate significant profits (or losses) on the sale of commodity.<sup>64</sup> Accordingly, NYSEG has a vested interest, Nucor maintains, in maximizing its own commodity sales and minimizing ESCO sales, which interests would be served by a low competitive price. Nucor argues that NYSEG has done precisely that by assigning costs to its delivery function that should be assigned to competitive services. Based on its analysis showing that 20% of NYSEG's overall profits could result from its sale of

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<sup>61</sup> ESCO II, p. 30.

<sup>62</sup> CPB Initial Brief, p. 3.

<sup>63</sup> Id.

<sup>64</sup> Nucor Initial Brief, p. 1.

commodity,<sup>65</sup> Nucor argues that 20% of NYSEG's A&G expenses should be assigned to its competitive services.

MI also focuses on the NYSEG proposals, arguing that unbundling is useful only if benefits result to consumers and to the further development of competitive markets. MI expresses three concerns: unbundling should not result in increased rates; unbundling should not be used to shift costs from competitive services to non-competitive services; and unbundling should not be used by the utilities as an opportunity to recover "ridiculous amounts of purportedly stranded costs."<sup>66</sup> Regarding cost allocations, MI argues that the utilities are attempting to assign "all possible costs" to non-competitive services, using what appear to be avoided cost principles in the embedded cost studies.<sup>67</sup> MI also notes that under NYSEG's recently approved rate plan the utility "is expected to earn substantial profits" from competitive commodity sales, and it speculates that this profit opportunity has already resulted in increased costs attributable to competitive functions and should be expected to do so in the future as well. It suggests that these increased competitive costs have not been reflected in NYSEG's study. This makes it even more important, according to MI, that adequate costs be allocated to the supply function.

## 2. Discussion

Most of the conceptual arguments raised by the parties can be answered by reference to earlier Commission decisions in this proceeding. On more than one occasion, the Commission has

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<sup>65</sup> Unlike Con Edison's pass-through of commodity costs, NYSEG's bundled-rate option (BRO) is priced to offer the utility a profit opportunity. Roughly 90% of NYSEG's customers are taking service under the BRO rate at the beginning of 2003.

<sup>66</sup> MI Initial Brief, p. 4. Regarding rate increases, the Commission has held that unbundled rates should be implemented in a revenue neutral manner (November Order, p. 4). The Commission has also noted that the costs at issue are not uneconomic capital costs (*i.e.*, stranded costs), but revenue requirement expenses that may not be covered by revenues due to customer migration (March Order, p. 23).

<sup>67</sup> MI Initial Brief, pp. 8, 9, n. 10.

declared its intention to create separately stated prices for competitive services based on the utilities' embedded costs. While the Commission recognizes that principles of cost-causation can be important,<sup>68</sup> it has also noted that using ECOS studies to derive competitive rates is a unique undertaking, and approaches used in the past may be of little guidance now.<sup>69</sup> From the customer's perspective, the Commission noted that the attractiveness of retail options will be diminished, and the development of the retail market impeded, unless the customer can avoid paying the utility for services it no longer purchases.<sup>70</sup> Therefore, the task here is to establish prices for utility competitive services that are just and reasonable to all parties: to consumers, both those who may desire to purchase competitive services from ESCOs and those who remain with the utility; for utilities, who are entitled to a reasonable opportunity to recover their prudently managed costs; and for the ESCOs, should be allowed to compete against utility costs that are not subsidized by monopoly revenues.

a. Utility Studies

On the basis of the record and the parties' briefs, I conclude that the Con Edison and NYSEG studies generally comply with the Commission's directives and can provide an adequate starting point for establishing unbundled competitive rates. The vast majority of Con Edison's and NYSEG's revenue requirements have been assigned to competitive and non-competitive functions on a cost-causation basis without challenge. While significant disagreements exist over the appropriate assignment of specific retailing and overhead costs (discussed in the next section), the bulk of each company's costs have been appropriately unbundled. The arguments of the non-utility parties that the studies violate the Commission's directives are grounded in disagreements over the appropriate allocation of a relatively small amount of

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<sup>68</sup> March Order, p. 24..

<sup>69</sup> November Order, p. 11.

<sup>70</sup> March Order, p. 24.

overhead and retailing costs, not on challenges to the majority of the dollars allocated by the studies. In effect, these parties are arguing that the results of the studies are inappropriate because a few of the costs have not been properly assigned.

Some of the non-utility parties have also urged that the Con Edison and NYSEG studies be rejected based on comparisons of the study results with overall revenue requirements, with the existing, negotiated backout credits, or with (unknown) ESCO cost structures or stand-alone costs. In my view, none of these arguments justifies a rejection of the entirety of the utility studies.

If all the utilities' costs are reasonably and fairly assigned to competitive and non-competitive services, the results will be just and reasonable rates, whether the assignments exceed or fall short of existing backout credits and regardless of their relationship to other appropriately assigned utility revenue requirements. Further, the purpose of the unbundling track is to unbundle utility costs and set utility rates based on those costs,<sup>71</sup> not to set rates based on a comparison with ESCO costs, which, in any event, are not part of this record.<sup>72</sup>

Central Hudson raises two unique arguments as the only utility party urging rejection of the Con Edison and NYSEG cost studies. It first contends that prospective utility prices

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<sup>71</sup> Some have argued that the purpose of this proceeding is to foster the development of competitive markets, and clearly that is one of the purposes of the Competitive Markets Proceeding. However, the Unbundling Track addressed herein was created only to expeditiously consider rate unbundling as one of the prerequisites to fostering market development (Order Directing Expedited Consideration of Rate Unbundling, supra). Techniques to increase the rate of customer migration or to otherwise foster market development were addressed in the recommended decision in the main proceeding.

<sup>72</sup> NEM is mistaken in arguing that a fundamental economic imperative is the determination of whether ESCOs could compete against the prices being set here. For one thing, the record here is inadequate on this issue. More fundamentally, competition in the marketplace will determine if ESCOs can compete, and the musings of regulatory authorities on this question are irrelevant.

should not be based on historical costs in light of the Commission's long-standing policy of setting rates on the basis of prospective costs. As a general matter I agree, and, in the future, unbundled rates for competitive services should be set in the context of a formal rate proceeding (including formal cost of service studies), where existing and future migration rates and utility cost mitigation efforts can be examined for their impact on revenues and revenue requirements. At this time, however, no utility rate plan incorporates these considerations and it may be years before formal rate proceedings are available for every utility to implement this preferred approach. By creating a proceeding to expeditiously establish competitive rates, the Commission has implied that awaiting formal rate proceedings is not in the public interest. In addition, the Commission has stated on a number of occasions that competitive rates should be set as soon as reasonably possible on the basis of embedded costs. Further, this is not a major rate proceeding to which the 1977 Policy Statement would apply, as the Commission's intent is to implement rates here in a revenue neutral manner; and even if the general policy did apply on its face, it should not be deemed to control the Commission's explicit directions to the contrary in this proceeding.

Central Hudson's second argument is that Con Edison's 2000 costs are unreliable--first, because Con Edison made only one normalizing adjustment to account for known or anticipated changes, and, second, because Staff did not undertake a prudence review of Con Edison's 2000 costs.<sup>73</sup> While the theory of this argument may be sound, it fails from a lack of proof. There is no evidence in this record identifying any required normalizing adjustments to Con Edison's studies that were not made, and Central Hudson fails to identify any such required adjustments. Similarly, Central Hudson fails to identify any of Con Edison's costs that should be deemed even prima facie imprudent and subject to removal from its studies on that account. Therefore,

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<sup>73</sup> It is at least unusual that a utility is suggesting the need for a Staff prudence investigation.

Central Hudson's challenges to Con Edison's study are purely speculative and are not adopted.

b. Staff's URM and GAM

While the theories supporting Staff's URM and GAM methods are attractive, I do not find them overly useful in deciding upon the assignment of specific costs to competitive or non-competitive services. For example, Staff functionalizes uncollectibles by revenues under the URM because an unpaid bill contains both competitive and non-competitive revenues (a cost-causation argument); under the GAM, Staff performs the same functionalization, but justifies it as pro-rating the costs and economies of scope of shared retailing efforts.<sup>74</sup> It appears from both the general and specific Staff arguments that the URM is not much more than the assignment of costs based on principles of cost-causation. It is not clear how following cost-causation principles results in treating "utility delivery service as a base service with other services being treated as incremental."<sup>75</sup>

Staff's GAM, however, does appear to vary significantly from the straightforward application of cost-causation principles. The GAM allocates retailing costs to all services on a pro-rata revenue basis in an effort intended to establish retail prices that are not unduly influenced by the economies of scope possessed by the utilities' overall operations. In my view, this approach presents a number of conceptual problems. First, there is no evidence in the record of the magnitude of the utilities' economies of scope. By how much would the utilities' costs increase if those economies did not exist? Does allocating costs by revenues have any relationship to the magnitude of the utilities' economies? Because there is no answer to these questions, it is impossible to conclude that the GAM cost assignments add an amount to the competitive price that fairly offsets the utilities' economies of scope.

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<sup>74</sup> Staff Initial Brief, p. 19.

<sup>75</sup> Id., p. 6.

Further, I question whether it is just and reasonable to set a utility price, as the GAM does, by functionalizing additional costs to the competitive services based on an economies-of-scope theory, while decreasing costs assigned to non-competitive services. If competitive rates are set at the GAM level (thereby, in theory, not reflecting utility economies), rates for non-competitive services will be set below existing costs, customer migration will create ever greater levels of revenue requirement shortfalls, and higher utility rates will necessarily result. Simply allocating more of the utility's actual costs from non-competitive services to competitive services without regard to cost-causation does not, in my view, reasonably approximate the elimination of scope or scale economies from the utilities' cost structures or more reasonably spread the utilities' costs. The approach simply strays too far from concepts of cost causation to yield reasonable results.<sup>76</sup>

Finally, and the ESCOs' arguments to the contrary notwithstanding, I cannot conclude from this record and the experience of retail access to date that prices set as high as the GAM level are required for retail competition.<sup>77</sup> For example, retail migration in the Con Edison territory has been comparatively successful with prices set at 70% of the GAM rate, while retail access in the NYSEG territory has been less successful even though prices are set at 180% of the GAM rate.<sup>78</sup> It would appear, as Staff testified, that many factors beyond the utility's competitive price can significantly influence the success or failure of retail competition.

Accordingly, I do not recommend that the GAM approach be adopted as a matter of statewide policy. Its adoption could lead to a potentially substantial increase in utility rates, and

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<sup>76</sup> Con Edison argues, for example, that the application of the GAM to its information resources costs so over-assigns costs to the competitive function that the results are irrational.

<sup>77</sup> If rates are set at too high a level, both the competitive markets and the economy of the State could be substantially harmed.

<sup>78</sup> Staff's Initial Brief, App. A, B. The competitive rates used in the comparison are for residential supply.

it may not, in any event, result in rates that are just and reasonable to all. Meanwhile, the URM approach is indistinguishable from the general application of cost-causation principles, and both are consistent with the directions of the Commission. However, the devil is in the details of the application of these principles, as discussed below under "Specific Costs." An ECOS study approach, reasonably based on cost causation principles but with sufficient flexibility to consider the reasonable interests of consumers, is the method that should be used in all ECOS studies.

c. The ESCO Statewide Approach

The ESCOs are unpersuasive in arguing that a single, statewide price be established for the electric supply function. Their recommendation is grounded in an adjustment of Staff's GAM allocation of retailing costs. Under GAM, Staff allocates 52% of retailing costs to the competitive functions; the ESCOs allocate 100%. This would imply, unreasonably, that the monopoly delivery services impose no costs for computer resources, call center operations, credit and collections efforts, etc.<sup>79</sup> This method abandons principles of cost-causation and produces an irrational result. In addition, these rates, the highest proposed in the proceeding, are well above existing rates, and, while not quantified in this record, the impact on utility rates from lost revenues could be significant.

It might be ideal from the perspective of market development to have a single statewide rate against which to compete, but the fact is that costs vary to a significant extent from utility to utility, and a uniform rate would be neither cost-based nor equitable.

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<sup>79</sup> ESCO I Initial Brief, App. A has a complete list of the activities.

For the foregoing reasons, the ESCOs' statewide price proposal is not recommended.<sup>80</sup>

d. Special Studies

Staff argues that it is burdensome to understand and verify special studies. Accordingly, it contends, "it is not at all clear that parties should be put through the time and trouble" to analyze them, and "regulators and customers should not bear the burden that their lack of knowledge causes."<sup>81</sup> The ESCOs also argue that the Con Edison and NYSEG special studies should be rejected because they have allegedly been produced only for the purpose of maximizing cost assignments to non-competitive services.<sup>82</sup> Understandably, the utilities defend their own and each others' studies, suggesting that a more-than-sufficient opportunity to investigate them was provided between their filing in March 2002 and the commencement of hearings in November 2002.<sup>83</sup>

While the acceptability of various aspects of the special studies filed by Con Edison and NYSEG will be discussed below, they should not be rejected on the generic grounds that they are complicated and difficult to analyze or that they have consistently been improperly used. Enough time has been allowed for all parties to investigate these studies, and specific challenges to them have been raised. Special studies can be an appropriate method for assigning embedded costs, and the fact that they are complicated and require significant efforts to review should not disqualify them.

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<sup>80</sup> The utilities' complaint that this proposal was first made in the ESCO briefs is not controlling. While the proposal should have been earlier disclosed, this aspect of the case deals mostly with policy questions, and a reasonable opportunity to respond to the proposal has been provided.

<sup>81</sup> Staff Initial Brief, p. 24.

<sup>82</sup> ESCO I Initial Brief, p. 28.

<sup>83</sup> Central Hudson Reply Brief, pp. 13-14; Con Edison Reply Brief, pp. 3-4; NFGDC Reply Brief, p. 6; NYSEG Reply Brief, pp. 16-18; Niagara Mohawk Reply Brief, pp. 3-4.

e. Binding Precedents

NFGDC, Niagara Mohawk, and Central Hudson express concerns that they not be bound by decisions made in the review of the Con Edison and NYSEG ECOS studies. Each argues that it differs materially from both Con Edison and NYSEG, but Niagara Mohawk's claims in this regard are especially broad. It claims that its ". . . service territory, rate and cost structure, settlement agreements, operations, services, customer mix, retail access programs and tariffs are different in most respects from Con Ed's and NYSEG's."<sup>84</sup>

The evidentiary records to be compiled for each of these allegedly disparate entities in the balance of the Unbundling Phase will determine whether these claims can be supported or whether any of the conclusions reached here might also be appropriate for any of the other utilities. Given that these concerns have been the subject of two prior rulings and that the evidence supporting these claims has yet to be reviewed, no purpose would be served by further discussion here.<sup>85</sup>

B. Specific Costs

In this section, the disputes over the allocations and assignments of specific costs in the Con Edison and NYSEG studies will be addressed, following a brief discussion of the context within which these decisions are being made.

As noted above, Staff began with the assertion that "the times they are a-changin'," quoting Bob Dylan. Central Hudson casts aspersions on this authority, characterizing Dylan's song as the theme song of 1960s radicals; but, regardless of the credibility of the source, Staff appears to be correct.<sup>86</sup> The

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<sup>84</sup> Niagara Mohawk Initial Brief, p. 33 (emphasis added).

<sup>85</sup> Case 00-M-0504, Ruling on Motion to Strike (issued October 7, 2002), and Ruling on Schedule, Process, and Discovery (issued July 23, 2002).

<sup>86</sup> While the Dylan lyrics may apply to the utility industry today, perhaps more apposite for a utility lament would be Paul Simon's lyrics: "Time, time, time, see what's become of me, while I look around for my possibilities. I was so hard to please." (A Hazy Shade of Winter, © Paul Simon, 1966.)

structure of the utility industry in New York as it existed for almost a century is today significantly different. With the divestiture of generation, utilities no longer have billions of dollars of generating plant rate base; they no longer buy gas, oil, coal, and enriched uranium for generating fuel; and they no longer have substantial payrolls and related labor expenses at generating plants. In place of the plant and fuel expenses, utilities now incur substantial purchased power costs, facing very different purchasing decisions that can significantly affect both the level and the volatility of energy rates.

In addition, a number of services provided solely by the utilities for decades are now open for competition. While Con Edison does not conceive of itself as a competitor for energy supply, the ESCOs who are attempting to lure its customers away no doubt have a different impression. Further, despite the utilities' arguments to the contrary,<sup>87</sup> a utility still has a vested interest in retaining its customers, even if, like Con Edison, the cost of supply is passed through to customers without a profit margin.<sup>88</sup> This interest is grounded in the perceived uncertainty regarding the recovery of revenues lost due to migration. Based on the briefs filed by the utilities, that uncertainty, in turn, appears to be grounded both in the Commission's limitation that lost revenue recovery will be permitted only if the utilities can establish that they "productively manage and reasonably mitigate their costs"<sup>89</sup> and in the uncertainty surrounding the ultimate operation of the lost revenue recovery mechanism.

It seems apparent, therefore, that the times have changed quite substantially for the utilities, regarding their cost structures, business plans and opportunities, and earnings

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<sup>87</sup> NFGDC Reply Brief, p. 7; Keyspan Delivery Reply Brief, pp. 2-3; Con Edison Reply Brief, pp. 1-2.

<sup>88</sup> There can be no doubt that NYSEG has a direct financial interest in retaining customers on its BRO rate due to the profit potential allowed on the commodity included in that bundled service as a result of its most recent rate proceeding.

<sup>89</sup> March Order, p. 23.

risks. This underscores Staff's point that ECOS studies performed today to develop competitive rates must be performed with the new landscape in mind. As the Commission noted, the historical application of ECOS concepts and methods "may not provide much useful guidance for the current efforts."<sup>90</sup> With this background in mind and with the expectation that the times will continue to change, the disputes over the assignment of specific costs will be addressed.

Staff challenges Con Edison's functionalization of the costs of credit and collections, uncollectibles, gas sales promotional expenses, working capital, information resources, and gas reliability costs.<sup>91</sup> The ESCOs challenge the functionalization of all customer care activities (e.g., call and service centers, complaints, credit and collections, theft of service), uncollectible costs, and A&G expenses.<sup>92</sup> The CPB challenges the functionalization of credit and collections and theft-related costs, overhead costs, and gas promotion costs. Many of the same issues are raised concerning NYSEG's study, and additional issues are raised by a late-joined question on the return on equity (ROE) NYSEG used in its study, the appropriate assignment of costs to the meter ownership function, the proper allocation of natural gas call center costs, and the proper allocation of regulatory commission expenses. Each of these areas is discussed below.

#### 1. Credit and Collections

Con Edison and NYSEG functionalized 100% of credit and collection costs (including theft of service related costs) to the non-competitive delivery services. Staff assigned a portion of the costs (about 53%) to non-competitive services and a

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<sup>90</sup> November Order, p. 11.

<sup>91</sup> Staff Initial Brief, pp. 25-31.

<sup>92</sup> ESCO II Initial Brief, pp. 12-28.

portion (about 47%) to competitive services,<sup>93</sup> based on revenues, as did the ESCOs<sup>94</sup> and CPB.

Con Edison defends its functionalization with the claim that it ". . . incurs credit and collections costs in providing a single product--delivery service."<sup>95</sup> According to Con Edison, even if 100% of its customers were to migrate to ESCO commodity service (thereby reducing Con Edison's total revenues by 40%-50%), Con Edison's credit and collection activities and costs would nevertheless remain the same, as would its legal obligations to the migrating customer.<sup>96</sup> Because its costs will not decrease proportionally with an increase in customer migration to other commodity suppliers, Con Edison concludes that credit and collection costs are all attributable to non-competitive delivery service.<sup>97</sup> Perhaps most broadly, Con Edison contends ". . . that its credit and collection and theft related activities were developed to support the Company's monopoly service - i.e., delivery service and not competitive functions . . ."<sup>98</sup> Finally, Con Edison contends that if these costs should be allocated to all functions, the allocation should be done on the basis of labor, not total revenues.

NYSEG likewise argues that it assigned 100% of these costs to delivery services because it would continue to incur these costs even if all customers migrated to competitive commodity suppliers.<sup>99</sup> In effect, NYSEG contends that the requirements of the Home Energy Fair Practices Act (HEFPA), a

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<sup>93</sup> Exhibit 47, schedule SP10-C.

<sup>94</sup> The ESCOs functionalized costs on the basis of revenue requirements less overhead costs (ESCO II Initial Brief, p. 23, n. 22), which should produce comparable results.

<sup>95</sup> Con Edison Initial Brief, p. 18.

<sup>96</sup> Id., pp. 18-19.

<sup>97</sup> Con Edison contends that there is no basis in the record to conclude that there is a linear relationship between credit and collection costs and customer migration (Con Edison Reply Brief, p. 8), despite Mr. Hornby's illustrative testimony to the contrary (Tr. 1064-1067).

<sup>98</sup> Id., p. 4.

<sup>99</sup> NYSEG's Initial Brief, p. 15.

major driver of its credit and collection costs, result in the company's inability to avoid any of these costs regardless of the level of retail migration.<sup>100</sup> NYSEG also argues that its functionalization of these costs is consistent with the Commission's March Order, which required, in preparing the ECOS studies, a consideration of efforts in related areas, such as the orders issued in the Alternate Billing Arrangements Case.<sup>101</sup> Because those orders designated certain activities as competitive for billing purposes, but did not include credit and collection costs within those competitive functions, the company views its 100% functionalization of these costs to non-competitive functions as consistent with the Commission's orders, and the adjusted functionalization of the non-utility parties as contrary to those orders.<sup>102</sup> The arguments of those parties fail, according to NYSEG, because they do not acknowledge that migration will not enable NYSEG to avoid any costs in this area.

The other utilities (Central Hudson, Keyspan Delivery, and Niagara Mohawk) generally support the approach taken by Con Edison and NYSEG. Central Hudson contends that, if principles of cost causation are appropriately applied and the utility ceases an activity, then the costs applied to that activity would also cease. Conversely, it argues, if costs do not cease when a customer migrates to another provider for a competitive service, then it cannot be argued that the competitive service "caused" the cost. This is not the application of an avoided cost methodology, according to Central Hudson, but the proper application of cost causation techniques.<sup>103</sup> Keyspan Delivery argues that the non-utility parties abandon principles of cost

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<sup>100</sup> Id., pp. 16-17.

<sup>101</sup> The company cites (Initial Brief., p. 17) two orders: Case 99-M-0631, Customer Billings Arrangements, Order Providing for Customer Choice of Billing Entity (issued March 22, 2000), and Order Establishing Uniform Retail Access Billing and Payment Processing Practices (issued May 18, 2001).

<sup>102</sup> NYSEG Reply Brief, pp. 25-27.

<sup>103</sup> Central Hudson Reply Brief, p. 20.

causation in an effort to develop inflated competitive rates.<sup>104</sup> Niagara Mohawk contends that credit and collection costs are driven by the number of bills generated, not by revenues, and the non-utility parties' use of revenues as an allocator abandons cost causation principles.<sup>105</sup>

Staff argues that these costs are analogous to uncollectible costs and should be functionalized on the same basis--i.e., by revenues. Staff notes that both utilities provide commodity service, and there is no logical reason not to allocate credit and collection costs to such services, other than by using an avoided cost approach, which has been rejected by the Commission. Staff also notes that the results of credit and collection activities are to generate revenues for the company, which include revenues for both commodity sales and delivery sales. Accordingly, it argues, the costs of the activities should be associated with the benefits.

The other non-utility parties generally agree with Staff. CPB contends that allocating no portion of credit and collection costs to commodity services is simply irrational.<sup>106</sup> Keyspan Supply argues that Con Edison's results reflect use of a top-down unbundling approach rather than the bottom-up approach directed by the Commission.<sup>107</sup> NEM argues that the utilities' allocations are an attempt to have the Commission adopt an avoided cost approach under the guide of cost causation, a position the Commission has already rejected.<sup>108</sup> Nucor concurs regarding NYSEG's studies.<sup>109</sup>

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<sup>104</sup> Keyspan Delivery Reply Brief, pp. 5-7.

<sup>105</sup> Niagara Mohawk Reply Brief, pp. 5-7.

<sup>106</sup> CPB Reply Brief, p. 4.

<sup>107</sup> Con Edison's approach was top-down, according to Keyspan Supply, because Con Edison first assigned its total revenue requirement for delivery service to non-competitive services and only thereafter examined the remaining costs (Keyspan Supply Reply Brief, p. 2).

<sup>108</sup> NEM Reply Brief, p. 2.

<sup>109</sup> Nucor Reply Brief, p. 2.

The Con Edison and NYSEG studies are not avoided cost studies; rather, they are based on traditional concepts of cost causation. It is uncontested that the costs allocated and assigned in the studies are embedded costs, and there is no calculation in the record of what the costs would be at the margin--i.e., if a single customer left or were added to the system. Furthermore, as Central Hudson correctly argues, if service X causes \$10 in costs and service X is eliminated, then one would expect a \$10 reduction in costs if principles of cost causation were correctly applied. That said, however, the Con Edison and NYSEG studies fail to consider the fact that there can be and usually will be more than one factor that influences or drives costs. While the number of customers affects credit and collection costs, there are other factors that can also affect the level of costs, such as the average total level of uncollectibles, the average per-customer level of delinquencies, or the amount owed by an individual customer. It is not reasonable to assume that the costs incurred to collect a \$10 overdue payment would be the same as the costs incurred to collect \$1000.<sup>110</sup> Thus, though the utilities applied principles of cost causation and may have done so in a manner consistent with pre-competition methods, that alone does not decide the issue.

Moreover, I find unpersuasive Con Edison's arguments that it incurs credit and collection costs in providing a single service--delivery--and that these activities were developed only to support delivery service. It is clear that Con Edison sells more than just delivery service and, when it collects overdue payments, the revenues include both delivery and commodity amounts. Further, these activities were created years ago to support strictly monopoly services including commodity as well as delivery. The assertion that collection activities created years

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<sup>110</sup> Con Edison (Tr. 898) acknowledged that there may be some impact on credit and collection activities from factors other than the number of customers alone. Were this not the case, it would raise serious questions of prudence regarding the utility's obligation to productively manage and reasonably mitigate its costs.

ago were only intended to support delivery functions is unreasonable.

NYSEG's reliance on prior Commission orders in the Customer Billing Arrangements proceeding also is unpersuasive. First, while the Commission did not include credit and collection costs within the competitive billing function, the orders do not address the question of spreading these costs to other competitive services. More fundamental, however, is the Commission's expressed intent that this case undertake a more complete review of utility costs than had been undertaken in establishing existing backout credits. The Commission directly addressed its experience in the Customer Billing Arrangements case as follows: "The experience gained through our efforts to set backout credits for billing and metering functions should illuminate but should not define the inquiry here."<sup>111</sup>

The orders cited by NYSEG are not binding here, and the argument that HEFPA will prevent the utility from avoiding any of these costs also is not determinative.<sup>112</sup> The point of this exercise is not to set a competitive rate based on costs that might be avoided, but to set just and reasonable competitive rates that fairly reflect utility embedded costs. If rates were set considering only the costs the utilities might avoid, there would be no need for a lost revenue recovery mechanism, for the lost revenues would equal the avoided costs. Further, as I noted earlier, total societal costs are likely to increase as utility economies of scope and scale are diminished, and the question here is how the utilities' costs are properly functionalized and assigned for the purpose of establishing a competitive rate that is fair to the utilities, the ESCOs, and the consumers.

I agree with Staff's observation that there is no logical reason not to allocate credit and collection costs to the prices of all services, especially if the customer's perspective

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<sup>111</sup> Order Directing Expedited Consideration of Rate Unbundling, supra, p. 4. See also November Order, p. 4.

<sup>112</sup> This alleged fact would be more relevant to the question of whether the utilities productively manage or reasonably mitigate their costs.

is considered. Credit and collection costs ought to be included in all prices, because collection efforts yield revenues attributable to all services, including competitive services. If a consumer elects to take fewer services from the utility, it seems reasonable that he would expect to avoid some portion of this utility payment for credit and collection services, probably an amount proportional to the reduction in the customer's utility payments. As the Commission stated: "If the customer cannot avoid such costs by migrating to a competitive supplier, the attractiveness of retail access is diminished and market development will be impeded."<sup>113</sup>

The utilities' studies might well have gone unchallenged in another era, when the intricate details being examined here were of less consequence and the purpose of the exercise was substantially different. In this proceeding, however, I find the company's functionalization of 100% of credit and collection costs to the delivery service to be unreasonable to the customers and the ESCOs. Nor am I convinced that the proper allocator is labor, as Con Edison contends. While a large portion of these costs are labor, that fact provides no basis for allocating credit and collection costs in the same proportion as all other labor costs.<sup>114</sup> Staff's proposal to allocate these costs to competitive and non-competitive services on the basis of revenues should be adopted.

A final issue concerns the use of revenues, including commodity, as an allocator of costs. Because commodity costs vary over time, NYSEG argues, assigning costs on the basis of revenues results in uncertain and fluctuating results.<sup>115</sup> Staff contends that there is a causal link between revenues, including commodity, and credit and collection costs, but NYSEG denies any linear relationship.

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<sup>113</sup> March Order, p. 24.

<sup>114</sup> Allocating these costs by labor would result in a very small percentage of these costs being assigned to competitive functions because the vast majority of a utility's labor costs are incurred in the non-competitive delivery area.

<sup>115</sup> NYSEG Reply Brief, p. 15.

As noted above, I believe there is a causal link, although it may not be linear, as NYSEG and Con Edison contend. Further, while commodity costs do vary over time, the volatility of average annual costs is not likely to approach the volatility of the spot markets. The evidence presented here does not support a conclusion that the variability of annual commodity costs would have a material impact on the use of revenues to allocate costs.

## 2. Uncollectibles

NYSEG allocated the cost of uncollectibles to competitive and non-competitive services based on revenues, considering these costs to be a function of revenues. Staff and the other non-utility parties generally agree, and the allocation seems reasonable from a customer perspective. NYSEG's approach should be approved.

Con Edison likewise allocated these costs based on revenues, but it adjusted the allocations between competitive and non-competitive services in light of a study showing that retail access customers had a lower level of uncollectibles in 2000 than the utility's system average. Staff and ESCO II imply that the future may not be reflected in the company's study and that uncollectibles will vary strictly with revenues and not with retail access.<sup>116</sup>

The Staff/ESCO/NYSEG position seems the most reasonable, and the Con Edison approach is not adopted. First, it is not clear that Con Edison's study is representative. At mid-year 2000 (the year of the embedded costs being studied) approximately 1.9% of the company's electric customers had migrated, and through December 2002, that percentage more than doubled to 5.3%.<sup>117</sup> It is more likely, in my view, that the uncollectible rate for retail access customers has changed since 2000 and will continue move toward the overall system average. Further, one of the reasons the ESCOs may be seeing a higher

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<sup>116</sup> Staff Initial Brief, p. 26; ESCO II Reply Brief, pp. 10-12.

<sup>117</sup> This information was drawn from the monthly migration reports submitted by the utilities.

uncollectible rate<sup>118</sup> than the utility for the same subset of customers is the possibly significant difference between the ESCOs' and the utilities' ability to require timely payment. Until recently, only utilities could turn off service to a customer for non-payment--a strong incentive to pay. The ESCOs could stop supplying commodity if the customer refused to pay, but the customer would be returned to utility service and would not be shut off for failure to pay the ESCO. Under Chapter 686 of the Laws of 2002, this situation has significantly changed, which could affect utility and ESCO uncollectibles alike.

Finally, from the customers' perspective, prices paid to the utility include utility system average uncollectible expense. If the customer migrates to a competitive commodity supplier, he or she would expect to avoid paying that system average cost on those amounts the customer now pays the ESCO. Con Edison's approach does not produce this result, and the results of its study, for all of the above reasons, are not accepted. Uncollectibles should be assigned based on revenues, without the adjustment proposed by Con Edison.

### 3. Gas Sales Promotion Expenses

NYSEG and Con Edison functionalize gas promotional expense entirely to delivery service, while Staff and the other non-utility studies functionalize the costs to both competitive and non-competitive services. Con Edison argues that these costs foster the use of gas and therefore of its delivery system as well. This increased system usage, regardless of the seller of the gas, benefits all gas users by lowering the per-customer delivery cost of the system, according to Con Edison.<sup>119</sup> According to its witness, none of the costs are used to advance Con Edison's sale of commodity. NYSEG points out in addition that when a customer switches to gas heating, the available

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<sup>118</sup> The ESCOs imply that their uncollectible experience is higher than the utilities, but there is no record evidence on this issue.

<sup>119</sup> Con Edison Initial Brief, pp. 27-28.

market for ESCO gas sales increases.<sup>120</sup> Staff argues that a customer purchasing commodity from an ESCO should not be burdened with the cost of the utility's gas promotional expenses.<sup>121</sup> It suggests that the ESCO customer would be paying twice for promotional expenses--once to the ESCO and once to the utility, thereby discouraging migration.

If the utilities had a profit opportunity in the sale of gas commodity, the benefits of the promotional expenses would accrue in part to the utility and in part to its customers. That would justify allocating some portion of the expense to competitive services, but that is not the case here. The benefits of these expenses will be reflected in delivery rates and will flow in equal measure to full service and delivery customers. The costs, therefore, are fairly allocated to all customers (i.e., the costs should be allocated to delivery). In addition, from the customer's perspective, cost-justified promotional expenses will by definition more than pay for themselves in benefits generated, and retail access customers should continue to pay for those costs so long as they continue to receive the benefits.

#### 4. Working Capital-EBCAP

Working capital issues were raised in two areas of Con Edison's study: the functionalization of the earnings base capitalization adjustment (EBCAP), and the cost of working capital used by Con Edison in connection with electric purchased power.<sup>122</sup> In addition, the ESCOs challenged NYSEG's failure to apply any working capital cost to purchased power.

Con Edison applied the EBCAP adjustment only to working capital, thereby reducing the cost of working capital and raising the cost of the company's remaining capital, as compared to the

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<sup>120</sup> NYSEG Initial Brief, p. 32.

<sup>121</sup> Staff Initial Brief, pp. 27-30.

<sup>122</sup> Con Edison Initial Brief, pp. 28-30. As Con Edison notes, the EBCAP issue affects a number of activities where capital carrying costs are required, especially in the area of gas storage costs.

uniform distribution of the EBCAP adjustment urged by Staff. Because the major component of working capital is estimated while other capitalization is known, and because the purpose of the EBCAP adjustment is to align rate base with capitalization, the company argues that the adjustment would be most appropriately applied to working capital alone. It also argues that Staff supported and the Commission approved this approach in the early 1990s.

Staff argues that Commission orders from an earlier era are not controlling, because the studies being examined here have been prepared for a substantially different purpose. The allocation of working capital net of the EBCAP adjustment as proposed by Con Edison would have little or no impact when the ECOS study is being used for interclass rate design, but it has a large impact if competitive rates are being set, especially on the working capital allowance for gas storage.<sup>123</sup> Staff also contends that three of the four main components of working capital are known, not estimated, and that Con Edison's justification for its allocation is therefore wrong.

As a general matter, the EBCAP adjustment reduces the company's rate base to equal its capitalization. The purpose is to prevent the company from earning a return on capitalization that it did not provide. While differences between rate base and capitalization can be caused by a number of factors, including the estimated portion of working capital noted by Con Edison, the application of the adjustment reduces the company's overall rate base. By not applying the adjustment to all rate base components, Con Edison artificially lowers the cost of working capital, while raising the cost on the balance of the company's rate base. Such a result is not reasonable where a fair allocation of all costs and credits to all services is being attempted. Accordingly, the EBCAP adjustment should be allocated to all capital as recommended by Staff.

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<sup>123</sup> Staff Initial Brief, p. 13.

5. Working Capital-Purchased Power

Regarding working capital for electric purchased power, Con Edison defended its use of a 6% short-term capital cost rate (rather than the company's overall cost of capital) based on the short, six-day lag between costs and revenues for this activity. It also argued that no working capital allowance for these activities is included in rates, and applying Staff's higher, average cost of capital rate would inflate the impact on the cost of supply without justification.

NYSEG contends that it followed the FERC method of calculating working capital, which excludes working capital on purchased power costs by definition. Because the application of the FERC method results in no working capital allowance for purchased power, NYSEG contends, the ESCOs' allocation of a working capital allowance to purchased power expense would be improper. NYSEG also argues that its rates do not include any allowance for working capital associated with purchased power.

As the companies argue in different contexts, Con Edison's and NYSEG's rates have been set on the basis of negotiated results, and the specific costs that are covered in the companies' revenue requirements depend on the views of the signatories to the agreements. It is not possible, therefore, to conclude that any particular costs are included or not included in rates. In addition, the purpose here is to identify and allocate historical costs, not historical rates. For similar reasons, the historical FERC approach to the calculation of working capital for the purpose of setting rates is not controlling. So long as there is a lag between payment for purchased power and the receipt of revenues to cover those payments (a fact Con Edison concedes), there is a need for working capital and there will be an associated cost. Accordingly, the ESCOs' proposal that NYSEG's study include working capital costs reflecting a six-day lag for purchased power is reasonable and should be adopted.

Regarding the cost rate for that working capital, Con Edison might justify its use of a short-term interest rate if it could establish that power was purchased strictly from the

proceeds of short-term loans. But because the various sources of capitalization are not generally isolated and separately tracked, it is unlikely that the company could make a showing that proceeds from short-term loans provided the exclusive source of funds to purchase power, and, in any event, the record here contains no such proof. As a result, I conclude that applying the companies' overall cost of capital would be the most reasonable way to calculate working capital costs for power purchases.

6. Meter Ownership Costs

Two issues are raised regarding competitive metering services as reflected in NYSEG's ECOS. First, Staff challenges NYSEG's assignment of meter installation costs to the meter ownership function rather than the meter service provider function as undertaken by Con Edison. According to Staff, NYSEG's approach is not consistent with the requirements of the November Order.<sup>124</sup> Second, Staff challenges as unsupported NYSEG's failure to spread clearing account costs to meter ownership.<sup>125</sup>

NYSEG argues that it assigned only initial installation costs to meter ownership, with the cost of subsequent exchanges or replacements being assigned to the meter service provider function.<sup>126</sup> It further notes that the choice between Staff's method and its own has no discernable impact on competitive metering prices because, under the current rules, meter ownership and meter service provider functions cannot be separately purchased. Regarding the assignment of customer care clearing accounts, NYSEG contends that its customer care special study revealed no customer care related costs associated with meter equipment. Finally, it notes that spreading clearing account costs to meter ownership could result in a double-count of labor related to the A&G expenses spread to these functions.

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<sup>124</sup> Staff Initial Brief, p. 9.

<sup>125</sup> Id., p. 20-21.

<sup>126</sup> NYSEG Reply Brief, pp. 24-25.

Staff appears to be correct that the November Order (Attachment A) places the costs of installing meters under the meter service provider function, and lists under meter ownership only "Physical Meters." And while the company appears to be correct that, under today's definitions of the market, its assignment of installation costs should make no difference, the most recent order on the assignment of metering costs should control, and the assignment of installation costs in NYSEG's study should be limited to the meter service provider function. In addition, if initial installation labor costs are not assigned to meter ownership, there should be no double count of labor costs.

NYSEG's Customer Care special study resulted in a zero allocation of clearing account costs to meter ownership, supply at market, and non-bypassable wires charge.<sup>127</sup> Staff adopted the study for the purpose of the URM except for gas customer contact costs (discussed below) and credit and collection costs (discussed above).<sup>128</sup> NYSEG argues that it is illogical to accept the study for some purposes and not for others.

It is appropriate, in my view, to accept some of the allocations resulting from a special study and to reject others. Accepting NYSEG's argument that the study should be accepted or rejected as a whole precludes any effort to analyze the functionalization and allocation of the individual costs that are examined in the special study. For example, Staff rejected the results of the study for natural gas call center costs in view of the fixed commodity price that existed during the study period, an adjustment that would not be possible if NYSEG's theory were adopted.

It was the Commission's intent in this case to examine each category of utility cost and to allocate each in a reasonable manner. Including a cost within a special study should not preclude a review of the reasonableness of the cost's allocation simply because it was grouped with other costs in the

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<sup>127</sup> NYSEG Initial Brief, p. 23.

<sup>128</sup> Staff Initial Brief, p. 10.

study. Conversely, the mere fact that one category of costs was not reasonably functionalized and assigned by the study does not justify rejecting the study's allocation of other costs. Therefore, it is not illogical, as NYSEG claims, to accept some allocations flowing from a special study and to reject others.

The November Order (Attachment A) required the utilities to justify any allocation of clearing accounts to less than all functions. In my view, NYSEG's special study fails to provide an adequate justification for not spreading the customer care clearing accounts to meter ownership.

#### 7. Regulatory Commission Expenses

Con Edison functionalized regulatory Commission expenses imposed under Public Service Law §18-a to the delivery function.<sup>129</sup> NYSEG functionalized these costs based on physical plant.<sup>130</sup> The ESCOs challenged these assignments, offering instead an allocation based on the revenue requirement of each service.<sup>131</sup> Contending that regulatory expenses are explicitly based on utility revenues, the ESCOs allege that this is one of the clearest allocations in the case.<sup>132</sup>

NYSEG argues in reply that these expenses are a result of the utility's role as a monopoly supplier of delivery services, and that its expenses would not change even if all its customers migrated to ESCOs.<sup>133</sup> Con Edison notes that its regulatory assessments will remain the same, despite migration, unless the ESCOs are willing to share the burden of regulatory costs.<sup>134</sup>

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<sup>129</sup> Con Edison Initial Brief, p. 30.

<sup>130</sup> NYSEG Initial Brief, p. 25. As a practical matter, NYSEG's allocation results in the vast majority of these costs being assigned to delivery because the vast majority of plant costs support the delivery function.

<sup>131</sup> ESCO II Initial Brief, p. 27.

<sup>132</sup> ESCO I Initial Brief, p. 26.

<sup>133</sup> NYSEG Reply Brief, pp. 27-28.

<sup>134</sup> Con Edison Reply Brief, p. 16.

The utilities correctly note that regulatory expenses are allocated among utilities on the basis of their relative revenues, but the expenses are not a function of utility revenues. More fundamentally, however, the question is whether a migrating consumer loses the benefits provided by the regulatory expense, such that the migrating consumer should expect to avoid the costs. Regulatory efforts benefit the ESCO customer and the utility customer alike. The regulator sets the utility price, which, one could argue, establishes a limit on the prices ESCOs can successfully charge. While ESCO prices are not regulated, the regulator defines critical market parameters (one of which is the utilities' price for competitive services), which ultimately benefit all customers. Further, under Chapter 686 of the Laws of 2002, it appears that the regulator will be addressing and resolving complaints between ESCOs and their customers, as it now does for customer-utility disputes.

Therefore, ESCO customers continue to "purchase" the benefits of regulatory Commission expenses whether they buy commodity from the utility or the ESCO, and it would be reasonable to continue to require them to contribute to that function in either case. Both the Con Edison and NYSEG studies accomplish this basic result, albeit in a slightly different manner, and both approaches should be approved.

#### 8. Rate of Return & NYSEG Commodity Risk

Two issues are raised in this area: the appropriate return to use for competitive services; and the return NYSEG used in its study. Except for the working capital associated with electric purchased power costs (discussed above), Con Edison used its return on equity sharing threshold to develop carrying costs in accordance with the Commission's November Order.<sup>135</sup> NYSEG used its allowed return for gas operations (10.5%) as recently approved by the Commission,<sup>136</sup> and its earned return for the year

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<sup>135</sup> November Order, p. 12.

<sup>136</sup> Case 01-G-1668, Rates, Charges, Rules, and Regulations for New York State Electric & Gas Corp - Gas Service, Order Establishing Rates (issued November 20, 2002).

2000 calculated in accordance with its 1998 rate plan.<sup>137</sup> NYSEG did not use either of the electric earnings sharing thresholds set forth in its most recent rate plan.<sup>138</sup>

The ESCOs argue generally that competitive endeavors are more risky than a monopoly business and, therefore, the cost of capital for competitive functions should be higher than the regulated allowance for a utility's overall business.<sup>139</sup>

Staff notes that changing the cost of capital would have only a de minimis impact on study results, except for the meter ownership function. Further, for Con Edison, a higher-than-allowed return was used in its ECOS study and, Staff argues, that return should partially address the ESCOs' concerns. In addition, Staff observes, no one has attempted on this record to quantify the inherent risk differential between competitive and non-competitive services.<sup>140</sup>

Staff rejects, however, NYSEG's use of an 11.1% overall return calculated for year 2000 electric operations and recommends that the study use the earnings sharing threshold contained in NYSEG's most recent proceeding.<sup>141</sup> NYSEG objects, arguing that it has no allowed return in its most recent rate plan (the first option offered by the Commission), that its rates were not set using its earnings sharing threshold (the second option offered), and that the most reasonable approach is to use its earned return for the period in question.<sup>142</sup>

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<sup>137</sup> NYSEG Reply Brief, pp. 9-11.

<sup>138</sup> In the Joint Proposal (p. 16), the terms of which were adopted with modifications in Cases 01-E-0359 and 01-M-0404, NYSEG has two earnings sharing thresholds applicable for the period 1/1/03 through 12/31/06. One threshold measures the company's return on its delivery business (12.5%) and one applies to its overall business including commodity profits (15.5%).

<sup>139</sup> ESCO I Initial Brief, pp. 8-9.

<sup>140</sup> Staff Initial Brief, pp. 15-16.

<sup>141</sup> NYSEG notes that the use of Staff's proposed 12.5% equity return would actually lower the overall capital costs included in NYSEG's study.

<sup>142</sup> NYSEG Reply Brief, pp. 9-11.

The Commission suggested the use, to calculate carrying charges, of the allowed return on equity, or if none exists, the earnings sharing threshold in a company's rate plan.<sup>143</sup> The Commission also allowed a different approach to be used if it could be justified. A fair reading of the Commission's order in this regard is that any party could propose a different approach, including an approach that would recognize the higher risks associated with competitive services. Con Edison's assertion that the Commission precluded such a step<sup>144</sup> is not correct.

The ESCOs argue that a higher return should be used in calculating carrying costs for competitive services, but they have not proposed a return that would be more appropriate for Con Edison or NYSEG. Staff's observations that the use of earnings threshold levels implicitly contains a competitive premium, and that the record supports no other adjustment, settle the matter for Con Edison, and no additional adjustment is warranted based on this record.

The situation for NYSEG differs significantly. As Nucor argues, NYSEG's newest rate plan subjects the company to possibly significant risks regarding commodity sales,<sup>145</sup> risks not faced by Con Edison. Those risks are reflected in two ways. First, NYSEG has been allowed to add a "premium" to the cost of commodity under its BRO service.<sup>146</sup> This premium was not in effect in 2000 and therefore is not reflected in NYSEG's ECOS study. Second, unlike Con Edison, NYSEG has two different earnings thresholds, one strictly limited to its delivery service (12.5%) and one that includes both delivery and commodity service (15.5%). Again, the increased risks and increased cost of capital associated with having a profit or loss opportunity in

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<sup>143</sup> November Order, p. 12.

<sup>144</sup> Con Edison Reply Brief, p. 31.

<sup>145</sup> Case 01-E-0359, NYSEG's Electric Price Protection Plan, Order Adopting Provisions of Joint Proposal with Modifications (issued February 27, 2002), pp. 7, 11, n. 11.

<sup>146</sup> A portion of the allowed 35% premium is intend to recover commodity related costs and a portion is intended to compensate for NYSEG's increased risk in offering a fixed-rate service by providing an additional profit margin.

competitive commodity sales are reflected in the dual sharing thresholds.

While this suggests that NYSEG should use a 15.5% equity return for competitive services, the use of a higher return would have almost no impact on costs assigned to competitive commodity, where NYSEG faces virtually all of its competitive risks. Rather than adjust capital costs, Nucor suggests that 20% of NYSEG's A&G expenses be functionalized to supply procurement, based on its calculation that profits from commodity sales could account for as much as 20% of the company's pre-tax earnings.<sup>147</sup> Nucor's analysis of outside services costs (a subset of A&G costs), leads it to conclude that the result of the company's allocations is unreasonable. Accordingly, Nucor would add an additional \$18 million of A&G costs to supply procurement.<sup>148</sup> Staff indicates that the URM allocates \$2.4 million of A&G costs to supply procurement, the GAM allocates \$11.4 million, and Staff quantifies Nucor's functionalization at about \$12.8 million.<sup>149</sup>

The evidence supports a finding that NYSEG's allocation of less than 1% of the costs of outside services to the competitive functions is unreasonable. Staff argues that the costs cited by Nucor are historical and should be normalized as non-recurring. It is clear, however, that the newly created (effective 1/1/03) electric commodity profit center will potentially result in new or additional costs and different cost allocations in the future, which were not considered when the study was undertaken. Therefore, I disagree with Staff's view that these costs should be treated as non-recurring.

A more reasonable allocation of outside services costs to electric commodity is required in NYSEG's study. While a

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<sup>147</sup> Nucor Initial Brief, p. 2.

<sup>148</sup> It is not clear whether Nucor is recommending that these costs be allocated to both electric and gas procurement or only to electric procurement.

<sup>149</sup> Staff Initial Brief, p. 32. The reason for the difference between Nucor's \$18 million adjustment and Staff's view of Nucor's adjustment at \$12.8 million is not clear.

special study of these costs might prove useful, in its absence, the \$9.8 million of outside services costs should be assigned by revenues to electric supply and delivery functions.<sup>150</sup> Except as otherwise required here, NYSEG's remaining A&G costs should be functionalized according to its study.

I also find Staff's arguments persuasive regarding the use of the 12.5% equity sharing threshold for NYSEG. In light of the significant changes in NYSEG's rates and profit centers since 2000, it seems more reasonable to use an updated proxy for NYSEG's capital costs. The fact that more recent information will result in a slight decline in the costs allocated to competitive services is irrelevant. The purpose here is to set reasonable competitive prices, and whether the best information available results in a higher or lower competitive rate than originally calculated does not matter to the task at hand.

#### 9. NYSEG Customer Care Costs

As noted above, Staff objected to the allocation of gas call center costs as contained in NYSEG's Customer Care special study. Staff argues that during the study's historical period, NYSEG's gas commodity prices were fixed, resulting in few calls or complaints concerning the cost of gas.<sup>151</sup> In essence, Staff argues that the recent change from a fixed gas commodity rate to a floating rate renders the special study an unreliable basis on which to assign these costs. The URM appears to adopt the company's position (notwithstanding Staff's objections), while the GAM spreads all customer contact costs by revenues to reflect the fact that all functions benefit from these services.

NYSEG assigned 100% of its customer contact costs to delivery because they are related to bill calculation, which, unlike bill issuance and payment processing, has not been

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<sup>150</sup> The outside services costs should be spread only to the electric supply and delivery functions, allocated by revenues.

<sup>151</sup> Staff's Initial Brief, p. 27. Staff did not specifically challenge the results of the study from the perspective of call center costs regarding electric supply.

determined in earlier Commission orders to be competitive.<sup>152</sup> NYSEG also allocates 100% of consumer affairs costs (costs to resolve customer complaints) to delivery, on the theory that the HEFPA complaint process is mandatory for both full service and delivery-only customers.

Staff's concern regarding the results of the special study concerning gas call center costs appear to be valid. If these costs can be separately identified and assigned, NYSEG should do so by revenues rather than in reliance on its special study. If not, all customer contact costs should be allocated by revenues. From an ESCO customer's perspective, calls concerning gas or electric commodity will no longer be placed to NYSEG, and such a customer should expect to be able to avoid some portion of these costs. While allocators other than revenues might be more reasonable, NYSEG's allocation of 100% of gas call center costs to delivery is not.

The same observation is valid regarding NYSEG's allocation of 100% of customer affairs costs to delivery. Full service customer complaints concerning commodity or delivery will continue to go to the utility, but ESCO commodity customers will be dealing with the ESCO for commodity inquiries or complaints. Therefore, it is reasonable to assume that a migrating customer should be able to avoid a portion of the utility costs. NYSEG's assignment of costs, however, will not allow that to happen.

NYSEG's arguments regarding HEFPA are not persuasive. When the briefs were filed in this proceeding, only the utilities were subject HEFPA, but now the ESCOs are as well.<sup>153</sup> In a sense, HEFPA protections have become competitive services. When a customer migrates, the HEFPA protections for the commodity portion of the service will be provided by the ESCOs, and those customers should not have to pay the utility for the same services. Under NYSEG's proposal, however, the customer avoids none of the utility HEFPA costs, while also being responsible for the ESCO's costs to provide HEFPA protections on commodity. If

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<sup>152</sup> NYSEG's Initial Brief, p. 19.

<sup>153</sup> An important exception is the obligation to serve, which is not imposed on the ESCOs (Chapter 686, Laws of 2002).

NYSEG's approach were adopted, monopoly revenues would be subsidizing a competitive service.

Based on the above, NYSEG's allocation of customer affairs costs solely to delivery should be rejected. These costs should be spread to all functions based on revenues.

10. Con Edison Information Resources,  
Call Center and Service Center Costs

Con Edison performed special studies regarding call center and service center costs, and allocated information resources (IR) costs based on the number of computers utilized in each function.<sup>154</sup> Regarding Staff's GAM allocation, Con Edison complains, for example, that spreading IR costs by revenues produces irrational results for both gas and electric functions. Staff defends its allocation of IR costs, arguing that computer records of customer information are retailing costs and they should be spread to all services by revenues under its GAM allocation theory.<sup>155</sup> Staff did not otherwise specifically challenge the Con Edison allocation of these costs between competitive and non-competitive services.

The ESCOs challenge Con Edison's allocation of customer care activities, specifically credit and collections (discussed above).<sup>156</sup> No specific challenges were raised to Con Edison's study of IR, call center, service center, or complaint handling costs. The ESCOs object to the allocations from a results perspective, arguing, for example, that "only 25%" of Accounts 901, 903, and 905 are allocated to the competitive function.

Con Edison's argument that the GAM (or a revenue based) allocation of IR costs produces irrational results is persuasive. If the GAM is adopted generally, it should not be applied to IR costs.

Regarding the balance of Con Edison's special studies in this area, the record contains no specific challenges and I remain unconvinced by the generic challenges raised by the ESCOs.

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<sup>154</sup> Con Edison Initial Brief, p. 23.

<sup>155</sup> Staff Reply Brief, p. 17.

<sup>156</sup> ESCO II Initial Brief, pp. 17-25.

Con Edison has spread the costs of service and call centers, IR services, and the meter action group to both competitive and non-competitive services in a rational manner. While there may be better approaches to functionalizing and assigning these costs, this record suggests the use of revenues as an allocator is not superior to Con Edison's study, and no other approach has been proposed by the parties. Con Edison's study regarding these costs should therefore be adopted, except as may be otherwise recommended herein.

11. Gas Reliability Costs

In accordance with the November Order, Con Edison detailed its costs of maintaining gas reliability and functionalized 100% of those costs to distribution.<sup>157</sup> The company explained that some of its assets are used to maintain supply reliability from interruptions due to well freeze-offs, hurricanes, and other events. Costs are also incurred to prevent service interruptions for ESCO terminations or defaults or for customers who voluntarily return to the utility. The company contends that these costs are now recovered only from full service customers, even though some of the costs are incurred for the direct benefit of ESCO customers who avoid paying for the service because of the current rate design. Con Edison requests that its method of calculating and functionalizing these costs be approved here for ultimate adoption in the next Con Edison and Orange and Rockland rate proceedings.

Staff argues that this issue need not and should not be addressed here. It need not be addressed, it argues, because the costs are part of gas expense, which is already unbundled from delivery rates and collected from customers in a gas supply charge.<sup>158</sup> Moreover, Staff maintains, the issue is complicated and is part of ongoing efforts in other forums. In its reply, Staff adds that not all of these costs are recovered solely from full service customers; as some are recovered from transportation

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<sup>157</sup> Con Edison Initial Brief, pp. 32-33.

<sup>158</sup> Staff Initial Brief, p. 31.

customers through gas balancing and virtual storage services.<sup>159</sup> Staff's position is supported by Niagara Mohawk and NYSEG.

Con Edison disagrees. It argues that there is no formal proceeding in which these issues are being considered generically and that the Natural Gas Reliability Advisory Council, where Staff believed the issue was being addressed, has never brought any issues to the Commission and is quite unlikely to do so.<sup>160</sup> It further argues that Staff's position now contradicts its July 31, 2001 comments supporting the review of reliability costs in this proceeding. The company also points to the November Order, which included these costs in the required functional unbundling. The fact that these costs are already unbundled should not matter, according to Con Edison, because the purpose here is both to unbundle and to functionalize costs to competitive and non-competitive services. A number of other cost categories that were previously unbundled were nevertheless functionalized and assigned to different services by Staff in this case, Con Edison submits, and the fact that reliability costs have been previously unbundled should not preclude their functionalization here.

Niagara Mohawk reviews the methodological differences between Con Edison and NYSEG, noting that the two utilities' costs and assets devoted to reliability differ significantly.<sup>161</sup> It concludes that, in light of these differences and considering market uncertainty and the absence of a clear definition of the supplier of last resort responsibility, it would be best to address these issues on a case-by-case basis in separate utility proceedings. In its reply brief, Niagara Mohawk suggests that the next phase of this proceeding, where utility-specific unbundled tariffs will be implemented, is the proper venue to deal with these costs. "The crucial step is to define Gas System Reliability as each utility's case is reviewed, rather than to

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<sup>159</sup> Staff Reply Brief, p. 20.

<sup>160</sup> Con Edison Initial Brief, p. 35; Con Edison Reply Brief, p. 17.

<sup>161</sup> Niagara Mohawk Initial Brief, pp. 22-23.

continually postpone the issue indefinitely due to its complexity."<sup>162</sup>

NYSEG argues that issues regarding reliability and gas rate design should be decided in the context of the phase 2 review contemplated in its gas rate plan approved by the Commission last fall. Under that plan, rates based on the unbundled costs of reliability as well as the costs unbundled and functionalized here would not be implemented until July 2004. NYSEG argues that under its rate plan, rate design issues and reliability cost recovery are intricately linked to rate moderation provisions, and making changes now, and again in a year, make little sense.

The ESCOs express no opinion on this issue.

Staff correctly observes that the issue of gas reliability costs is complicated, especially for NYSEG, with its separate gas service areas and gas cost mitigation plan. Con Edison, too, appears justified in its complaint that this issue has gone unresolved for too long and is nowhere pending a resolution. NYSEG's argument that these costs be considered in the context of its phase 2 process as approved by the Commission also appears reasonable.

One of the problems with the state of the record on these questions is the failure of the parties to join issue. Con Edison claims to have presented a complete and detailed analysis of reliability costs and their appropriate functionalization, but, instead of challenging the study, Staff simply recommends that the issue be delayed. NYSEG also submitted a study and Staff offered illustrative exhibits, but Staff never addressed the studies in brief, relying instead on its recommendation to put off a decision on these matters. Therefore, I find no joinder of issue on these questions, and what may be accomplished in this proceeding remains unclear.

It appears from the information provided by Con Edison that a portion of its reliability costs are attributable to ESCO customers (whom it serves as the provider of last resort by

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<sup>162</sup> Niagara Mohawk Reply Brief, p. 16. It appears that Niagara Mohawk ultimately supports Con Edison, at least in part.

providing back-up service in the event of an ESCO failure) and a portion are attributable to full service customers (e.g., the costs of maintaining daily flows despite freeze-offs, hurricanes, etc.). The ESCOs do not have to be prepared to provide POLR service, but it is reasonable to assume that they must make some effort to avoid supply interruptions due to factors such as freeze-offs and violent weather. In addition, the record supports a finding that at least some reliability costs are currently being recovered from ESCO customers. In my view, however, it is unlikely that current prices fairly apportion these costs between full service and delivery customers.

The only option available on this record is Con Edison's study, allocating 100% of reliability costs to the delivery function, but I do not believe that allocation is reasonable. A migrating gas commodity customer must expect that the ESCO will take those necessary precautions to keep the customer's gas flowing. The customer should not have to pay the utility as well for the same service. On the other hand, the utility alone is required to be ready to serve all customers in the event of an ESCO default, and reliability costs for this purpose can be substantial. All customers should be required to pay these last resort provider costs. Accordingly, Con Edison's complete functionalization of these costs to delivery is not reasonable and should not be adopted.

Nevertheless, and if it remains possible, I would recommend that this issue be resolved in the implementation phase of this proceeding and that Con Edison be directed to reexamine these costs and allocate them on a reasonable basis to both competitive and non-competitive gas supply. This might be accomplished together with the rerun of its ECOS study and the filing of proposed tariffs.

NYSEG's recommendation that reliability cost issues be addressed in phase 2 of its gas proceeding should be adopted, but its treatment of these costs should include a reasonable allocation to competitive supply.

12. Energy Services

Competitive energy services is one of the functional areas identified by the Commission in its November Order. Con Edison found no costs to put in this category and NYSEG found only a small amount.<sup>163</sup> Staff and the utilities agree that there is no need now to develop rates for these services, but Staff recommends that the utilities track these costs and report them in their next major rate proceeding.

NYSEG opposes Staff's tracking proposal, arguing that Staff has demonstrated no benefit from it that would outweigh the costs. It also notes that sales of such services/products inure to the benefit of all ratepayers.<sup>164</sup> It does not appear that Con Edison objected to Staff's recommendation.

NYSEG's arguments are unconvincing. If Staff can be faulted for failing to quantify the benefits of its recommendation, NYSEG can be faulted for failing to quantify the costs. In addition, NYSEG contends that the sale of these services/products benefits all ratepayers, but that cannot be known unless the revenues and costs are known--that is, tracked.

Staff's recommendation that these costs be tracked and reported with the utility's next major or rate proceeding should be adopted.

III. LOST REVENUE RECOVERY MECHANISM

The Commission stated in its March Order (p. 23):

Accordingly, we reject the proposals for partial or total disallowance of the recovery of revenue shortfalls where the original revenue allowances were designed to cover these costs. However, we reaffirm our statement that the utilities have an obligation to productively manage and reasonably mitigate their costs.

To recover any of the revenue allowances whose recovery might be precluded by migration, the Commission directed the utilities to develop a two-part mechanism. One part would recover revenues

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<sup>163</sup> Staff's Initial Brief, p. 23.

<sup>164</sup> NYSEG Reply Brief, p. 19.

from all customers, and the second would recover revenues only from utility full-service customers.<sup>165</sup> A conservative estimate of migration and lost revenues, net of short-run avoided costs, would form the basis for the charge to full service customers, a true-up for actual migration levels would be performed after the fact, and revenue shortfalls would be charged to all customers in a transition surcharge.

One of the more controversial aspects of this mechanism relates to the Commission's requirement that net migration or net lost revenues consider the actual level of revenues the utility receives as compared to the revenues allowed to cover utility costs in setting rates.<sup>166</sup> ". . . [I]t would not be reasonable to increase the utility's revenues if its customer base (or sales) after migration exceeded that on which rates were premised. If the utility has more sales or more customers than assumed when rates were set despite customer migration, all of the utility's costs would be recovered and none should be stranded."<sup>167</sup>

Con Edison proposed separate, prospective gas and electric Transition Adjustments based on a conservative estimate of migration, a calculation of lost revenues based on competitive prices, and an estimate of short-run avoided costs. The estimated revenue losses would be charged to all ratepayers. A true-up for actual migration levels and actual avoided costs would be performed after the fact, with the results charged or credited to all ratepayers.<sup>168</sup>

NYSEG's proposed electric mechanism is largely based on its most recently approved electric rate plan, which specifically provides for lost revenue recovery and anticipates the results of this proceeding. The mechanism includes a threshold level of lost revenues (\$4.0 million/year), beyond which lost revenues are

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<sup>165</sup> March Order, p. 24.

<sup>166</sup> November Order, p. 24, n. 24.

<sup>167</sup> Case 00-M-0504, Order on Rehearing and Clarification Petitions (issued May 30, 2002), p. 6.

<sup>168</sup> Con Edison Initial Brief, pp. 36-37.

recoverable from all ratepayers.<sup>169</sup> The mechanism does not contain two parts, nor does it collect any portion of the revenue shortfall only from full-service utility customers. NYSEG's gas mechanism consists of two parts, with conservatively estimated migration-related lost revenues collected in a charge to full service customers and any reconciling amounts, after the fact, charged to all customers.

Staff sees no reason to create a new mechanism for NYSEG electric revenues because an acceptable mechanism already exists in its rate plan.<sup>170</sup> It also tentatively concludes that the mechanism NYSEG proposed for gas complies with the Commission's orders.<sup>171</sup>

In contrast, Staff concludes that Con Edison's mechanism does not comply with the Commission's directives in many respects. Staff points out that the mechanism recovers all revenue shortfalls from all customers, rather than creating a two-part mechanism with some portion of costs collected only from full service customers. Staff notes that Con Edison petitioned for rehearing of this issue, and its position was rejected. Staff also alleges that Con Edison's mechanism improperly seeks recovery for past, present, and future migration, rather than only future migration as envisioned by the Commission. Staff further argues that the level of short-run avoided costs the company now estimates (0.09 mill/kWh) is well below that assumed in Phase 4 and 5 of Con Edison's retail access plan (1.0 mill/kWh non-demand; 0.5 mill/kWh demand), and adopting Con Edison's estimate would yield a higher level of lost revenue recovery than currently allowed.

Staff also challenges Con Edison's position from the perspective of cost (loss) causation. Instead of charging those

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<sup>169</sup> As a technical matter the revenues above \$4 million are charged to the Asset Sale Gain Account. The moneys in that account belong to the ratepayers.

<sup>170</sup> Staff Initial Brief, p.44.

<sup>171</sup> Staff did not completely sign off on NYSEG's sample calculation because it was based on the assumption that only the existing merchant function charge would be avoidable until its Phase 2 issues are decided in July 2004.

customers who continue to cause the company to incur costs for competitive services (its full service customers), Staff argues, Con Edison's mechanism in fact charges migrating customers for unrecovered competitive service costs.<sup>172</sup> While migrating customers may cause revenues to be lost, it is the remaining full service customers who continue to cause utility costs to be incurred. Accordingly, Staff claims, Con Edison is abandoning cost causation principles.

Staff notes also that the mechanisms envisioned by the Commission were designed to work much as the process for setting revenue requirements in a rate proceeding. If revenues are projected to decline (for example, on account of customer migration or a declining economy), rates are raised for remaining customers, who continue to purchase services from the utility.

The CPB also concludes that Con Edison's mechanism fails to comply with the Commission's directives.<sup>173</sup> CPB opposes Con Edison's claim that it should be compensated for all migration, even beyond that implicitly or explicitly reflected in current rates. It argues further that Con Edison provided neither an estimate of avoided costs nor any explanation of its efforts to productively manage and reasonably mitigate its costs. Until these are provided, CPB contends, no recovery of lost revenue should be permitted. MI also stresses the importance of strictly enforcing the requirement for productive management and reasonable mitigation before the recovery of lost revenues is permitted.<sup>174</sup>

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<sup>172</sup> Staff Reply Brief, p. 24.

<sup>173</sup> CPB Initial Brief, pp. 12-15.

<sup>174</sup> MI Initial Brief, pp. 6-8.

The CPB additionally expresses a number of concerns about NYSEG's proposals.<sup>175</sup> First, it argues that NYSEG's estimates of avoided costs contain no adequate explanation of the company's management and mitigation of costs. Second, CPB objects to the proposal to recover in this mechanism NYSEG's incremental costs of implementing competitive services, citing the Commission's decision that such costs have already been considered in the utilities' various rate plans.<sup>176</sup>

Con Edison maintains its mechanism complies with the Commission orders. It first contends that the Commission never mandated recovering a portion of lost revenues only from full-service customers.<sup>177</sup> Further, the company submits that its mechanism follows principles of cost causation, as the Commission directed, by charging retail access customers for the lost revenues they cause by migrating. The company challenges the Staff view, alleging it is Staff that violates the Commission order, by charging full service customers "100% of all lost revenues."<sup>178</sup> That approach, according to Con Edison, allows ESCO customers to avoid all costs associated with the utility's POLR responsibilities, contrary to the Commission's direction. Con Edison also notes that the Staff interpretation could produce anomalous results if estimates of future migration were overstated.

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<sup>175</sup> One of CPB's concerns appears to have been a misunderstanding. CPB argued that NYSEG estimated a 10% incremental increase in migration, an estimate that is more aggressive than intended by the Commission (CPB Initial Brief, p. 20). It appears, however, that NYSEG used the 10% migration level as the upward boundary in a study designed to calculate short-run avoided costs (NYSEG Initial Brief, p. 23). It was not estimating a 10% increase in migration.

<sup>176</sup> CPB Initial Brief, p. 21 citing March Order, p. 24, n. 5.

<sup>177</sup> The Commission said that the situation of a migrating customer "suggests" that a portion of revenue shortfalls "should" be collected from full service customers. Con Edison argues that this language is not directive (Con Edison Initial Brief, p. 38, citing March Order, p. 24).

<sup>178</sup> Id., p. 39.

Con Edison also disputes Staff's understanding that the mechanism should be limited to net incremental migration. The company's base rates, it argues, are not based on any level of customer migration, as demonstrated by the existence of a mechanism to recover lost revenues in each of its phase 4 and 5 retail access plans. In addition, the company denies any intention to recover past or present lost revenues and states that its intent is to recover only those lost revenues related to the prices set here.

Con Edison claims further that its earnings levels are irrelevant to this proceeding. In its view, it is not subject to the Commission's order limiting lost revenue recovery based on a review of the company's allowed and achieved revenues for the company's current rates are not premised on an agreed-upon sales level.<sup>179</sup> Further, denying a utility the recovery of lost revenues based on the utility's earnings levels would eliminate any incentive the utility had to foster retail competition. In addition, Con Edison claims, if the Commission disallows recovery of lost revenues because the utility's earnings are too high, it ". . . would impair the ability of the Company to achieve the benefit of the bargain reached in its current rate plans . . .".<sup>180</sup> Regarding the incentive to mitigate its costs, Con Edison states:

Utilities could hardly be expected to reduce costs, which cost cuts ultimately inure fully to the benefit of customers, if such cost cuts would require utilities to forgo recovery of an equal amount of lost revenues.<sup>181</sup>

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<sup>179</sup> Con Edison Initial Brief, p. 43. Staff contradicts this claim, alleging that Con Edison and Staff have agreed on a sales forecast as the basis for the company's existing rates. Staff further argues that Con Edison's existing sales level is so far above the ratemaking level that a lost revenue recovery mechanism is probably not needed for the company (Staff Reply Brief, p. 27).

<sup>180</sup> Con Edison Initial Brief, p. 45.

<sup>181</sup> Id., p. 44.

Finally, Con Edison denies submitting as part of its draft tariff either an estimate of avoided costs or an estimate of future migration; accordingly, it says, the parties' criticisms regarding such estimates lacks any basis.

In response to CPB's claims, NYSEG argues that the two-tiered mechanism discussed by the Commission does not apply to its electric services.<sup>182</sup> Further, NYSEG defends its short-run avoided cost calculation, suggesting that it meets the requirement of productive management and reasonable mitigation of costs and asserting there is no record evidence to the contrary. Finally, NYSEG denies any intent to recover in its gas revenue recovery mechanism the incremental cost of implementing unbundled rates, noting that the recovery of such costs are addressed in its recent gas settlement.

In my view, the Commission defined the parameters of the lost revenue recovery mechanism in an effort to be fair to all parties. From the utility's perspective, it is a true-up mechanism, designed to ensure that revenues are not lost to the utility in the event of poor forecasts. From the ratepayers' perspective, the mechanism focuses on revenues that are truly lost; that is, recovery is allowed only if actual revenues are less than the revenues allowed by the Commission to reimburse the utility for its costs. As the Commission stated, it would not be reasonable to allow the utility to collect lost revenues, if its actual revenues exceeded those allowed in base rates. In other words, by any reasonable definition of regulation, a utility has no lost revenues if its actual revenues after migration still exceed the revenues it was originally allowed to recover its costs.

Con Edison's arguments that this approach is unreasonable or cannot be applied to its situation are unpersuasive. First, Con Edison correctly observes that, as a general matter, it would be contrary to the intention of the Commission to deny the recovery of lost revenues--and I agree. What the company fails to appreciate is that it would be equally

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<sup>182</sup> NYSEG Reply Brief, pp. 40-42.

unfair and unreasonable to allow the utility to recover lost revenues when there are none. The company's position assumes that there will be net lost revenues for every migrating customer, ignoring the potential for new customers (or returning customers) to make up the revenues previously "lost." In fact, Con Edison's approach would allow ratepayers to be charged higher rates for lost revenues regardless of the level of the utility's actual revenues or its actual financial performance. An example shows how unfair such a result could be. If a utility had an equity return level of 35%, for example,<sup>183</sup> the Con Edison approach would require ratepayers to pay the utility even more for what must be considered under those earning circumstances to be "phantom" lost revenues. This is precisely why the Commission found it unreasonable to allow the recoupment of lost revenues without first considering the level of revenues actually received by the utility.

Nor is Con Edison convincing in arguing that the Commission's approach somehow denies the company the benefits of its rate settlement or presents disincentives for cost minimization. The mechanism established by the Commission is consistent with longstanding ratemaking principles. Staff correctly observes that migration-related lost revenues are being treated just as a forecast reduction in revenues from any other source (such as a downturn in the economy) are treated in a rate proceeding. Under normal ratemaking principles, total forecasted revenues would not include "lost revenues" and, by definition, base rates would include sufficient revenues to cover all prudent costs. Because, in the ordinary case, the utility would be at risk for the accuracy of the migration forecasts, the Commission here determined that there would be a true-up to actual net

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<sup>183</sup> Earned returns in this range are certainly possible, as reflected in Case 01-E-0359, NYSEG's Electric Price Protection Plan, Order Clarifying Data Required (issued April 25, 2001), p. 4.

migration levels.<sup>184</sup> This spares the utility a significant portion of the risk that revenues will not be sufficient to cover costs.

Further, the mechanism works in a manner analogous to the Commission's historical treatment of utility requests to defer material levels of costs that were not anticipated or otherwise provided for in setting rates. Based on its assertion that revenues lost to migration are not reflected in its rates, Con Edison is actually arguing that it will have unrecovered costs due to migration. An application to have such costs added to future rates (i.e., deferred for later recovery) would be granted by the Commission only if certain conditions were met. First, the amounts involved would have to be material in comparison to the company's earnings. The Commission could have incorporated a similar threshold in the recovery mechanism here, but it did not do so. Accordingly, lost revenue recovery is permitted for every dollar of actual revenue shortfall, again reducing the company's financial risk compared to the provisions the Commission could have imposed.

An additional deferral condition concerns the level of the company's actual earnings. Deferrals will not generally be granted if the company is overearning, i.e., if its actual earnings in the historical period exceed the equity return allowed for the period. If a utility earns its allowed return, by definition it covers its cost of capital and meets reasonable shareholder expectations. Under such circumstances, a deferral would not be permitted. As the Commission recently stated:

The third test in examining deferred accounting requests relates to a utility's earnings position. The Commission has traditionally denied deferred accounting requests if the utility has sufficient earnings to absorb the costs. . . . Specifically, the company should be permitted

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<sup>184</sup> In my view, the Commission meant by "net migration" the total number of migrating customers less the number of ESCO customers who returned to the utility and less the number of new utility customers beyond the level of customer growth that was assumed in setting rates.

to defer SIR costs up to its authorized return on equity (ROE) of 10.3%. Earnings above 10.3% should be used to offset the company's SIR costs.<sup>185</sup>

Therefore, the Commission could have limited the recovery of lost revenues to situations where a utility was not earning its allowed return, but it chose not to do so. This provides another benefit to the utilities. For example, a utility could be earning in excess of its allowed return despite revenue shortfalls as a result of productive cost management, productivity gains, or reasonable cost mitigation. In such a case, the Commission could have decided that, because the utility was earning its allowed return, there would be no need for lost revenue recovery. The Commission's mechanism, however, does not take that position and it allows revenue recovery whether or not the allowed return is being earned. Therefore, the Commission's mechanism, which allows lost revenues to be recovered only when overall revenues are, in fact, below the forecast level, is both consistent with traditional ratemaking principles and more favorable to the utilities in a number of ways than would be a strict application of those principles.

The only situation where the Commission's mechanism denies the utility the recovery of lost revenues above and beyond base rates is when there are in fact no lost revenues. Allowing the utilities to add to their profit margins under such circumstances would not be just and reasonable to the ratepayers and would be affirmatively harmful to economic development within the State.

Con Edison argues, however, that comparing projected revenue levels on which rates are based with its actual revenues is impossible because its rates were based on a settlement that did not include a detailed revenue requirement. This argument is also unpersuasive. First, Staff contends that a revenue forecast on which rates are based has been explicitly agreed upon, and the company has not contradicted this claim. Second, this concern

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<sup>185</sup> Case 01-G-1821, Central Hudson Petition to Defer Environmental Site Investigation and Remediation Costs, Memorandum Order (issued October 25, 2002), p. 5.

was addressed by the Commission when Con Edison raised this argument seeking rehearing of the March Order. The Commission noted the concern but expressed its confidence "that reasonable estimates can be made on individual utility bases, even if the identical methodology may not be appropriate for all."<sup>186</sup>

Finally, if a revenue forecast were not available or could not be calculated from a rate allowance, the utility's earning position could be used as noted above regarding deferrals. Accordingly, I find no merit in Con Edison's contention that an acceptable calculation of actual lost revenues cannot be made due to the structure of its rate plan.

In addition, I find Con Edison's position regarding its incentives to reduce costs somewhat curious. Con Edison suggests that utilities should not be expected to reduce costs unless they are allowed to recover an equal amount of lost revenues after the costs have been eliminated.<sup>187</sup> As I understand its statement, a utility would not reduce its costs unless it were also allowed to continue recovering revenues designed to cover the very costs that no longer exist. It would be difficult, in my view, to characterize such an approach as productive or prudent management or to assume that it would rise to the level of reasonable cost mitigation.

Notwithstanding all of the foregoing, however, and being sensitive to the utilities' demands that denying all lost revenue recovery (where revenues are not lost) would amount to denying them the benefit of their negotiated rate plans,<sup>188</sup> I would recommend an additional condition be added to the Commission's description of the limitation on the application of the recovery mechanism. Recovery of net migration-lost revenues (as above defined) should be permitted unless both of the

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<sup>186</sup> Case 00-M-0504, Order on Rehearing and Clarification Petitions (issued May 30, 2002), p.6.

<sup>187</sup> Con Edison Initial Brief, p. 44.

<sup>188</sup> The utilities who make this argument are actually assuming that a benefit of the rate plan is a regulatory guarantee that they will lose no customers and suffer no loss of revenues during its term.

following are true: (a) actual revenues are higher than allowed revenues; and (b) the company's actual earnings are at or above its earnings sharing threshold. This additional limitation would allow the utilities to recover lost revenues and add to their profitability well above their allowed returns even if there were no revenues lost. The utilities' returns would be affected only where their earned returns are being shared with ratepayers.<sup>189</sup>

Another questionable aspect of Con Edison's proposal is the absence of a two-tier mechanism. The Commission found that competition would be assisted if a portion of any lost revenues were recovered from full service utility customers and a portion were recovered from all customers.<sup>190</sup> Based on the flexibility allowed the utilities in designing the mechanism, I find neither Con Edison's filing nor NYSEG's to violate the Commission's orders. But in light of the Commission's discussions of the mechanism, only NYSEG's proposal is acceptable.

One of the basic reasons the Commission adopted a two-part approach was its observation that a migrating customer must be able to avoid the utility's charges for services no longer taken, but should not be able to avoid the charges for POLR service. The mechanism that flows from NYSEG's electric rate plan accomplishes a similar result. Migrating customers will avoid paying for the first \$4 million of lost revenues, but thereafter will shoulder the same level of costs as other customers. While this is not exactly the result the Commission described, it is sufficiently similar, in my view, to be acceptable. NYSEG's gas mechanism which is based on a two-tier approach is also acceptable, as Staff explained.

Con Edison's mechanism, in contrast, is unacceptable in this regard and its arguments in support of its position are unpersuasive. Unlike NYSEG, Con Edison does not have a rate plan containing a lost revenue recovery mechanism. The mechanism

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<sup>189</sup> Above Con Edison's earnings sharing threshold, the company shares incremental earnings 65% to ratepayers and 35% to the company.

<sup>190</sup> Case 00-M-0504, Order on Rehearing and Clarification Petitions (issued May 30, 2002), p. 5; March Order, p. 24.

currently in place for Con Edison expires this spring with the conclusion of phase 5 of its retail access plan. Therefore, there is no constraint on the terms of the Con Edison mechanism, and it should include the two-tier mechanism preferred by the Commission unless it can propose an equivalent approach that also meets the Commission's goals. The company's proposal, however, falls short of this mark.<sup>191</sup>

Con Edison argues that it is simply following principles of cost causation by charging migrating customers for revenue losses they cause. But Staff correctly notes that this is, in fact, a loss causation principle--Con Edison is charging customers who do not take a service for the ongoing costs of providing a service to other customers remaining with the utility. In my opinion, this is the opposite of the result intended by the Commission.

Con Edison correctly notes, however, that if estimated migration levels are set too high (at or above actual migration), ESCO customers would avoid paying any portion of the utility's POLR costs, or might actually receive a credit in the true-up. This is a legitimate concern, going to the Commission's definition of a "conservative" estimate of future migration. I therefore recommend that a reasonable estimate of future migration be produced, but that, when implementing the cost recovery mechanism for full service customers, the rate impact be reduced by one-third. This should render the estimates adequately conservative and should greatly reduce the possibility of anomalous results.

As adjusted above, the two-tier mechanism discussed by the Commission should be required for Con Edison gas and electric service.

It seems most reasonable to decide the reasonableness of estimated future migration rates and estimates of short-run

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<sup>191</sup> Staff's arguments that the company is seeking past, present, and future migration through this mechanism appear to be incorrect. The company is seeking lost revenue recovery from those customers who will be paying the rates established here.

avoided costs in the context of individual utility dockets (the next phase of this process). When true-ups are undertaken, actual levels of migration and actual avoided costs can be calculated and a determination can be made at that time concerning the utility's effective management and reasonable mitigation of costs.

A final point should be noted. All of the utilities express concerns that the introduction of competition, mainly for commodity, will negatively affect their earnings. The actual results for the first four years of retail competition for Con Edison and NYSEG do not support that concern. Based on the "Financial Statistics of the Major Investor-Owned Utilities in New York State" published by the Department of Public Service, the average, company-wide return for 1998-2001 for Con Edison was 13.3% and for NYSEG was 26.2%. While the utilities' concerns are not baseless, it appears that Con Edison and NYSEG have experienced no lost revenues and have been able to more than cover all of their costs in base rate, notwithstanding the introduction of retail competition. If customer migration levels for these companies ever grow beyond single digits, the results might not be the same, but for the short term it appears that utility earnings erosion due to current levels of customer migration is not a significant concern.

#### IV. IMPLEMENTATION ISSUES

In implementing competitive prices for the utilities a number of matters should first be considered. Foremost among those are the potential rate impacts and competitive market impacts that might arise from substituting the prices calculated here for the existing backout credits.

One might assume that replacing a backout credit with a higher price would both stimulate migration and increase lost revenues and, thereby, utility rates. Conversely, replacing the backout credit with a lower price might be assumed to discourage migration and reduce lost revenues. But actual experience across the State with different levels of backout credits suggests that the factors encouraging migration go well beyond the level of the

backout credit. For example, all utilities except Con Edison are now operating under 4 mill/2 mill backout credits, yet customer migration for Orange and Rockland Utilities is at 21.8% while customer migration for NYSEG is 3.2%. With one-half the level of these backout credits, Con Edison migration is at 5%.<sup>192</sup> These statistics strongly suggest that factors other than the level of backout credits have significant impacts on the extent of customer migration. Staff estimates an overall positive impact on Con Edison's and an overall negative impact on NYSEG's retail access program based on the competitive prices calculated here, but states ". . . it cannot be determined whether these effects will be the primary drivers of success of retail access in either franchise."<sup>193</sup>

From the consumer's perspective, higher competitive prices will directly benefit ESCO customers and ESCOs, but could negatively affect utility full service customers. To the extent the new prices are close to current backouts, the effects should be de minimis. Further, the impact on full service customers will be de minimis if the utilities continue to earn above their earnings sharing thresholds. Based on the assumption that earnings at that level reflect total revenues well above allowed revenues, there would be no lost revenues to recover and there would be no impact on utility rates.

This appears to be the case for both NYSEG and Con Edison. For NYSEG electric, the lost revenues associated with its current level of migration can be subsumed in the \$4 million deadband provided for in its rate proceeding. In addition, NYSEG's earned electric return through September 30, 2002 is 16.4%, above the 15.5% earnings sharing threshold. This suggests that NYSEG's electric rates are set at a level that fully compensates the utility for its costs at its current level of migration. Accordingly, no lost revenue recovery is required beyond that provided in its rate plan, except for incremental migration.

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<sup>192</sup> Staff Initial Brief, p. 33.

<sup>193</sup> Id., p. 36.

In addition, NYSEG's ongoing electric rate plan and the contracts entered into by customers and ESCOs in reliance on the backout credits included in that plan, suggest that the Commission should use caution in now implementing significantly lower competitive prices. The NYSEG plan contemplates resetting rates on January 1, 2005, and it seems most fair to all parties to await that resetting to implement competitive prices.<sup>194</sup> Whether there will be a need for the lost revenue recovery mechanism or whether it should be limited to incremental migration are questions that can be revisited at that time.

The NYSEG gas situation is unique. Its newest rate plan includes a bill mitigation plan designed to phase in the impact of moving to a market-based gas supply charge.<sup>195</sup> While the parties agree that the company's merchant function charge (MFC) should not be changed until July 2004, both Staff and CPB on brief offer alternative suggestions to address the newly calculated competitive prices prior to July 2004.<sup>196</sup> Staff recommends that any increment above the current MFC be applied as a credit to delivery charges. CPB urges that the company be required to submit a proposal to deal with the rates calculated here.

NYSEG opposes both proposals. It argues that any implementation now of competitive prices above the MFC will simply exacerbate amounts to be recovered under its bill mitigation plan. Further, implementing Staff's recommendation could result in negative delivery charges during the interim.

NYSEG's arguments on this issue are convincing, and it is therefore recommended that the existing MFC remain in effect to July 2004 and that the competitive prices calculated here not be implemented until that time. Further, all but a small portion of the current MFC reflects short-run avoided costs, suggesting

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<sup>194</sup> Because the embedded prices examined in this case may be too dated for use in 2005, the Commission should consider requiring the filing of an updated study prior to the implementation of the new rates.

<sup>195</sup> NYSEG Reply Brief, p. 39.

<sup>196</sup> Staff Initial Brief, p. 41; CPB Initial Brief, p. 23.

that lost revenues will be quite small over the next year. In light of NYSEG's acceptable gas revenue recovery mechanism (adjusted by my recommendations above), I would recommend that the mechanism be implemented as part of the phase 2 proceedings in its gas case.

A lost revenue recovery mechanism also appears unnecessary at this time for Con Edison gas or electric operations. Through September 2002, the company was earning 13.05% on electric operations, with earnings sharing beginning at 11.75%, and 12.87% for gas operations, with earnings sharing at 11.5%. Unless migration levels increase substantially, it appears that Con Edison's base rates will fully recover its costs. Accordingly, any revenue recovery mechanism implemented for Con Edison now should be based only on incremental migration, i.e., customer migration above the current 5% level, because current rates more than cover all costs even though 5% of its customers are now purchasing from ESCOs.

Because Con Edison is about to embark on phase 6 of its retail access program and because the recommended calculation of the competitive prices for Con Edison is expected to produce figures close to current backouts, it is recommended that these prices be implemented for Con Edison as soon as possible. Whether a lost revenue recovery mechanism can be justified and whether it should be limited to future incremental migration in light of the current levels of Con Edison's revenues can be determined in the next phase.

#### V. CONCLUSIONS

Based on the above, I recommend the following:

1. NYSEG should be directed to recalculate its competitive rates (ECOS study) as recommended above and implement the gas rates and recovery mechanism in July 2004 and the electric rates and recovery mechanism (if needed) in January 2005.

2. Con Edison should be directed to recalculate its competitive rates (ECOS study) as recommended above and to implement the gas and electric rates and, if needed, a revenue recovery mechanism as soon as reasonably possible.

March 24, 2003  
JES:yrs

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