



Couch White, LLP  
540 Broadway  
P.O. Box 22222  
Albany, New York 12201-2222  
(518) 426-4600  
Telecopier: (518) 426-0376

Robert M. Loughney  
Partner  
Direct Dial: (518) 320-3404  
Direct Telecopier: (518) 320-3495  
email: rloughney@couchwhite.com

Brief  
05-S-1376  
OEE  
OHADR  
OGC

August 7, 2006

**VIA HAND DELIVERY**

Hon. Jaclyn Brillig  
Secretary  
State of New York Public  
Service Commission  
Three Empire State Plaza  
Albany, New York 12223-1350

Re: Case 05-S-1376 - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service

Dear Secretary Brillig:

Pursuant to the Commission's regulations and the procedures adopted in the above-referenced proceeding, please find enclosed twenty-five (25) copies of the Post-Hearing Brief in Support of Joint Proposal submitted on behalf of the City of New York.

Please have the extra copies of the Post-Hearing Brief time-stamped and returned to our messenger. Please call me if you have any questions.

Very truly yours,

COUCH WHITE, LLP

*Robert M. Loughney / MHB*

Robert M. Loughney

RML/MHB/slg  
Enclosures

cc: ALJ Rafael A. Epstein (via Hand Delivery; w/enc.)  
Active Parties List (via e-mail and U.S. Mail; w/enc.)

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PUBLIC SERVICE COMMISSION

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Proceeding on Motion of the Commission as to  
the Rates, Charges, Rules and Regulations of  
Consolidated Edison Company of New York,  
Inc. for Steam Service

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Case 05-S-1376

POST-HEARING BRIEF  
OF  
THE CITY OF NEW YORK

Dated: August 7, 2006

COUCH WHITE, LLP  
540 BROADWAY  
P.O. BOX 22222  
ALBANY, NEW YORK 12201  
(518) 426-4600

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## PRELIMINARY STATEMENT

In accordance with the schedule established by Administrative Law Judge Rafael A. Epstein ("ALJ Epstein") in Case 05-S-1376, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service, the City of New York (the "City"), one of the largest customers on the Consolidated Edison Company of New York, Inc. ("Con Edison") steam system, hereby submits its Post-Hearing Brief in Support of the Joint Proposal filed with the State of New York Public Service Commission ("Commission") on June 2, 2006 in this proceeding.<sup>1</sup> For the reasons set forth herein, the City urges the Commission to adopt the Joint Proposal, to which the City is a signatory, without modification.

The Joint Proposal that was filed in this proceeding was the result of extensive settlement negotiations in March, April, May and June, 2006. The Joint Proposal advances a comprehensive resolution of all of the outstanding issues in this proceeding and is supported by the vast majority of the active parties, including all of the parties representing Con Edison steam customers.<sup>2</sup> The Joint Proposal reflects numerous, interrelated compromises and

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<sup>1</sup> Citations to the Joint Proposal are preceded by the notation "JP." Citations to the stenographic minutes and exhibits in this proceeding are preceded by the notations "S.M." and "Ex.," respectively. Citations to the initial statements in support or opposition to the Joint Proposal are preceded by the party's name, as abbreviated herein, and "Initial Statement" (e.g., City Initial Statement, p. \_\_).

<sup>2</sup> The Joint Proposal has been executed and is supported by the following eight parties (collectively, the "Signatory Parties"): Con Edison; Department of Public Service Staff ("Staff"); the City; Consumer Power Advocates ("CPA"); ConsumerPowerline; the E Cubed

concessions by the Signatory Parties that, collectively, address all of the substantive issues in this proceeding and resolve them in a fair and reasonable manner.

On June 16, 2006, seven parties, including the City, filed statements supporting the Joint Proposal.<sup>3</sup> On June 30, 2006, Con Edison, Staff and the City filed reply statements. On July 12, 2006, an evidentiary hearing was held before ALJ Epstein. Despite the resounding and widespread support for the Joint Proposal, two parties – the County of Westchester (“County”) and TransGas Energy Systems LLC (“TGE”) (collectively, the “Opponents”) – filed statements or testimony opposing select provisions of the Joint Proposal. Specifically, the County is opposed to the manner in which the Joint Proposal allocates the costs of the East River Repowering Project (“ERRP”) between Con Edison’s electric and steam departments. The County also is opposed to the provisions of the Joint Proposal that address the process for examining future steam supply options, as is TGE. However, as demonstrated herein: (a) the Joint Proposal is in the public interest and should be adopted without modification by the Commission; and (b) the objections of the County and TGE to the Joint Proposal are without merit and should be rejected.

The City’s Post-Hearing Brief is organized into three sections. In Point I, the City demonstrates why the Joint Proposal is in the public interest and should be adopted in its entirety. In Point II, the City refutes the County’s objections to the Joint Proposal’s provisions allocating the costs of the ERRP. In Point III, the City justifies the Joint

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Company, LLC; New York Energy Consumers Council, Inc. (“NYECC”); and Pace Energy Project (“Pace”).

<sup>3</sup> The other parties filing statements supporting the Joint Proposal were: Con Edison, Staff, CPA, ConsumerPowerline, NYECC and Pace.

Proposal's provisions regarding the examination of future steam resources and responds to the objections of the County and TGE with respect thereto.

## ARGUMENT

### POINT I

#### **THE JOINT PROPOSAL IS IN THE PUBLIC INTEREST AND SHOULD BE ADOPTED IN ITS ENTIRETY IN THIS PROCEEDING**

The City urges the Commission to adopt the Joint Proposal, without modification, in this proceeding. For numerous reasons, adoption of the Joint Proposal is in the public interest.

In evaluating proposed multi-year rate settlements, the Commission traditionally considers the following factors:

- (i) the settlement's consistency with law and with the regulatory, economic, social and environmental policies of the Commission and the State;
- (ii) whether the result compares favorably with the likely result of full litigation and is within the range of reasonable outcomes;
- (iii) whether the settlement strikes a fair balance among the interests of ratepayers and investors and the long-term soundness of the utility;
- (iv) the existence of a rational basis for the decision;
- (v) the completeness of the record; and
- (vi) whether the settlement is contested.<sup>4</sup>

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<sup>4</sup> Case 90-M-0255, Proceeding on Motion of the Commission Concerning its Procedures for Settlement and Stipulation Agreements, filed in C 11175, and Case 92-M-0138, In the Matter of the Rules and Regulations of the Public Service Commission Contained in 16 NYCRR, Chapter I, Rules of Procedures – Proposed Amendments to Subchapter A, General, Part 2, Hearings and Rehearings by the Addition of a New Section 2.6, Settlement Procedures, filed in C 11175, Opinion No. 92-2, Opinion, Order and Resolution Adopting Settlement Procedures and Guidelines (issued March 24, 1992) at 30.

The City submits that when these factors are examined in the context of this proceeding, the inevitable conclusion is that the Joint Proposal is in the public interest and should be adopted.

Initially, there can be no real dispute that the Joint Proposal is consistent with the law, as well as the regulatory, economic, social and environmental policies of the Commission and the State. Indeed, there has been no real claim to the contrary. The Joint Proposal advances a multi-year resolution to the steam rate case filed by Con Edison, and is consistent with similar rate plans advanced, and adopted by the Commission, in other utility rate proceedings (including Con Edison's last steam rate proceeding). The Joint Proposal provides for rate stability by avoiding large rate increases for a two-year period,<sup>5</sup> and also implements a series of economic development initiatives that include potential revenue adjustments if Con Edison does not meet established performance metrics. Moreover, as detailed in Point II, *infra*, the proposed resolution of cost allocation issues related to the ERRP is wholly consistent with Commission policy and precedent.

The Joint Proposal also "compares favorably with the likely result of full litigation and is within the range of reasonable outcomes." Many parties in this proceeding – other than Con Edison – contested the need for any base rate increase. For example, City witness Dr. Rosenberg testified that depreciation costs were overstated and the revenue requirement needed to be reduced significantly. (See S.M. 170-71.) Staff's litigated case recommended no change to base rates in the first rate year. (See S.M. 171.) In light of the disparate positions advanced on revenue requirement issues, the Joint Proposal compares

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<sup>5</sup> The Joint Proposal has a two-year term – Rate Year 1 ("RY1") runs from October 1, 2006 through September 30, 2007, and Rate Year 2 ("RY2") runs from October 1, 2007 through September 30, 2008.

favorably with a potential litigated result. Moreover, inasmuch as the Joint Proposal maintains the Commission's longstanding methodology for allocating ERRP costs, its provisions clearly are consistent with the likely result of litigation on that issue.

In terms of "whether the settlement strikes a fair balance among the interests of ratepayers and investors and the long-term soundness of the utility," the Commission need only examine the identities of the Signatory Parties to confirm that this criteria has been satisfied. In terms of ratepayer interests, it is noteworthy that the parties representing Con Edison's steam customers all support the Joint Proposal, as does Staff. Con Edison's support of the Joint Proposal lends strong credence that the settlement also is in the best interests of the utility's investors and long-term business prospects. Thus, the Joint Proposal strikes a fair balance between customers and utility shareholders, fostering the goal of operating a safe and reliable steam system at the lowest practical cost, while providing the utility an opportunity to earn a reasonable return.

Additionally, there is a rational basis for adoption of the Joint Proposal, and the record in this proceeding now is or soon can be considered "complete" under any reasonable standard. Following Con Edison's rate case filing, the parties engaged in extensive discovery and many filed responsive and/or rebuttal testimony. Thereafter, the parties participated in lengthy settlement negotiations, which culminated in the Joint Proposal. Proponents and opponents of the Joint Proposal were allowed to make two pre-hearing submissions advancing their positions. Thereafter, an evidentiary hearing was conducted, at which all parties were accorded the opportunity to conduct cross-examination and further develop the record. The procedural schedule herein permits parties – both for

and against the Joint Proposal – to submit initial and reply post-hearing briefs to the Commission. Thus, the record addresses thoroughly the primary issues in this proceeding, including revenue requirement and rate design issues. Accordingly, there has been more than ample opportunity to develop fully the record on any and all contested issues. The City asserts that record developed in support of the Joint Proposal is overwhelming. (See, e.g., S.M. 169-79, detailing, from the City's perspective, some of the important provisions of the Joint Proposal making its adoption in the public interest.)

The final factor considered typically by the Commission in evaluating multi-year rate settlements is whether the settlement is contested. In this proceeding, only two parties – the County and TGE – are opposed to the Joint Proposal. Significantly, the scope of those parties' opposition is very narrow. Moreover, it warrants notice that neither of the Opponents represents Con Edison steam customers, nor does either party currently provide steam to the utility, or have a contract to do so in the future. On the other hand, the Signatory Parties are comprised of Con Edison, Staff and six other parties, including the City, that represent a broad spectrum of steam customers and environmental and other interests that are dependant on the terms of the utility's steam tariffs for their business interests. The Signatory Parties possess diverse – and often adverse – interests, yet they have managed to put aside their differences in this proceeding to support a Joint Proposal that is in the public interest.

For all the reasons set forth herein, the City urges the Commission to adopt the Joint Proposal in its entirety in this proceeding.

## POINT II

### **THE COST ALLOCATION OF THE ERRP IS IN THE PUBLIC INTEREST AND SHOULD BE ADOPTED**

It is uncontroverted that the ERRP cost allocation methodology advanced in the Joint Proposal is the same incremental cost approach approved by the Commission in Con Edison's last steam rate proceeding. Nevertheless, the County opposes the Joint Proposal's allocation of ERRP costs because it allegedly provides a subsidy to the steam department in contravention of prior Commission precedent and to the disadvantage of electric customers. Contrary to the County's assertions, however, the ERRP cost allocation methodology advanced in the Joint Proposal is consistent with Commission precedent, establishes an equitable allocation of costs between electric and steam customers, and is in the public interest.

The Joint Proposal provides that for RY1, carrying charges on the ERRP (*i.e.*, return on investment, depreciation, and property and other taxes) will continue to be allocated and recovered through the steam fuel adjustment clause in the manner approved by the Commission in Con Edison's last steam proceeding rate plan, except that the total carrying charges on capital costs allocable to steam shall be based on actual total capital costs (including AFUDC) not to exceed \$788.3 million.<sup>6</sup> The Joint Proposal also provides that, commencing in RY2, the steam department's share of ERRP carrying charges will be

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<sup>6</sup> Ex. 1 at 9; see also, Case 03-S-1672, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service, Order Adopting the Terms of a Joint Proposal (issued September 27, 2004) ("2004 Steam Rate Order") at 4.

transferred into base rates on an earning-neutral basis, subject to any amount disallowed by the Commission based on its review of the construction and related costs of the ERRP. (Ex. 1 at 9.) Importantly, the methodology advanced in the Joint Proposal to allocate costs between the electric and steam departments is the same approach approved by the Commission in the last steam proceeding, over the same objections by the County.<sup>7</sup>

In testimony opposing the Joint Proposal,<sup>8</sup> the County raises two objections to the ERRP cost allocation: (a) the cost of the ERRP has substantially exceeded its original estimate by approximately \$394 million and the majority of the increase (approximately \$78.5 million per year) is being borne by electric customers as rent (S.M. 339-40); and (b) the electric department pays a disproportionate share of the ERRP's operating costs, including fuel, and, therefore, the costs allocated to the electric department should not exceed the value of the energy produced by the plant. (S.M. 339-40, 345.) For the reasons set forth below, the County's objections are without merit and should be rejected.

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<sup>7</sup> Unlike the City and other Signatory Parties, which are electric and steam customers of Con Edison, the County only is an electric customer of the utility. Consequently, the County's motivation for attempting to shift costs away from the electric department and onto the steam department is transparent.

<sup>8</sup> The County submitted testimony and exhibits from Frank W. Radigan.

**A. The Joint Proposal's ERRP Cost Allocation Methodology Is Consistent With Commission Policy and Precedent**

It has been over a quarter century since the Commission first approved the “incremental cost” allocation methodology between Con Edison’s electric and steam departments.<sup>9</sup> In its first case addressing incremental costs, the Commission considered the electric department’s growing demand for the electricity produced by the utility’s combined steam/electric generating stations, in addition to the potential for a destructive, massive exodus from the steam system if it was over-allocated costs. In recognizing what could become a disastrous situation, the Commission approved the allocation of all joint electric and steam production costs to the electric department except those related to the incremental cost of producing steam.<sup>10</sup> More recently, the Commission extended the incremental cost allocation in Case 99-S-1621, over the County’s objections, ruling that “the long-standing allocation of cost between electric and steam has been reasonable.”<sup>11</sup>

In Case 03-S-1672, the Company’s last steam rate proceeding, the County again raised objections to the manner in which the Joint Proposal in that proceeding allocated ERRP costs between Con Edison’s electric and steam departments. The objections raised by the County in Case 03-S-1672 are nearly identical to those it raises here, i.e., the ERRP cost

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<sup>9</sup> See Case 27276, Consolidated Edison Company of New York, Inc. – Steam Rates, Opinion No. 78-27 (issued November 14, 1978).

<sup>10</sup> Id., Opinion No. 78-27, 18 NYPSC 1770.

<sup>11</sup> Case 99-S-1621, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service, Opinion No. 00-15, Opinion and Order Adopting Terms of Settlement (issued December 1, 2000) at 21.

allocation allegedly subsidizes the steam department at the expense of the electric department. In Case 03-S-1672, the Commission rejected the County's arguments:

In this case, Westchester claims a "more proportionate" allocation of the East River Repowering Project costs is warranted because of the specific circumstances related to this facility. Contrary to Westchester's allegations, we find that the ERRP was selected and is being constructed for the substantial benefits it will provide for both the electric and steam systems. Westchester is incorrect to assert that the facility's primary or exclusive benefits only extend to the steam system.

The electric system will receive substantial benefits from this in-City electric plant because it will serve load pockets on Manhattan's East Side and elsewhere in the borough. Consequently, we find that upon its completion and commencement of operations, the ERRP will become an essential component of both the electric and steam systems.<sup>12</sup>

In this proceeding, the County has argued that the promised value of the ERRP to electric customers has not materialized and, therefore, more costs should be allocated to Con Edison's steam department. (S.M. 345.)<sup>13</sup> In Case 03-S-1672, the Commission considered and rejected a virtually identical argument, recognizing specifically that the electric department's share of the ERRP costs might exceed the market value of electricity generated at the plant:

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<sup>12</sup> Case 03-S-1672, supra, 2004 Steam Rate Order at 26-27.

<sup>13</sup> The County argues that the ERRP allocation methodology is unfair because it results in the electric department paying fuel costs that exceeds the market value of the electricity produced by the ERRP. (S.M. 339.) Because of this alleged "inequity," the County advocates that steam rates be increased by \$37 million. (Id.) However, the ERRP cost allocation here is the same as the one approved in the 2004 Steam Rate Order, and based on a methodology that "fairly distributes the cost of ERRP based on principles of cost causation."

While the prevailing market prices for electricity in New York City do not match, or cover entirely, the amount of ERRP-related costs allocated to the electric department, they do, in fact, eliminate a substantial portion of them from further consideration. Moreover, the portion that is not covered is roughly matched by the amount of Waterside-related costs that Consolidated Edison will be able to avoid. On these bases alone it is fair to conclude, and we find, that the cost allocations are fair.<sup>14</sup>

Additionally, the Commission accorded weight to the following, incremental benefits to “entirely eliminate” the argument that the ERRP cost allocation did not make economic sense for the electric department: sharing of First Avenue proceeds; improved operational efficiencies; reduced environmental emissions; improved economic development; and, importantly, avoided transmission and distribution system reinforcements in the East River load pocket in Manhattan.<sup>15</sup> Based on these numerous considerations, in Con Edison’s last steam rate proceeding the Commission approved the “incremental approach” for allocating ERRP costs that is included in the Joint Proposal pending here.<sup>16</sup>

The County’s objections to the Joint Proposal’s ERRP cost allocation methodology should be rejected. The Joint Proposal follows well-settled Commission policy and precedent in allocating the ERRP costs between Con Edison’s electric and steam departments and is in the public interest.

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<sup>14</sup> Case 03-S-1672, supra, 2004 Steam Rate Order at 26-27 (footnote omitted.)

<sup>15</sup> Case 03-S-1672, supra, 2004 Steam Rate Order at 27-28.

<sup>16</sup> Id. at 28.

**B. The ERRP Cost Allocation is an Integral Component of the Joint Proposal That Must Not Be Modified**

The two-year rate plan advanced in the Joint Proposal contains no increase to base steam rates. (Ex. 1 at 3-4.) Indeed, the proposed base rate freeze is a critical element of the Joint Proposal for many of the Signatory Parties. Without the rate freeze, some parties, including the City, would not have supported the Joint Proposal, and there may not have been any settlement at all in this proceeding.

In his testimony, County witness Radigan proposes that steam customers assume any difference in fuel costs that exceed the market value of electricity produced by ERRP. (S.M. 339.) Based on the ERRP's first year of operation, the impact of Mr. Radigan's proposal would be a \$37 million steam rate increase in RY1. By seeking to impose such a significant rate increase on steam customers, the County would undercut, fundamentally, the very consideration – i.e., a base rate freeze – that compelled many of the Signatory Parties to make concessions to resolve other issues and, ultimately, support the Joint Proposal.

The County's position is untenable from a customer impact perspective. The County's proposed cost allocation would result in a rate increase that could force steam customers off the system to seek alternative energy sources for their heating and cooling requirements. Adoption of such a proposal could result in a "death spiral" – i.e., rate increases that force some customers off of the system, leading to higher rates for fewer customers, causing remaining customers to leave the system, etc. – that the Joint Proposal strives to avoid.

Moreover, the County's approach ignores the ramifications of a migration of steam customers to electric usage. As City witness Dr. Rosenberg pointed out in his pre-filed

direct testimony, the electric department receives numerous direct and indirect benefits from the operation of the steam system. (Ex. 8 at 10.) Specifically, electric customers receive the benefit of sales of energy, capacity and ancillary services into the New York Independent System Operator, Inc. at Zone J prices. This is confirmed in the Steam Business Development Plan:

In addition to the direct value provided to its customers, the steam system reduced the need for peak summer electricity capacity by about 375 megawatts, benefiting all electric customers in the southeast New York market. The system also avoids the need for additional in-City electricity and natural gas infrastructure and other associate energy costs (e.g. electric energy) and customer expenses that would be incurred were the steam system unavailable.<sup>17</sup>

Finally, in the past the Commission has expressed concerns about unwarranted cost reallocations that could force steam customers to switch to electric service. For example, in Case 27276, the Commission stated:

The record here is clear enough. There has been an exodus from the steam system attributable to conversions and it is also undisputed that lower rates would aid in stemming the tide of conversions. If the ultimate result of ever-increasing rates is the departure of all steam customers from the system, it will be disadvantageous to Con Edison's electric and gas customers. The ultimate benefit of retention of steam customers, flows, therefore, to all of Con Edison's customers and not merely to steam customers.<sup>18</sup>

Similarly, in Case 99-S-1621, the Commission concluded that:

As to Westchester County's argument that the steam subsidy should be eliminated immediately, we are not persuaded to

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<sup>17</sup> Steam Business Development Plan (dated August 26, 2005) at 14.

<sup>18</sup> Case 27276, Opinion No. 78-27; 18 NYPSC 1770.

disturb the electric rate plan for this result, particularly when the effect would be only a 1% rate reduction for electric customers, while increasing steam base rates by 20%. The depression of steam system demand might well have a negative impact on electric ratepayers, particularly at a time when the demand for electricity in New York City is already high relative to supply.<sup>19</sup>

The County's proposal – which would destroy the delicate balancing of interests achieved by the Joint Proposal and result in steam rate increases – clearly is inconsistent with Commission policy.

The Joint Proposal's ERRP cost allocation methodology provides a structured, reasonable approach to allocating ERRP costs to Con Edison's electric and steam departments. From the perspective of many Signatory Parties, including the City, it is an essential element of the Joint Proposal. If the County's proposal to modify that methodology, and thereby increase base steam rates (potentially by a significant amount) is adopted, the City would not support such a revised Joint Proposal, and likely would oppose it actively.<sup>20</sup> Westchester's proposal to increase steam rates has not been justified in the context of this proceeding, particularly when such a proposal would undermine the entire settlement that was negotiated.

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<sup>19</sup> Case 99-S-1621, supra, Opinion No. 00-15 at 20.

<sup>20</sup> Pursuant to the Joint Proposal, the Signatory Parties retain the option to oppose the Joint Proposal if it is not adopted according to its terms. (Ex. 1, § K.5.)

**C. The County's Concerns With Respect to the Overall Cost of the ERRP Are Not Relevant Here**

The County is aghast at the overall cost of the ERRP plant (S.M. 339-40), and perhaps rightfully so.<sup>21</sup> Significantly, however, the fact that ERRP cost more to construct and operate than was budgeted originally does not provide a basis for changing the well-grounded ERRP cost allocation methodology. The substantial benefits that the ERRP provides to the electric department, relied upon by the Commission in the 2004 Steam Rate Order, still are present (and, given rising electric demand, may be perceived as even more valuable in the future). The situation that the market price of the fuel used at the ERRP, or the energy and capacity prices paid for the ERRP's output, during the facility's first year of operation did not maximize profits to the County's liking has no bearing on the equity of the ERRP cost allocation methodology – those are limited and uncontrollable market outcomes.<sup>22</sup> The County's position that the ERRP cost allocation should be adjusted annually (S.M. 345) to ensure that the electric department is protected fully from the vagaries of the natural gas and

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<sup>21</sup> The City also has concerns about the ultimate costs of the ERRP, but understands that any adjustment to those costs must be pursuant to a finding of imprudence by the Commission, which remains a possibility. The prudence of the ERRP investment, however, should not determine how the costs are allocated here.

<sup>22</sup> The County's reliance on the ERRP operating statistics during its first year of operation is questionable, at best. The first year of operation for any plant necessarily includes ramp-up problems that may affect operational efficiencies. In addition, markets during the Fall and Winter of 2005 were distorted by the effects of hurricanes Katrina and Rita.

electric markets is inconsistent with Commission precedent and cost causation principles and should be rejected.<sup>23</sup>

The County also claims that, based on one year of operating information, the ERRP's fuel costs as allocated to the steam system are lower than those of the other Con Edison steam-electric stations. (S.M. 341.) The County contends that the discrepancy between the fuel costs of the ERRP and that of Con Edison's other steam-electric stations is the result of how the utility calculates its heat rate at these facilities. (S.M. 343.) This argument is based on the unsustainable presumption that the heat rate of the ERRP – a new, state-of-the-art facility – should be consistent with the heat rates of facilities that were constructed decades ago, and at least one of which (i.e., the Waterside facility) no longer exists. The ERRP has different capital costs, equipment vintage, efficiencies and technology when compared to Con Edison's other sources of steam, all contributing to differences in heat rates that should be anticipated.

Con Edison witness Shansky explained that the significant differences in the heat rates between the ERRP and the utility's other steam-electric plants can be attributed to the different technologies each facility uses to generate steam. (S.M. 257.) For instance, the ERRP uses a gas turbine ("GT") and a heat recovery steam generator ("HRSG"), as opposed to a boiler and steam turbine found in most of the other steam-electric plants. (Id.) The

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<sup>23</sup> The County's position also ignores entirely the potential impact on the delivered price of electricity if the steam rate increase that the County would impose here and in the future would lead, as some have suggested, to the ultimate demise of the steam system, and the concomitant addition of 375 MW of peak load to the electric system. Under such circumstances, the detrimental impacts to Con Edison's electric customers, in the form of higher prices, probably would dwarf the "savings" that the County is struggling to create at the expense of steam customers in this proceeding.

ERRP's technology allows electricity first to be generated in the GT, and its waste heat to be captured in the HRSG, where it is used to produce steam. (S.M. 258.)

Pursuant to the Commission's longstanding incremental cost methodology, it is appropriate to assign all of the ERRP's fuel cost to electricity generation because no additional, or incremental, fuel is required to produce steam. Conversely, Con Edison's other steam-electric facilities use conventional boilers where they first produce high-pressure steam, and some but not all of the energy in the steam then is used to produce electricity. (S.M. 258.) With the conventional boiler facilities, the incremental cost methodology would assign a much larger proportion of fuel costs to steam production compared with the technology used by the ERRP. Thus, the allocation of ERRP fuel costs is consistent with the technology employed by that facility.

It is uncontroverted that the ERRP cost allocation methodology advanced in the Joint Proposal is the same incremental cost approach approved by the Commission in Con Edison's last steam rate proceeding. The first year operational results of the ERRP, with which the County is displeased, do not undermine in any way the wisdom of the Commission's prior decisions. Movement in commodity prices affects the cost of electricity and steam produced by the ERRP, and should play no role in selecting the proper ERRP cost allocation methodology. Accordingly, the County's objections to the ERRP cost allocation methodology set forth in the Joint Proposal should be rejected.

### POINT III

#### **THE JOINT PROPOSAL PROVIDES ADEQUATE SAFEGUARDS FOR EXAMINING FUTURE OPTIONS FOR PROVIDING STEAM**

The Opponents contend that the Joint Proposal's provisions regarding the examination of future steam resources require modification because they do not require Con Edison to examine adequately third-party supply options. (See S.M. 346; TGE Initial Statement at 6.) To the contrary, the Joint Proposal provides for a comprehensive examination of all possible steam resource options, including self-production and third-party supply. (Ex. 1 at 34.) Pursuant to the Joint Proposal, Con Edison would be required to prepare an investment grade evaluation of two Hudson Avenue repowering options as identified in Phase I of the Steam Production Study, or only one option if the utility believes there is a clear and convincing option. (Ex. 1 at 32.) The purpose of the evaluation is to develop a detailed scope for the project, including cost and performance information at a level of detail that would be sufficient to support an investment decision to construct a replacement plant for the Hudson Avenue facility. (Id.)

The Joint Proposal also provides for the creation of a Steam Resource Plan. (Ex. 1 at 34.) The Steam Resource Plan requires Con Edison to examine and discuss various resource options that the utility may utilize to satisfy its future steam demand, including maintaining and/or rebuilding existing boilers, constructing a new boiler or cogeneration facility, or purchasing competitively-produced steam from a third party. Importantly, if Con Edison does not prepare and submit a Steam Resource Plan within the time period specified

in the Joint Proposal, it would be subject to a \$2 million revenue adjustment. The Steam Resource Plan is required to be completed and filed with the Commission by no later than August 1, 2007, or 12 months after Phase I of the Steam Production Study is completed. The Joint Proposal requires that the investment grade evaluation be considered in the development of the Steam Resource Plan. Accordingly, the investment grade evaluation must be completed prior to the Steam Resource Plan being finalized.

During the evidentiary hearing in this proceeding, Con Edison witness Bozgo testified as follows in response to cross-examination by TGE concerning the Joint Proposal's provisions on developing a Steam Resource Plan and the examination of competitively-procured capacity:

Q. In reviewing the JP, is it your testimony that it is mandatory that [the] company is to examine competitive procured capacity?

A. Under the resource plan, which is still to be developed, it would be evaluated.

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Q. The company will examine competitively procured capacity, you are committing the company to examine that?

A. That's correct.

(S.M. 73-74, 76.)

Additionally, during cross-examination by TGE, Dr. Rosenberg emphasized that a complete resource plan must be one that examines all viable options:

Q. It's your interpretation of the Joint Proposal that it is mandatory that Con Edison must examine offers from third parties to sell steam?

- A. Con Ed will produce a resource plan, and that resource plan must consider all options, and besides which it would be imprudent for Con Ed to preemptively eliminate any viable options.

(S.M. 199.)

In response to cross-examination by TGE as to whether there would be a requirement to seek competitively-procured capacity as part of the Steam Resource Plan, Con Edison witness Padula testified that “[i]t would be our expectation that the company would seek competitively procured capacity.” (S.M. 150.) As demonstrated extensively and repeatedly throughout the record in this proceeding, the Joint Proposal ensures that all viable options will be examined as part of the Steam Resource Plan, including third-party supply.

**A. TGE’s Objections to the Joint Proposal Should be Rejected**

TGE objects to the Joint Proposal because it somehow believes that the settlement eliminates Con Edison’s obligation to examine steam production from third-party sources, a requirement already placed upon and acknowledged repeatedly by the utility. (See, e.g., S.M. 58, 64.) TGE professes to be concerned that the process outlined in the Joint Proposal regarding the Steam Production Study “is unfair to entities that seek to supply steam to Con Edison at competitive prices.” (TGE Initial Statement at 3.) TGE proposes that Section I of the Joint Proposal be modified to provide that “Con Edison will agree to negotiate with TransGas ... the potential terms of a steam sales agreement based upon Con Edison’s full avoided steam production and capacity costs .... Con Edison’s rationale for accepting or rejecting the potential terms [of a steam sales agreement] shall be provided in

the Steam Resource Plan with supporting cost details.” (Id. at 8-9.) TGE’s proposal even anticipates the necessity of assistance of Staff and/or an Administrative Law Judge to negotiate what admittedly are “potential” contractual terms.

Initially, TGE’s proposed addition to the Joint Proposal is not necessary. As noted above, the Joint Proposal already provides that Con Edison must evaluate self-supply and third-party supply options against each other as part of the Steam Resource Plan and then “fully support and justify” the utility’s future resource selection. (Ex. 1 at 34.) Presumably, Con Edison would be unable to complete the comparative analysis required under the Joint Proposal, or satisfy any relevant prudence standard, without determining the terms and conditions under which available third-party supply options could be procured. Thus, the Joint Proposal already ensures that third-party supply options will be evaluated fairly, and TGE’s proposed modification should be rejected as wholly unnecessary.

Inasmuch as the Joint Proposal already ensures a balanced review of all supply options, including those that TGE may choose to offer, the City suspects that the driving force behind TGE’s proposed modification to the Joint Proposal is its desire to control – for its own financial gain – Con Edison’s ability to evaluate TGE’s proposal. For example, TGE’s proposed modification would mandate that Con Edison’s “full avoided steam production and capacity costs” be used as the basis for pricing any third-party supply option, including those advanced by TGE. (TGE Initial Statement at 8-9.) The City disagrees with TGE’s attempt to bind Con Edison, in the Joint Proposal, as to how and under what structure the utility may negotiate the terms and conditions of any third-party supply contract. The Joint Proposal should not be utilized to introduce restraints on Con Edison’s ability to

examine supply options from third parties or make business decisions impacting the utility's customers and shareholders. TGE's proposed modification of the Joint Proposal is not in the best interest of steam customers.

TGE's proposal also contemplates a cumbersome negotiating process, including the potential involvement of third-party facilitators or mediators. Again, this is not necessary – as set forth in detail above, the Joint Proposal ensures that eligible third-party suppliers will be included in the comparative analysis required for the Steam Resource Plan. If TGE or another supplier feels that it is shortchanged during that process, it can make its complaints known to the Commission and seek appropriate redress. There is no basis upon which the Commission should pre-judge that a dispute requiring resolution will arise.

In support of its proposed modification of the Joint Proposal, TGE relies on a Commission Order requiring Con Edison to negotiate with steam suppliers. (TGE Initial Statement at 7-8.)<sup>24</sup> In the Steam Plan Order, the Commission ruled that “Con Edison should be willing to enter into negotiations with any producer that can offer pricing under the terms that are competitive with Con Edison's own avoided steam costs, so long as doing so does not result in the new owner having excessive market power ....”<sup>25</sup>

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<sup>24</sup> See Case 96-S-1065, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service and Case 96-S-1121, Petition of Consolidated Edison Company of New York, Inc. for Determination of Accounting and Ratemaking Treatment Applicable to the Company's Costs of Converting Boilers at the 59th Street and East River Generating Plants to Burn Natural Gas, Order Concerning Phase II Steam Plant Report (issued December 2, 1999) (“Steam Plan Order”).

<sup>25</sup> Cases 96-S-1065 and 96-S-1121, supra, Steam Plan Order at 7.

TGE argues that the Joint Proposal would eliminate the obligations established in the Steam Plan Order while “Con Edison developed proposals for its own plants and the TransGas Proposal would languish and grow stale.” (TGE Initial Statement at 8.) TGE’s argument lacks merit for two reasons. First, there is no limitation or other language in the Joint Proposal that eliminates or restricts Con Edison’s obligation to examine and consider offers from third-party suppliers such as TGE. To the contrary, as noted above, the Joint Proposal requires Con Edison to examine self-supply and third-party supply options and identify the option selected by the utility with full support and justification in its Steam Resource Plan. (Ex. 1 at 34.) Second, even if, arguendo, TGE is able to establish at some time in the future that Con Edison has committed a violation of the Steam Plan Order, this is not the appropriate time or forum to address such a speculative matter. Before the Commission is a Joint Proposal that advances a multi-year steam rate plan; there is no compelling reason why the Commission should modify that Joint Proposal now to address a possible future violation of a prior Commission order (that can be resolved in an administrative proceeding if and when such violation ever were to occur).

Finally, the modification to the Joint Proposal advocated by TGE is unlawful, as it would grant a potential steam supplier (i.e., TGE) a Commission-endorsed preference in negotiating a supply contract with Con Edison in violation of New York Public Service Law section 79(3).<sup>26</sup> In essence, TGE is requesting that the Commission order Con Edison to negotiate the terms of a steam contract with TGE, compare the terms of a potential contract with TGE against an investment grade study and any other resource options studied by the

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<sup>26</sup> N.Y. Pub. Serv. Law § 79(3).

utility, and provide its rationale for entering or not entering into a contract with TGE in the Steam Resource Plan with supporting cost details. (TGE Initial Statement at 8-9.) While TGE phrases its proposed revision to the Joint Proposal to include other potential steam suppliers, it nonetheless explicitly endorses TGE, something the Commission is, or should be, prohibited from doing. Accordingly, the Commission should reject TGE's proposed modification to the Joint Proposal because it unlawfully would create a real or perceived undue preference to a potential steam supplier.

**B. The County's Objections to the Joint Proposal's Process for Addressing Future Steam Supply Options Should Be Rejected**

In his testimony, Mr. Radigan observes initially that "any new production studies should be conducted with full input from all interested parties, including Westchester." (S.M. 336.) With respect to the Steam Resource Plan, Mr. Radigan concludes that no new steam resource decision should be made until a "full and open review" is conducted. (S.M. 337.) Inexplicably, Mr. Radigan then prejudices the results of the Steam Production Study and the Steam Resource Plan by proclaiming that, due to perceived problems at the ERRP, "Con Edison should seek to acquire any additional capacity from other sources rather than procure additional steam itself." (S.M. 346.)

As noted above, the Joint Proposal provides that Con Edison must develop a Steam Resource Plan and, as part of that Plan, the utility must examine a number of supply options, including competitively-procured capacity. (Ex. 1 at 34.) The County's position that Con Edison should be precluded from analyzing any self-supply options is unreasonable

and demonstrates further the County's general antipathy toward Con Edison's steam customers. Steam customers could be harmed severely if Con Edison is not allowed to seek the least-cost option, which could well be a self-supply option. Moreover, to preclude all future self-supply options would ensure that third-party suppliers gain a superior negotiating position in any future dealings with Con Edison. In short, the County's position would help to ensure that steam customers absorb potentially unfair and excessive rates. Accordingly, inasmuch as the Steam Resource Plan addresses adequately the various options that Con Edison should examine if it is determined that additional steam capacity is needed, the Commission should reject the County's argument that the utility be permitted to examine only capacity supplied by third parties.

With respect to the County's concerns about the overall steam planning process, the Joint Proposal ensures that a "full and open" review will take place. The Steam Production Study provisions of the Joint Proposal are intended only to ensure that Con Edison will complete, in a timely fashion, a thorough analysis of two of the Hudson Avenue repowering options identified from Phase I of the Steam Production Study that was ratified by the Commission in the 2004 Steam Rate Order. The rationale for selecting the preferred options must be presented to the Steam Business Development Task Force, which includes the County and TGE. In addition, interested parties will be updated as milestones are met and receive copies of the investment grade evaluations when they are filed with the Commission. (Ex. 1 at 32-33.)

Importantly, the results of the investment grade evaluations of the preferred Hudson Avenue repowering options do not pre-ordain that one of those options will be

chosen to satisfy future resource requirements. Instead, those self-supply options will be evaluated against other supply options, including potential third-party supply agreements, in the Steam Resource Plan. (Ex. 1 at 34.) That Plan must examine and evaluate all resource options and identify and support a recommended option. (Id.) In sum, the Joint Proposal provisions requiring an investment grade evaluation and the preparation of a Steam Resource Plan simply require the Company to evaluate all potential sources of steam on a level playing field and make a rational decision.

Finally, the Steam Resource Plan must be filed with the Commission, at which time it will be subject to review and comment by interested parties. Of course, Staff also will review the Plan and provide its comments. In short, the process advanced in the Joint Proposal for evaluating future steam supply resource options protects fully the rights of interested parties to review and comment on Con Edison's decision. Accordingly, the County's objections to the proposed process should be rejected. There is no need to modify the Joint Proposal in response to the County's arguments.

**CONCLUSION**

For the reasons set forth in the City's Statement in Support, its Reply Statement in Support, and herein, the Joint Proposal should be adopted in its entirety and the objections of the County and TGE to the ERRP cost allocation provisions and the Steam Production Study should be rejected.

Dated: August 7, 2006  
Albany, New York

Respectfully submitted,

*Moshe H. Bonder*

Robert M. Loughney, Esq.  
Moshe H. Bonder, Esq.  
COUCH WHITE, LLP  
Attorneys for The City of New York  
540 Broadway  
P.O. Box 22222  
Albany, New York 12201-2222  
(518) 426-4600

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**CERTIFICATION OF SERVICE**

I hereby certify that on this day a true copy of the above document was served upon the attorney of record for each party by mail/by hand/overnight delivery.

Date: 8/7/06 *Ally D. Durand Thomas*