



March 12, 2013

VIA ELECTRONIC FILING

Honorable Jeffrey C. Cohen, Acting Secretary
New York State Public Service Commission
Three Empire State Plaza
Albany, NY 12223-1350

RE: Case 12-G-0297 – Proceeding on Motion of the Commission to
Examine Policies Regarding the Expansion of Natural Gas Service

Dear Acting Secretary Cohen:

In accordance with the Commission's Notice of Technical Conference and Notice Soliciting Comments, issued and effective November 30, 2012, attached please find jointly-submitted comments of New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation.

Should you have any questions, please contact me at (607) 762-8710.

Respectfully submitted,

A handwritten signature in black ink that reads "Lori A. Cole".

Lori A. Cole
Manager – Regulatory & Tariffs
Rates and Regulatory Economics Department

Enclosures

BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

-----x

Proceeding on Motion of the Commission to Examine Policies
Regarding the Expansion of Natural Gas Service

Case 12-G-0297

----- x

**COMMENTS OF
NEW YORK STATE ELECTRIC & GAS CORPORATION AND
ROCHESTER GAS AND ELECTRIC CORPORATION**

Dated: March 12, 2013

BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

-----x

Proceeding on Motion of the Commission to Examine Policies
Regarding the Expansion of Natural Gas Service

Case 12-G-0297

-----x

**COMMENTS OF
NEW YORK STATE ELECTRIC & GAS CORPORATION AND
ROCHESTER GAS AND ELECTRIC CORPORATION**

A. Introduction

On November 30, 2012, the New York State Public Service Commission (the “Commission”) initiated a proceeding to examine its policies regarding the expansion of natural gas service in New York State.¹ On the same day, the Commission issued a Notice of Technical Conference and Notice Soliciting Comments (“Notice”).² The Notice invited interested parties to submit comments on twenty-one issues. New York State Electric & Gas Corporation (“NYSEG”) and Rochester Gas and Electric Corporation (“RG&E”) (together “the Companies”) hereby respectfully submit responses to the issues included in the Notice.

B. Responses to the Notice

1. Please explain your understanding (and for utilities, your implementation) of Commission regulations and the Natural Gas Expansion Policy including your views on whether they encourage or deter expansion of the natural gas delivery system in New York State. Do you feel that the Commission regulations and Policy should be modified and if so, how?

¹ Case 12-G-0297 – Proceeding on Motion of the Commission to Examine Policies Regarding the Expansion of Natural Gas Service, Order Instituting Proceeding and Establishing Further Procedures, at 10 (Nov. 30, 2012).

² Case 12-G-0297, Notice of Technical Conference and Notice Soliciting Comments (Nov. 30, 2012). The Companies participated in the Technical Conference held on January 9, 2013.

The Companies view the Commission's policy set forth in the Statement of Policy Regarding Rate Treatment to be Afforded to the Expansion of Gas Service into New Franchise Areas ("Policy Statement") as a mechanism to assess each municipality's request to provide natural gas service to a franchise in a consistent and equitable manner.³ The Policy Statement provided clarity to gas utilities on the risks and opportunities of expanding gas service into new franchise areas. The Policy Statement adopted a five-year development period to assess economic impacts of franchise expansions and provided normal ratemaking treatment for all investment, revenues, and expenses if the franchise proposal was projected to earn the allowed rate of return by the fifth year of the development period. On the other hand, if the franchise proposal was not expected to earn the allowed return within the five-year development period, revenue imputations necessary to achieve the allowed return would be made in rate proceedings during the five-year development period. However, utilities would be able to assess surcharges on all customers in the new franchise area to reduce any revenue deficiencies.

NYSEG and RG&E recognize the need for economic metrics that encourage worthwhile gas franchise expansions and minimize uneconomic franchise expansions, and at the same time the corresponding need to make the metric relatively easy to administer. The Policy Statement has been a useful guideline for assessing the risks and opportunities of gas franchises given the circumstances that existed when the Policy Statement was adopted and for many years thereafter. However, the Policy Statement should be re-examined given the relatively low commodity costs for gas, ample supplies of gas now available in the Northeast, and the State's interest in expanding natural gas because of its benefits for increased economic growth and reduced carbon emissions.

³ Case 89-G-078, issued and effective December 11, 1989.

- 2 & 3. Regarding the Commission's regulation of the natural gas delivery system and the system itself, do you believe that the interests of utility shareholders, ratepayers, and the State as a whole are aligned? Please explain. Are there provisions of current policies or regulations that appropriately incentivize the expansion of the natural gas delivery system in New York State? Are these sufficient? If not, please suggest alternatives.

The Commission's current policies and regulations have generally served the interests of utility shareholders, customers and the State as a whole by providing a cost-effective approach to evaluate gas franchise expansions. NYSEG and RG&E continually look for gas franchise expansion opportunities. In the early 1990s, NYSEG was very active in expanding gas service into new areas which were economically viable. Recently this activity has slowed because of the relatively high cost of expanding into un-served areas near NYSEG's existing gas franchise areas.

The Companies believe the Commission should re-examine the use of a five-year development period to assess the economic viability of gas franchise expansions. For example, given the public benefits of expanding gas usage throughout the state (e.g., economic and environmental benefits), a longer development period (e.g., 10 years) might be more appropriate. A longer development period may make currently unattractive expansions more attractive to utilities and future customers. Furthermore, given the average expected life of gas distribution plant, the use of a longer development period should not result in uneconomic expansions.

4. Identify current barriers inhibiting conversion to natural gas usage from other heating fuels - other than the cost of replacing heating equipment. Please explain how the barrier inhibits conversion and provide suggestions for reducing or eliminating the barrier – including the cost of replacing heating equipment.

In addition to the cost of replacing heating equipment, main extension surcharges and excess length gas service charges inhibit customers from converting to natural gas usage from other heating fuels. Charges for main extensions and excess length services add to the

customer's total cost to convert to natural gas. Another barrier to be considered is the remaining useful life of a customer's existing heating equipment. These barriers can be reduced by offering conversion rebates and providing assistance in securing financing options.

5. Please identify the outreach and education efforts currently employed by the utility for the purposes of gauging interest in natural gas service and/or soliciting new customers in areas where interest in the possibility of obtaining service has been expressed. Are the efforts sufficient? How can they be improved? Would expanded or improved outreach and education programs increase conversion to natural gas by customers who reside within the 100 feet zone of existing utility infrastructure (and, accordingly would not pay for the extension)? How can the utility identify, communicate and engage with such customers? When an individual customer requests service, please describe the utility's efforts to communicate with or solicit other customers in the neighborhood/area.

Currently, the Companies' Marketing & Sales personnel contact potential customers along a proposed main extension (via mail) to ascertain their interest in converting to natural gas. In the Companies' experience, these efforts are sufficient. However, such efforts could be improved by direct contact via telephone or in person. Expanded outreach to customers within the 100 foot zone of existing infrastructure would increase conversions. The utility can identify these customers by using tax parcel data and utility billing and mapping systems. When a customer requests service and a main extension is required, the potential customers along the proposed main extension are identified and letters are sent to them to determine their interest in natural gas.

6. Please identify the typical flow of communication and information between the utility and a customer requesting service that would require extension of a gas main sufficient to require a surcharge. Please provide any examples of written communication.

When a potential customer calls the Companies' Customer Relations Center requesting service, he/she is placed in a queue that specifically addresses requests for the installation of new service. The customer service representative obtains the relevant information and creates a

ticket. The ticket is sent to the local gas field planner. The gas field planner determines the service size and cost to extend natural gas service to the potential customer. At times, the Companies' Marketing & Sales personnel will initiate customer contact via mail to ascertain interest in gas service along a potential main extension. Based on the number of interested customers, the anticipated usage and the cost of installation, the Company calculates a surcharge and, if applicable, informs the customers who initially expressed an interest in gas service. These customers are asked to confirm their commitment to accepting natural gas service based on the surcharge amount. Ultimately, the Company establishes a final group of customers that are willing to pay the required surcharge. The final group of customers receives a surcharge agreement for signature. Once all surcharge agreements are signed, the Company commences construction of the main and service.

7. What issues should be given consideration prior to expansion of the natural gas delivery system? Should such considerations include protections for a group or groups of customers? If so, what should be and what types of protections should be considered?

If applicable, the Commission should consider giving broader authorization when granting a utility's request to exercise or amend a franchise. The existing infrastructure of the natural gas delivery system should also be considered as these expansions occur. The natural gas market should expand when it is cost effective to do so and should not consider protections for different groups of customers. Such considerations increase costs for ineligible customers.

8. Are there existing utility specific pilot programs focused on new approaches to line extensions or new franchise expansions of the natural gas delivery system? If so, please describe the pilot program. If not, could such a pilot program be beneficial and, how would it be designed?

NYSEG and RG&E currently do not have a specific pilot program focused on new approaches to natural gas line extensions or new franchise expansions. However, a pilot program might be beneficial for those areas where it is economically difficult to justify

expansion under the guidelines of the Policy Statement. Some potential pilot designs could include:

- i. Use of different development periods (e.g., 5, 10, 15 years) in assessing the need for revenue imputation depending upon the cost of expansion and customer density.
- ii. Modifications to the customer surcharge process. Establish surcharges at the outset of the project which will not change regardless of customer adoption. Thereafter, establish an account for any excess or shortfall. The excess or shortfall will be applied to rates in subsequent years.
- iii. Allow project expansions to be included as part of the utility's rate base.
- iv. Investigate opportunities with Municipalities and Economic Development Agencies to assist in contributing to construction costs for an entire town as opposed to an individual large customer.
- v. Develop partnerships with community leaders in performing customer surveys and load estimates.
- vi. Develop a dedicated website for the pilot expansion project.
- vii. Develop an infrastructure program that uses funds from existing surcharges (e.g. EEPS, RPS). Expansion of natural gas by converting from less environmentally friendly fuels has quantifiable benefits which may support energy efficiency or renewable targets.

9. The Commission’s regulations (§230.2[f]) provide that “each corporation may, in its tariff schedules, extend such obligation [to provide certain main and service line extensions without cost to the customer]; to the extent the provision of additional facilities without charge is cost-justified.” Identify whether the utility ever provides residential customers with more than 100 feet of gas main or service line without surcharge. Please explain why and under what circumstances or, if never, why not. Is the utility aware of any geographic areas in its service territory where potential cost justified extensions of greater than 100 feet are currently un-served? If not, has the utility ever attempted to ascertain or develop such information? What should be the appropriate length of main and/or service provided without surcharge? Please explain.

In accordance with its tariffs, NYSEG provides residential heating customers with service length equal to the greater of 100 feet or the footage equivalent to 70% of the estimated annual revenue and RG&E provides 100 feet of service. Both Companies provide residential customers up to 100 feet of main.

NYSEG’s tariffs already provide a mechanism to provide footage greater than 100 feet if the estimated annual revenue of the customer justifies the amount of footage. NYSEG has not performed studies to specifically review the thresholds for evaluating extensions for areas currently unserved. However, it has been NYSEG’s experience that the 100 feet of service is greater than the footage equivalent to 70% of estimated annual revenue, and therefore has only provided the 100 feet. RG&E has not performed any such studies.

10. Does the utility provide programs that could assist low income customers or those on a fixed income to overcome the barriers to conversion to natural gas?

No.

11. Are there potential funding mechanisms for expansion of the natural gas delivery system other than through utility rates or direct customer payments (surcharges, CIACs or other)?

Potential funding mechanisms outside of utility rates or direct customer payments include sources of funding from the governments of the communities that benefit from the provision of natural gas service. These sources of funding can come in the form of direct grants, Payment In

Lieu Of Tax (PILOT) agreements or Tax Increment Financing agreements (TIFs). Depending upon the design, these mechanisms will either offset the capital cost of constructing the project or reduce the property tax burden on the owner of the system, both of which will enhance the financial viability of the project.

PILOT agreements have been used in New York as an incentive for investment in taxable infrastructure or other facilities that create a public benefit. A traditional example includes the offering of a PIOLT to large manufacturing companies to induce the company to locate in a community. A PILOT may be negotiated to limit or defer the property taxes on a developer, striking a balance between public and private economic needs. Offering PILOTs to developers of natural gas systems also fits within this balance.

TIFs are more popular in other states and occur when a municipality elects to provide financial assistance to local economic development projects (e.g., infrastructure improvements, business expansions) by using new property taxes that result from the commercial investment and corresponding increase in property value. Where available, TIFs are a tool that permits a municipality to participate in local project financing by using some or all of the new property taxes from a capital investment within a designated geographic district. The municipality has the option of using the “incremental” taxes to retire bonds it has issued for the project, compensate a developer or business for development project costs, or fund other eligible municipal economic development activities. The designation of a TIF district requires proper notice, a local public hearing, the majority vote of the municipal legislative body, and state approval. Although there are laws that allow TIFs in New York, they are not very popular due to the fact that they only address true property tax revenues and not school tax revenues which make up the majority of a

tax bill. However, Assemblyman Robin Schimminger and Senator Catherine Young recently introduced legislation that is intended to address this shortcoming.

In addition, the concept of developing a distribution system improvement charge (DSIC), similar to a mechanism implemented in Pennsylvania to improve infrastructure, would facilitate expansion in the Companies service territories.⁴ A DSIC establishes a rate mechanism to recover the capitalized costs related to repair, improvement and replacement utility infrastructure. A DSIC can reduce regulatory lag, improve access to capital at lower rates, and accelerate infrastructure improvement and replacement.

12. Are existing natural gas efficiency programs adequate and optimal to serve the expansion of customers within 100 feet of existing utility infrastructure? If not, what changes, including possibly the level of funding, could be made to improve the existing efficiency programs? Would efficiency programs targeted to conversion customers result in increased energy savings, and if so, how?

The Companies have substantial funding available within the current Energy Efficiency Portfolio Standards (“EEPS”) Orders for residential gas energy efficiency boiler and furnace replacements which can be utilized by customers making such conversions, who are within 100 feet of existing utility infrastructure. However, most water heating, and all cooking and clothes drying appliances are currently ineligible for a rebate within this program. Modification to the existing Residential Gas HVAC program to include natural gas water heating, cooking and clothes drying equipment, would likely increase the number of units converted and would therefore increase energy savings. In addition, the Companies have petitioned the Commission to reduce the funding and the energy efficiency targets for this program from those ordered in 2011, to reflect the actual participation in the program annually since its inception, and the probability of future demand similar to the historic participation in the program. Action on this

⁴ Pennsylvania Public Utility (Code), Chapter 13, Subchapter B, Sections 1350 through 1360 of the Code, which deals with distribution (and collection) systems and allows specified utility types to petition the Commission for an additional rate mechanism, known as a DSIC. See 66 Pa. C.S. §§ 1350-1360.

petition may reduce the funding available for participation from customers in new conversion markets.

NYSEG and RG&E have funds available for non-residential natural gas equipment conversion, if the new equipment provides the energy savings required by the New York State Technical Manual as well as other EEPS program requirements. The amount of funding available for expansion customers will be mitigated in part by demand from other customers; NYSEG and RG&E have recently received approval to combine two gas rebate programs, which will in the future make the funds more accessible.

It is not clear whether efficiency programs targeted to conversion customers would be any more or less effective than are current programs without such targets, if only the target mechanism were changed. It is possible that relaxing other EEPS requirements (such as TRC requirements and payback periods) may encourage more conversions, even without targeting conversion customers. However, changes of this nature would have an effect on the overall savings attributable to the programs and achievement of statewide energy savings targets. Currently, budgets for EEPS programs are based in part on the effective cost per unit saved, which may be impacted by any change in savings or TRC requirements.

13. Do Revenue Decoupling Mechanisms (RDMs) impact expansion of the natural gas delivery system?

The current RDM structure in New York has not impacted the expansion of natural gas delivery service.

14. Does the utility have any information or estimates concerning the existence of commercial or industrial customers who may add and/or retain jobs if they could switch their process or heating fuel to natural gas? If so, how many jobs might be added or retained?

The Companies do not have any such information or estimates.

15. Are there specific industries in the State that would benefit from an expanded natural gas delivery system? Please describe.

The Companies believe the agricultural business sector (e.g., food processing companies, large farms with grain dryers) could benefit from an expanded natural gas delivery system.

Also, it would be beneficial to develop a more robust economic development grant program for gas infrastructure assistance on the utility side and/or customer side of the meter to help offset costs for a project and influence the decision to invest. Currently gas infrastructure program assistance for both RG&E and NYSEG is minimal compared to its electric infrastructure programs. Additionally, a program that provides economic development grants to supplement the Companies' energy efficiency gas rebate programs or New York State Energy Research and Development Authority ("NYSERDA") energy efficiency programs, similar to those developed for electric economic development grant programs could facilitate natural gas expansion.

16. Are there potential partnerships between various entities involved in the energy and heating markets in New York State that could facilitate expansion of the natural gas delivery system? If so, please provide examples and whether your organization would be willing to take part in such a partnership. Who would be best suited for encouraging and developing such partnerships? What role should the public sector play?

NYSEG and RG&E believe that partnerships, direct or indirect, are often the solution to bridging the gap between a potential LDC distribution system and interstate pipelines, the traditional source of supply. In fact, there exist a few examples where expansion was enabled by coordination. Such examples include taking service from other LDCs and intrastate pipelines afforded lightened regulation and built primarily for other purposes. NYSEG and RG&E anticipate emerging opportunities where coordination will enable expansion to areas previously unserved due to lack of an economic source of supply, including but not limited to connections

to strategically sited gathering systems, direct connections to indigenous supply, and distributed sources such as compressed natural gas (CNG) and liquefied natural gas (LNG).

Establishing these emerging opportunities as sufficiently reliable for LDC firm service will take coordination between the potential supplier and the utility. There is a natural incentive to develop solutions to this issue given the desire for the upstream suppliers to have a firm market for supply and for the LDC's need for reliability. NYSEG and RG&E look forward to developing these strategic initiatives as opportunities become more fully developed or actionable.

From a policy perspective, the Commission should encourage LDC distribution system investments that relieve constraints on the system and allow for increased flows from new upstream sources. It also encourages up stream investment to match load. In addition, the LDC benefits from more economic supply, capacity for expansion, and economic replacement of aging infrastructure.

17. Are there programs currently administered by utilities or federal, state or local agencies that assist customers with heating fuel conversions? Are there roles that other agencies, such as the New York State Energy Research and Development Authority (NYSERDA), should play in expansion of the natural gas delivery system? Should the Energy Efficiency Portfolio Standard (EEPS) programs be expanded or modified to encourage conversions to natural gas before end-of-life replacements?

NYSEG and RG&E offer two programs which assist customers with the installation of more efficient heating systems, including installations which effectively convert the heating process from other fuels to natural gas. These programs are the Residential Gas HVAC Program and the Commercial/Industrial Rebate Program. The assistance, in the form of rebates for residential, commercial and industrial customers, requires the new natural gas heating unit provide documented energy savings over a standard code compliant natural gas base unit. In

addition, systems may be replaced and qualify for rebates, before end-of-life replacement within the current guidelines of the EEPS programs.

The current EEPS programs operated by NYSEG and RG&E do not encourage conversion to natural gas, but do not prohibit the conversion if appropriate energy savings are simultaneously achieved.

NYSEG and RG&E also offers incentives for energy efficient replacement heating equipment, designed in the same framework of technical requirements as those programs operated by NYSEG and RG&E. NYSEG and RG&E's role in the expansion of the natural gas delivery system should be the same as their role currently in the offering of customer incentives for this energy efficient replacement heating equipment.

18. Are there opportunities to coordinate natural gas delivery system expansion projects with other available resources, such as economic development, energy efficiency, or environmental protection? Please provide specific examples, if possible.

Yes, there are a number of economic development partners such as NYSEG and the New York Power Authority, business attraction organizations such as the Buffalo Niagara Enterprise and Greater Rochester Enterprise, Southern Tier Economic Growth (STEG), Three Rivers Development Corporation (Corning), Tompkins County Area Development (TCAD), Empire State Development, and Industrial Development Associations, as well as local municipal community development organizations and county offices of energy development that are willing to participate in opportunities to attract expansion projects.

19. Are there changes that could be made to the environmental impact review process involved in granting or expanding gas franchise areas that could improve or streamline the process?

Yes, there should be different levels of environmental review based upon proposed length, location, and proposed construction technique for the expansion. There should also be

clear thresholds or checklists which would dictate the different levels of the environmental review process.

For example, an expansion that is less than a tenth of a mile, within existing previously disturbed corridors such as public rights-of-way, or that would mitigate environmental impacts by directional drilling should have a simpler review process than a longer length expansion into environmentally sensitive areas or undeveloped areas.

Also, consideration should be given to a general environmental overview in granting a franchise with a more detailed review prior to actual construction. It is conceivable that a franchise can be granted for a given area but not built until years later.

20. Please identify, if any, areas of the State where provision of natural gas delivery service is unrealistic because of environmental constraints, construction permitting requirements or other factors and explain why service to such areas is believed to be unrealistic. Are there any areas of the State that require special consideration regarding expansion of the natural gas system?

Permitting and mitigation costs for construction in the Adirondack Park, State Forests, Wetlands, and Wildlife Refuse Areas may make the project costs prohibitive to provide natural gas service in these areas. Portions of these areas are not developed and, therefore, the demand for new gas service in these areas is unknown.

21. Please explain your utility's natural gas delivery system expansion planning process including any large-scale and or long-term plans that are in place or are being considered.

The natural gas delivery system expansion planning process at NYSEG and RG&E is primarily based on financially viable projects which have adequate customer demand. The typical process in determining where to expand gas to new communities (including other activities that need to be accomplished) involve the following:

- Identify towns near an existing source of supply
- Identify anchor customers

- Estimate additional residential/small commercial connections
- Estimate cost of construction
- Obtain franchise from the municipality
- Secure agreements with anchor customers
- Refine construction estimates and revenue projections
- Demonstrate five-year return threshold
- File petition with the Commission
- Construct on receipt of certificate
- Connect customers upon request for service

The planning process for providing service to new customers in existing franchise areas typically begins with a request for service from a prospective customer. Developing construction cost estimates and revenue projections from these customers then follows. Construction of the services to the new customer commences upon the economic feasibility of the expansion and potentially customers agreeing to a construction cost contribution if the revenues do not justify the expense. Extensions within a new Commission-approved franchise area are subject to the Companies' tariff provisions and the Commission's rules relating to installations of mains, services, extensions, and extension of company facilities to serve customers. Currently, NYSEG and RG&E do not have any natural gas delivery system expansion plans that it would consider large-scale or long-term that are in place or are being considered. The Companies have infrastructure improvement projects planned for areas that have existing gas service and are experiencing load growth.

C. Conclusion

The Companies respectfully request that the Commission consider the comments above and adopt the recommendations contained herein.

Dated: March 12, 2013

Respectfully submitted,

A handwritten signature in cursive script that reads "Lori A. Cole". The signature is written in black ink and is positioned above a horizontal line.

Lori A. Cole
Manager – Regulatory & Tariffs

On behalf of
New York State Electric & Gas Corporation
and Rochester Gas and Electric Corporation