STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on December 11, 2014

COMMISSIONERS PRESENT:

Audrey Zibelman, Chair
Patricia L. Acampora
Garry A. Brown
Gregg C. Sayre
Diane X. Burman

CASE 14-G-0214 - Petition of KeySpan Gas East Corporation d/b/a National Grid for Authority to Defer Costs Associated with Incremental Capital Expenditures and Other Related Relief.

ORDER DIRECTING INVESTMENTS AND ALLOWING, IN PART, DEFERRAL AUTHORITY FOR COSTS ASSOCIATED WITH INCREMENTAL CAPITAL EXPENDITURES AND ESTABLISHING A SURCHARGE

(Issued and Effective December 15, 2014)

BY THE COMMISSION:

INTRODUCTION

By verified petition dated June 13, 2014, KeySpan Gas East Corporation d/b/a National Grid (KEDLI or the Company) requested authority to establish a new deferral accounting mechanism that it claims will allow for a three-year $700 million capital investment program in gas infrastructure while preserving base rate stability. The Company maintains that its proposed investment in gas infrastructure will increase gas safety and reliability, modernize gas transmission and distribution assets, promote energy affordability, and enhance storm resiliency and the Company’s ability to respond to severe weather events.

KEDLI’s proposal would permit the Company to defer for future recovery in rates the pre-tax revenue requirement associated with its capital spending program to the extent such investment exceeds the level of book depreciation expense reflected in rates. KEDLI also proposes that the new mechanism eliminate its existing City/State Construction and Non-Growth Related Capital deferral mechanisms.

Because KEDLI’s proposed capital program addresses the critical need for the Company to make materially increased investments to further our policy goals surrounding leak prone pipe-removal and energy affordability, we are directing the Company to make those investments in its gas distribution system to serve the public interest. We discuss herein the mechanisms, including a surcharge and a new deferral, that, due to the extraordinary circumstance of KEDLI’s inability to file for a base rate increase, we will allow to provide for the costs of such investments.

We estimate that an average residential heating customer would face a 3.3% increase in the Company’s next rate case stemming only from the capital investments approved in the order (i.e., not factoring in any other cost increases the Company is likely to seek recovery for in its filing, including the return on investments made from January 1, 2013 through December 31, 2014 and any rate year investments projected in the rate year), assuming a surcharge was not implemented and the deferral costs were amortized over three years (see page 7 of Attachment II). As discussed in this Order, the deferral impact to an average residential customer in the Company’s next rate case is reduced with the implementation of a surcharge. The surcharge itself will be a bill increase of approximately 1.2% ($1.37 per month for a residential customer), in effect from April 2015 through December 31, 2016. If the amortization of the growth deferrals begins in January 2017, at the same time the surcharge for the leak prone pipe expires, then the bill impact on customers will be approximately 1.5% (a $1.69 per month impact for a residential customer).

BACKGROUND

KEDLI's last base rate increase became effective January 1, 2008.[1] Since then, the Company's base rates have been frozen to the present date.[2] KEDLI maintains that it is not able, at this time, to file for new base rates that would support the proposed investment due to KEDLI's difficulties in accessing and verifying accurate data since it implemented its US Foundation Project in November 2012; a position confirmed by its outside auditors. KEDLI states that its financial reporting issues have prevented it from preparing accurate test year data, normalizing such data, forecasting a rate year and linking the 150 days under our policy in major rate proceedings in order to file a base rate case to support the proposed investment. The Company has stated that it does not expect to be able to file for new base rate relief until early 2016.

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[1] See Cases 06-M-0878 et al., National Grid PLC and Keyspan Corporation – Petition for Merger Approval, Abbreviated Order Authorizing Acquisition Subject to Conditions and Making Some Revenue Requirement Determinations for KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island (issued August 23, 2007) (August 23 Order); Order Authorizing Acquisition Subject to Conditions and Making some Revenue Requirement Determinations for KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island (issued September 17, 2007) (September 17 Order); Cases 06-G-1186, et al., KeySpan Energy Delivery Long Island – Gas Rates, Order Adopting Gas Rate Plans for KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island (issued December 21, 2007).

[2] See September 17 Order at 72.

KEDLI's rate plan expired on December 31, 2012, and the Company is currently in a "stay out" period with no provision, absent Commission or other legally mandated action, that would allow for the recovery of incremental capital expenditures. In the final year of KEDLI's rate plan, it spent $138.3 million in making capital improvements. The Joint Proposal underlying KEDLI's rate plan required the Company to spend a set amount of "non-growth" investment capital in calendar year (CY) 2012. To the extent such amount was underspent, the Company had to defer the full revenue requirement effect of that shortfall to its balancing account.

In addition, the Joint Proposal authorized KEDLI to defer to its balancing account the full revenue requirement effect associated with the difference between the annual forecast amount of KEDLI's annual City/State Construction expenditures, if such expenditures exceed the forecast by more than 20%. KEDLI claims that the current rate plan does not preclude it from seeking to establish new deferral mechanisms.

VERIFIED PETITION

KEDLI claims that it is committed to maintaining the integrity of its gas distribution system despite its accounting system implementation difficulties. The Company, therefore, seeks to implement mechanisms that will enable it to proceed with a three-year capital program of over $700 million without having to file for new base rates to support that investment (see Attachment II, page 3).

KEDLI's petition describes a capital program that includes: (1) the proactive replacement of over 250 miles of leak prone pipe; (2) the installation of over 180 miles of new gas main associated with customer growth; (3) the commencement of service to more than 33,000 new gas accounts; (4) the completion of installation of 568,000 storm resilient automated meter reading (AMR) devices; (5) enhanced gas supply opportunities arising from completion of the Brooklyn/Queens interconnect project (a major transmission project); (6) lower energy costs, enhanced economic development and job creation, and reduced emissions of greenhouse gases from new gas customers converting from oil to gas heat; and (7) continuation of a base rate freeze that has been in place since 2008. The Company states that a new accounting mechanism is necessary so that it can proceed with its proposed ramp up of capital spending to achieve the aforementioned objectives while preserving its ability to earn compensatory returns.

In making its request, KEDLI references recent gas pipeline safety incidents, such as the explosions in San Bruno, California and Allentown, Pennsylvania, that have increased the focus of the industry, its regulators and the general public on gas pipeline safety. The Company states that during a period in which the cost of debt is relatively low, local distribution companies and other owners and operators of natural gas delivery infrastructure across the country are being incented to accelerate the replacement of aging gas infrastructure, especially for infrastructure that is most prone to producing leaks.

Second, the Company states that recent weather events such as Superstorm Sandy and Hurricane Irene have also served to encourage natural gas distributors operating in areas that are vulnerable to storms and flooding to look for ways to protect their facilities from severe weather events. The impact of recent storms on KEDLI's infrastructure has caused it to study the ability of its distribution system to withstand extreme weather impacts and the general resilience of its infrastructure. Based on its review, the Company has developed plans to harden its infrastructure, providing for greater protection of its critical assets from future storms.

Third, the Company notes that the current service conditions and environment are very different from when we ordered its last rate plan in 2007. KEDLI points to the heretofore unprecedented increase in the availability of relatively low cost natural gas as particularly conducive to the growth of the natural gas distribution business from both an economic and security/reliability perspective.

In KEDLI's service territory, 43% of its customers use natural gas for heating. This low percentage of heating customers, as compared to New York's other natural gas distribution companies, makes KEDLI's service territory unique in its opportunity for growth in the Company's service territory.

Based on all the foregoing, KEDLI claims that it is in the best interests of the Company and its customers to significantly increase capital spending to modernize its transmission assets, increase the size and scope of its infrastructure replacement and storm resiliency programs, and develop its distribution network. Thus, KEDLI proposes to invest capital at substantially increased levels during the fiscal years[3] (FY) 2015-2017, consisting of FY 2015 at $240.0 million, FY 2016 at $220.7 million and FY 2017 at $241.7 million (Attachment II, page 3).

KEDLI explains that the primary drivers of the proposed incremental expenditures in FY 2015 through FY 2017

[3] KEDLI's fiscal year spans a twelve-month period from April 1 of the current year to March 31 of the following year. For example, FY 2015 spans the twelve-month period beginning April 1, 2014 and ending March 31, 2015. The FY 2015-2017 period begins on April 1, 2014, and ends March 31, 2017.

are: (1) enhanced proactive main replacement; (2) increased expenditures for pipeline integrity projects; (3) system reinforcement, reliability and pressure regulating projects; (4) enhanced growth-related spending for new mains and services; (5) continued City/State Construction requirements; and (6) the installation of storm-resilient AMR equipment. KEDLI claims that its increased capital spending program will provide significant safety, reliability and service improvements to its existing and future customers, while allowing it to further develop its distribution network to meet customer demand.

Leak Prone Pipe Replacement

KEDLI has had a proactive program to replace leak prone pipe in place for a number of years. The Company has approximately 3,927 miles of leak prone pipe in its transmission and distribution system and is currently required to replace, on an annual basis, 50 miles of leak prone pipe.[4] The Company proposes to accelerate the pace of this program to improve public safety and system performance. By accelerating the removal and replacement of leak prone pipe, the Company expects reduced leaks and anticipates that it will nearly cut in half the number of years that it will take to completely replace its leak prone pipe inventory.

The Company has prioritized the replacement of aging and deteriorating infrastructure on its distribution system and, more specifically, proposes to replace 70 miles of leak prone pipe in FY 2015, 80 miles in FY 2016 and 100 miles in FY 2017.

[4] KEDLI explains that leak prone pipe includes all (i) unprotected (i.e., noncathodically protected) steel pipe whether bare or coated, (ii) cast and wrought iron pipe, and (iii) pre-1985 Aldyl-A plastic pipe.

The Company projects it will achieve its proposed leak prone pipe mileage goals for removal via its construction work covered within six budget categories: leak prone pipe pro-active replacement, City/State construction, reliability and reinforcement, leak/reactive main replacement, water intrusion and storm hardening.

KEDLI explains that it will continue to prioritize segments of distribution main for replacement using a risk ranking algorithm that calculates a relative risk score for leak prone pipe segments based on specific performance data and localized incident probabilities and consequences. As part of its risk assessment, KEDLI states that it will target replacement of main located in flood prone areas to harden the system against future weather events, in addition to looking for synergistic opportunities when it develops and implements its capital investment plans.

Pipeline Integrity

KEDLI states that its transmission pipeline Integrity Management Plan (IMP) is a federally mandated safety program, established in response to the Pipeline Safety Improvement Act of 2002, with the purpose of identifying and addressing defects affecting the physical soundness of Company facilities before they become safety/performance problems. The IMP requires the Company to conduct baseline and periodic reassessments of its transmission facilities to identify and evaluate potential threats that could affect High-Consequence Areas in the event of a pipeline failure, as well as remediation of significant defects discovered during such assessments. The Company explains that the tests and inspections are an operating expense, but capital work is required to support in-line inspections (e.g., installation of pig launchers and receivers, and pipe reconfiguration/replacement) and to resolve issues discovered during pipeline inspections. KEDLI forecasts the related FY 2015 through FY 2016 capital work will increase the amount of its transmission system that can be made subject to in-line inspections from 17% to 40%.

System Reinforcement, Reliability and Pressure Regulation Projects

KEDLI states that its system reinforcement program consists of projects intended to ensure that minimum system design pressures are maintained throughout the gas network during periods of peak demand, as a result of firm customer growth that has occurred over the last several years. The Company is slated to complete a number of projects to ensure its ability to meet those peak requirements which will enhance its ability to maintain reliable service. KEDLI claims that the reinforcement projects are essential to its efforts to serve growing demand in eastern Long Island, the Hicksville/Westbury area and the Rockaway Peninsula.

KEDLI reports that it recorded eight of its top ten daily sendout totals during the winter of 2013-2014, including a record sendout for firm load of 923,350 dekatherms on January 7, 2014, a day during which KEDLI experienced a system wide average temperature of 9 degrees Fahrenheit. The Company points out that recent growth in peak sendout supports the need to ensure that minimum system design pressures can be maintained throughout the distribution network during periods of peak demand. The completion of the proposed reinforcement and pressure regulation projects will ensure that KEDLI is capable of satisfying the requirements of its current customers, as well as meeting the growing demand from new customers interested in converting to natural gas.

Growth-Related Spending

KEDLI states that there are more than 400,000 structures in its service territory without gas service, and another 100,000 non-heat customers. The Company explains that low commodity prices have led to a dramatic increase in the demand for natural gas service, particularly on the Rockaway Peninsula in Queens and in unserved areas of eastern Long Island. KEDLI further states that expanding the availability of gas service on Long Island can bring significant economic benefits in the form of energy cost savings, job creation and increased local tax revenues, as well as environmental benefits resulting from lower emissions. However, to serve new customers, KEDLI claims it must make significant capital investments in mains, services and related system reinforcements.

The growth-related capital spending included in the Company's current rate plan for CY 2012 reflected an assumption that KEDLI would be required to add approximately 30 miles of main and 5,000 services and meters to fulfill its legal obligation to support customer development, largely attributable to incremental conversions. In contrast, KEDLI's budget for FY 2015 through FY 2017 projects that it will be required to add 50, 60 and 70 miles of main and 8,650, 9,450 and 9,430 services in FY 2015, FY 2016 and FY 2017, respectively, to meet its customer addition goal of 33,000 new accounts by the end of FY 2017.[5]

KEDLI states that its forecast of growth capital expenditures reflects projected spending associated with a new

[5] KEDLI estimates that it will install 27,530 new services and some of those services will have multiple meters. The Company, therefore, projects it will have 33,000 new gas accounts at the end of FY 2017.

Neighborhood Expansion Program under which the Company would utilize geospatial, engineering, main, supply, customer interest, customer load and other data in its modeling to identify promising locations for development projects – streets or neighborhoods where prospective customer density would support entitlements-based main extensions (i.e., locations with not less than eight potential customers per 500 feet of main). Once these areas are identified, the Company proposes to secure commitments from a threshold level of customers to justify the capital investment in the infrastructure necessary to serve the area.

KEDLI proposes that if it is able to secure commitments to proceed from enough customers to cover at least 60% of the cost of the main extension, it will proceed with the project without charging Contributions In Aid of Construction (CIAC). It also would then market gas service to additional customers in the area to achieve the entitlement coverage for the main investment and to maximize customer conversion rates. KEDLI notes that its proposed Neighborhood Expansion Program is functionally identical to a program that has been deployed on a pilot basis by Niagara Mohawk Power Corporation (NMPC) as part of the Gas Growth Collaborative that was part of Case 12-G-0202.

Approximately 85% of these new gas customers are conversions (primarily customers converting from oil to natural gas) with the other 15% comprised of new construction projects. The Company claims that the Neighborhood Expansion Program will increase the annual conversions in KEDLI's service territory over three years by 150, 450, and 930 customers, respectively. Additionally, the program will result in the construction of gas main capable of serving another 3,000 potential customers.

KEDLI claims that its efforts to promote increased customer growth will provide significant societal benefits in the form of energy savings to its customers, reductions in emissions of greenhouse gas, and increases state and local tax revenue.

City/State Expenditures

The Company performs City/State Construction work to accommodate state or municipal construction activity that could threaten the integrity of the Company's natural gas facilities. Such work includes water, sewer, and drainage infrastructure projects, street reconstruction, road realignment and bridge replacement. KEDLI's budgeted expenditures are estimated based on a review of the known and planned work identified by governmental authorities and take into account historical work volumes and unit cost information.

AMR

KEDLI is currently installing AMRs throughout its service territory and expects to complete the entire conversion program in FY 2017. KEDLI states that it is implementing AMRs at this time because it no longer has access to the shared meter reading workforce that previously read both electric and gas meters on Long Island because of the ended working agreement between KEDLI and the Long Island Power Authority (LIPA).

KEDLI claims the installation of AMRs will decrease the incidence of estimated bills that require later adjustment and erroneous bills that require cancellation and rebilling. KEDLI also claims that the AMR installation will enhance storm resiliency and improve customer service. In the aftermath of major storms such as Superstorm Sandy, meters are often not read for some period of time during restoration activities because the Company needs to use the meter reading workforce to assist in storm recovery. Moreover, manual meters in flood prone areas are more vulnerable to storm damage than AMRs. With AMRs, the Company states that it can confirm remotely if the customer is using gas regardless of whether the customer is at home. Also, the AMR devices can store forty days of hourly data, which assists in resolving billing disputes or with service restoration issues following extended outages.

Defer the Costs of KEDLI's Expanded Capital Program

KEDLI is forecasting returns on equity for calendar years 2014, 2015 and 2016 of 6.6%, 5.9% and 5.5% (assuming a 45% equity ratio) respectively (see Attachment 1, page 1 of 8), reflecting the proposed capital spending program but without a deferral mechanism.[6] The new deferral mechanism would permit for the deferral, for future recovery in rates, of the pre-tax revenue requirement (including the related book depreciation expense and carrying costs totaling $56.7 million for the proposed three-year period) associated with the $700 million capital spending program to the extent that the amount of such investment exceeds the level of book depreciation expense currently reflected in rates.

KEDLI also informs us that it is forecasting returns on common equity for calendar years 2014, 2015 and 2016 of 6.65%, 6.99% and 7.65% (assuming a 45% equity ratio) and 6.45%, 6.78% and 7.39% (assuming a 48% ratio) after reflecting the $56.7 million deferral (see Attachment 1, page 2 of 8). In addition, KEDLI is proposing to eliminate the existing City/State Construction and Non-Growth Related Capital deferral mechanism because they would be duplicative should we approve the proposed new deferral mechanism.[7]

[6] Verified petition at 16, 18.

[7] See verified petition at 17-18.

Incremental Revenue Sources

The Company proposes to reduce the impact the deferrals may have on future base rates by offsetting them with new or incremental sources of revenue. KEDLI also opined that revenues from certain new charges being assessed to electric generation customers under Service Classification (SC) Nos. 7 and 14 could be used to reduce the deferral balance. Another possibility offered by the Company is that a portion of pipeline refunds or the customers' share of off-system sales margins and capacity release credits be used for deferral balance mitigation, particularly if these refunds/margins/credits increase over the next few years.

KEDLI requests that we afford the Company the flexibility to advance proposals to use new or expanding revenue sources to reduce its future deferred cost balance. KEDLI also proposes that any customer share of revenues from charges assessed to electric generation customers taking gas service, off-system sales and capacity release, estimated at $27.2 million be used as offsets.[8]

According to the Company, if it files for a gas base rate increase effective January 1, 2017, assuming the forecasted capital expenditure revenue requirement deferrals mirror actual results, there will be a deferral balance of $29.6 million after reflecting the $27.2 million of offsets,[9] plus an additional revenue requirement of $35.9 million to reflect the increase in rate base for the capital expenditures receiving deferral treatment (CYs 2014-2016) which will need to be recovered from customers. Under the Company's proposal, if base rates were to

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[8] See verified petition at 19.

[9] The deferral balance forecast is $56.7 million absent any mitigation.

be reset on January 1, 2017, there would be an increase in base delivery rates for residential customers of 7.30% (assuming the deferred costs are amortized over a three year period), resulting in a 3.7% residential bill impact.

The current KEDLI rate plan allows for an equity return of 9.8% with an equity ratio of 45%.[10] KEDLI is proposing to update its cost of capital for carrying charges on the deferred capital expenditures, increasing the equity ratio to 48% with an allowed return on equity of 9.4%.[11] On a pre-tax weighted average cost of capital basis, the current allowed return on equity of 9.8% (at a 45% equity ratio) is equivalent to an allowed return of 9.4% (at a 48% equity ratio).

KEDLI is further proposing that two caps be applied to the new deferral mechanism. First, the capital expenditures eligible for deferral treatment be capped at $700 million for FYs 2015 through 2017.[12] Second, KEDLI would not be permitted to defer pre-tax revenue requirements on capital expenditures in any year its return on equity exceeds 9.15% using a 48% equity ratio.[13]

As part of its proposal, KEDLI anticipates continuing the Joint Proposal’s earnings sharing provision for the CYs 2014, 2015 and 2016. KEDLI’s rate plan provides for various levels of sharing between customers and shareholders for earnings above a 10.50% return on equity (45% equity ratio). In its petition, KEDLI proposes to limit the revenue requirement deferrals in any year its return on equity exceeds 9.15% (48%

[10] Verified petition at 17, n.25.

[11] Verified petition at 17.

[12] Verified petition at 17 and Exhibit A.

[13] Verified petition at 17.

equity ratio). This proposed treatment of capital expenditure revenue requirements would prevent KEDLI's earned return on equity from exceeding 9.15% at a 48% equity ratio, or 9.53% at a 45% equity ratio. As either level is well below the rate plan's initial sharing threshold of 10.50%, KEDLI's proposal effectively eliminates any sharing under the existing rate plan's terms.

PUBLIC COMMENTS

A Notice of Proposed Rulemaking was published in the State Register on July 16, 2014, in accordance with State Administrative Procedure Act (SAPA) §201(1) (NY DOS SAPA No. 28-14-00012-P). The comment period expired August 30, 2014. Comments were received on August 27, 2014 by the City of New York (NYC).

In its comments, NYC first notes that its June 2013 report on the City's resiliency to extreme weather and other events identified natural gas local distribution companies as owning infrastructure in need of reinforcement and storm hardening measures (Resiliency Report). NYC also notes that the Resiliency Report's recommendations for natural gas distribution systems were based on KEDLI's experience with storm related outages and damage in the Rockaways from Superstorm Sandy. Thus, NYC agrees that KEDLI needs to make capital investments in its system to improve safety and reliability, including those investments identified in KEDLI's verified petition.

Notwithstanding its desire to see KEDLI make the capital improvements, NYC observes that a rate proceeding, rather than a deferral petition, is the proper mechanism for considering an investment program of the magnitude proposed by the Company. NYC also states that the issues with using a deferral as the method by which to seek relief for an increased capital budget are compounded by KEDLI's implication in its three-year proposal that it intends not to file a proper rate case for another three years.

NYC comments that some of the problems with addressing KEDLI's capital needs through a deferral petition include not being able to review the specific projects KEDLI will undertake, KEDLI's prioritization for the proposed work and whether such work is appropriate, whether the proposed costs are properly considered incremental, or if offsetting adjustments could be made to other portions of KEDLI's capital budget to eliminate or reduce the deferral. In addition, NYC notes that there is no justification for the 9.4% return on equity proposed by KEDLI by which to measure its deferral, and that such amount appears excessive when compared to other recent Commission ordered returns.

Despite the foregoing issues, NYC agrees that, given the necessity of such work, it should not be delayed while the Company prepares a rate case, but that the Commission should adopt measures to protect customers in the event that the Commission makes later determinations that KEDLI did not need incremental funding for its proposed programs, or in the case that the Commission determines that the work performed was not appropriate.

For such protections, NYC recommends making the deferral on a temporary basis only such that the Commission could provide refunds should the desire for such become evident at a later date. NYC also recommends that the Commission limit any such deferral authority to 18 months to two years, by which time KEDLI should be able to develop a rate case. NYC then recommends that the Commission establish a 9.0% return on equity for the temporary deferral authority with the Company, in its next rate filing, able to present evidence as to why a higher return should have been granted, but with the opportunity for other parties to challenge the Company's showing.

NYC's comments also note the potential applicability of PSL §66(12), indicating that the Company's request may require rate case treatment inasmuch as its request might increase the Company's aggregate revenues by greater than two and a half percent. As such, the Company's request would require a hearing.

DISCUSSION

KEDLI seeks our approval to implement accounting mechanisms that will enable it to proceed with a three-year capital program of over $700 million. The Company's capital program includes the proactive replacement of over 250 miles of leak prone pipe, the installation of more than 180 miles of new gas main and the commencement of service to more than 33,000 new gas accounts.

Under normal circumstances, the Company would file for rate relief and the magnitude of the requested increase would trigger a major rate proceeding under Section 66(12) of the Public Service Law. It is in that context that we would review the Company's proposed capital plan.

Over the last two years, however, KEDLI's parent National Grid has experienced severe problems and cost over runs associated with the implementation of it software based SAP financial system. As a result of its ongoing implementation difficulties, National Grid has been unable to consistently access and verify accurate accounting data for its affiliates. These accounting issues have prohibited KEDLI from filing required reports with the Commission in a timely manner. More relevant to our purposes here, these issues have precluded KEDLI from developing an accurate test year, rendering it unable to file for a base rate increase to address the capital investment needs of the Company's gas system.

KEDLI states that, as of October 2014, the accuracy of the data produced through its US Foundation Project can be relied upon in a rate case. To prepare a case before filing for new rates, however, KEDLI must have a full year of test data unaffected by its previous accounting issues. Once the Company files its case, new rates would not become effective for approximately 11 months thereafter during which time the Company's filing is subjected to, among other things, discovery by interested parties, opposing testimony, an opportunity to reply, and hearings, whether on the full litigated record, or on the merits of a joint proposal resulting from settlement negotiations. Therefore, allowing for a full rate case to proceed, the earliest we could deal with KEDLI's capital investment plan is approximately January 1, 2017. The Company is simply not in a position to file for rate relief. The Company's mostly self-created problems with its accounting books and records, however, cannot be allowed to put customers at risk or leave them without the opportunity to obtain gas service through distribution network development. Consequently, in this Order, we address and implement mechanisms so that KEDLI can make investments that will serve the interests of its customers and allow it to continue to provide safe and adequate service.

KEDLI is, in fact, proposing to make significant investment in its gas distribution system to address and improve the condition of the system. Despite KEDLI's distribution system having the largest type three leak backlog in the state and, at 3,927 miles of existing leak prone pipe, 32% of all existing leak prone pipe in the state, the Company's current rate plan, established in 2007, requires that it replace only 50 miles of leak prone pipe per year.

Moreover, there are more than 400,000 structures without gas service and another 100,000 low use non-heat customers in KEDLI’s service area. With the commodity price of gas projected to remain low, further developing the distribution network will benefit communities served by KEDLI and promote energy affordability. Such benefits to the local communities will be realized in the form of significant energy savings, job creation, lower emissions by switching from oil to natural gas, and similar tangible impacts.

We have reviewed the Company’s proposed capital plan and believe it is reasonable at this time. We appreciate that the program is designed to further our policy goals of enhancing system reliability and safety, particularly in the acceleration of removing leak prone pipe from the distribution system. We note here, however, that we fully expect the Company to propose in its next base rate filing further acceleration in its leak prone pipe removal and replacement along with proposed solutions to the challenges that the ramp-up creates.

In this Order, we are directing KEDLI to undertake a majority of its proposed capital program for the next two calendar years in accordance with the discussion contained herein. For the balance of its capital needs related to those programs we are ordering KEDLI to undertake, our Order today creates an Exogenous Cost under the Company’s existing rate plan. As such, KEDLI is entitled to deferral treatment of such costs.[14] To address the Company's capital needs for making the investments and to minimize future customer bill impacts, we anticipate creating a 21-month surcharge mechanism capped at $23.4 million dollars, cumulatively, to recover carrying costs associated with the removal of leak prone pipe. Moreover, we find that the intervening years and the extraordinary circumstances presented to us here have made it necessary for us to revisit the terms under which the Company's deferral mechanism created in the merger Joint Proposal operates.

Although we could call the Company in for a rate review, we find the exercise of such authority would create more problems than it would solve given the Company's financial reporting difficulties. Accordingly, we find cause to modify the Company's rate plan Exogenous Cost deferral mechanism, as well as certain gas safety metrics and their associated revenue adjustments.

As some of the items we contemplate today were not included in the Company's verified petition, such as the surcharge and the associated gas safety metrics changes, we will require the Company to make a filing of tariff leaves for such surcharge that will be sent out for public comment pursuant to SAPA. In the SAPA notice, we will include our intention to consider changes to the Company's rate plan for its gas safety metrics, thereby affording the public with fair notice and an opportunity to be heard on these additional matters. After such

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[14] Under Section X.C.5 of the July 6, 2007, Merger and Revenue Requirement Joint Proposal, adopted by our September 17 Order, the Company is entitled to defer "one hundred percent of all costs … associated with or caused by … any legislative, court or regulatory change, which imposes new or modifies existing obligations or duties." Our directives here create such a regulatory change by modifying an existing KEDLI obligation or duty.

comment period has ended, we anticipate releasing an Order discussing the Company's tariff filing for the surcharge, as well as any modifications we may find necessary to the Company's rate plan.

As discussed in more detail below, we believe that this result strikes a fair balance between the needs of the Company and the needs of its ratepayers, as well as the potential customers that may be added through capital investments. That being said, we stress that this relief is extraordinary in nature and that our action here is not intended to create a departure from established precedent disfavoring authorization for future deferral. We take this action only because of our desire to see the Company make strides to fulfill our policy goals, but recognizing that our preferred method of reviewing all the Company's rates would result in frustration and uncertainty for all. We also assure the Company's customers that our action today is not our final word on the actual costs incurred. For the surcharge, to the extent that we later find the costs incurred to have been duplicative or otherwise unwarranted, they will remain subject to refund. As for any amounts placed into deferral, such expenditures will remain subject to audit in either the Company's next rate filing or whenever the Company petitions to begin collecting on the deferred balance.

Accordingly, we order the Company to undertake elements of its capital investment plan. In doing so, we recognize that our order creates a regulatory obligation that did not exist at the time of the Company's last rate plan, creating an Exogenous Cost eligible for deferral treatment. Given that existing deferral authority, we modify the rate plan to reflect the current regulatory environment. Other than the details discussed in this order and the future order we anticipate deciding on the surcharge tariff amendments, however, all other rate plan provisions continue pending a future rate review when the Company is finally able to file.

Capital Plan

KEDLI proposes a Capital Investment Plan that covers FY 2015 through FY 2017, including a forecast and plan for its capital budget on the basis of investment category. The Company plans to spend over $700 million over the next three fiscal years to address the current condition of its gas transmission and distribution assets.[15] The Company forecasts capital budgets of $240.023 million, $220.685 million and $241.725 million for FY 2015, FY 2016 and FY 2017, respectively (shown in Exhibit A of the verified petition and Attachment II). In comparison, the final year of KEDLI's last rate plan had a CY capital budget of $126.617 million, as shown in Attachment II, page 1 (excluding information technology, facilities and other expenditures).

The Company breaks down its budget into four categories: (1) mandated, (2) reliability, (3) growth and (4) non-infrastructure. KEDLI uses a combination of planning tools to specify and identify where investments should be made, and recognizes investments need to respond to customer requests and comply with statutory or non-discretionary requirements. The investment plan is comprised of both load-growth and non-load based projects.

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[15] The Company develops a five year Capital Investment Plan and then presents such plan to its Board of Directors in March of each year. The Board of Directors approves a capital budget for the upcoming fiscal year and takes note of the other annual capital plans.

Since KEDLI filed its petition, Department of Public Service Staff (Staff) has conducted an extensive review of KEDLI's proposed capital plan for FY 2015, FY 2016 and FY 2017 by budget category. During its review, Staff had multiple meetings with the Company, sent numerous information requests and made site visits to assess the condition of the gas network. Overall, Staff indicates that it supports the budgets and believes the Company's proposed investment levels are necessary and appropriate.

Although we find that the increased budget in KEDLI's capital plan is needed, much of the work, such as pipeline integrity, system reliability, and City/State construction is required by existing regulation or law. Our concern here is two-fold. Given KEDLI's standing relative to its peer utilities, the 50 mile per year replacement of leak prone pipe must be increased. Additionally, given the heretofore slower pace of distribution network development in KEDLI's service territory, KEDLI's investment in network development opportunities must be accelerated. We do not believe the minimum amounts included in either of these requirements sufficiently address the issues facing the Company. Our directives, expanding the minimum legal requirements imposed on the Company by existing law, therefore, best serve the public interest.

Herein, we will allow for two deferrals, one for the replacement of leak prone pipe and another for growth expenditures. These deferrals will be established for calendar years 2015 and 2016. We will cap the leak prone pipe capital expenditures at $211.728 million over the two year period and will also cap the growth expenditures at $202.964 million over the two year period (see Attachment II, page 5). These programs account for 87% of the calendar year 2015 capital budget and 92%

of the calendar year 2016 capital budget (see Attachment II, page 4).

Joint Proposal Deferral Provisions

KEDLI proposed to eliminate the existing City/State Construction and Non-Growth related capital deferral mechanisms because they would be duplicative. As we are not approving the Company's proposal as filed, however, we must consider the impact of our actions on the existing City/State Construction and Non-Growth Related Capital deferral mechanisms.

The City/State Construction deferral mechanism allowed the Company to defer, to its Balancing Account, the full revenue requirement effect associated with the difference between the projected level of City/State Construction expenditures, net of reimbursements, for each calendar year and the actual capital spending for City/State construction, net of reimbursements, if that difference exceeded a 20% threshold. Should KEDLI's actual City/State construction expenditures exceed such threshold, it could make a filing that demonstrated the amounts were reasonable and beyond the Company's control.

The Company forecasts in it petition that more than 70% of its City/State capital expenditures include the removal of leak prone pipe. To further our goals of removing the Company's leak prone pipe inventory, we will eliminate this deferral mechanism. More details regarding our cost recovery mechanisms and associated mileage requirements for leak prone pipe capital expenditures are discussed below.

The Non-Growth related capital deferral mechanism was included in the last rate order as an important customer protection to incorporate in the Company's rate plan a method by which is similar to the Net Plant true-ups established in all of our rate orders for major gas utilities. Prior to a fairly standardized capital expenditure true-up mechanism, delivery rates would be set based upon a forecast of plant in service in the rate year. If the expenditures were not made, all else equal, the customers' rates would have been set too high and the utility would have higher profits. Thus, the Non-Growth related capital deferral mechanism protects customers by crediting them with the carrying charges of forecast investments that were not made.

In this proceeding, delivery rates are not being adjusted and customers will only pay for the actual level of investments made in CYs 2015 and 2016 through the new mechanisms we establish herein. However, we believe that there needs to be a minimum level of investment made in order to provide safe and adequate service and to incent the Company to make its base investments. We, therefore, will continue the Non-Growth related capital deferral provision.

Leak Prone Pipe Replacement

Leak prone pipe is generally considered steel pipe that is unprotected, cast iron pipe and some vintages of plastic pipe that can become brittle. Unprotected pipe is pipe that lacks adequate coating and cathodic protection rendering it vulnerable to corrosion. Data collected by Staff and the United States Department of Transportation shows that corrosion is a leading cause of natural gas pipe leakage. Additionally, leaks on underground piping can create safety risks to the public and can, in some instances, lead to potentially hazardous incidents.

Thus, it is in all KEDLI customers' best interest, and in the public interest at large, for the Company to accelerate its leak prone pipe replacement program. Such acceleration will uncontrovertibly improve system safety and reliability. Moreover, because the Company uses a risk-based algorithm for determining what pipe to prioritize for removal, it asserts that it can target leak prone pipe in flood prone areas maximizing reliability benefits and achieving some measure of storm hardening in the process.

Our goal is to have the gas utilities remove and replace inventory of leak prone pipe as quickly as possible, while acknowledging rate impacts to customers and the challenges the gas utilities face with a significant acceleration in their replacement programs. The Company proposes to replace 70, 80 and 100 miles of leak prone pipe in FY 2015, FY 2016 and FY 2017, respectively. The mileage targets proposed by KEDLI represent a 40%, 60% and 100% increase over the current target which will result in halving the current number of years to remove the entire leak prone pipe inventory (75 years to less than 38 years).

The challenges the Company faces in ramping up the program include securing sufficient internal and external labor, municipal permitting and material availability. Also, an accelerated leak prone pipe replacement program may compete with utility resources for distribution network development efforts and obligations to provide service. We accept the Company's proposed ramp up for CY 2015 and CY 2016, and we believe that even more acceleration in the future is necessary to adequately address KEDLI's service area needs.

Further, we have standardized the measurement of the removal of leak prone pipe for New York State gas utilities to be on a calendar year, and we will continue this practice for the targets we now impose on KEDLI. Consequently, we direct the Company to replace 77.5 miles of leak prone pipe in CY 2015 and 95.0 miles in CY 2016 and authorize it to spend up to its forecasted budget of $211.728 million over the two-year period to reach the number of replacement miles (see Attachment II, page 5). Additionally, we believe that the Company will continue to be able to increase the leak prone pipe program beyond 2017 by an additional 20 miles and require the Company, in its next filing addressing leak prone pipe removal, whether it be for rates or otherwise, to propose at a minimum the removal of 115 miles for CY 2017.[16]

We also find it necessary to review the negative revenue adjustments associated with the leak prone pipe replacement program. Pursuant to the terms of the Company's August 23 Order, if KEDLI fails to replace 50 miles of leak prone pipe in a calendar year it incurs a negative revenue adjustment of $480,000 per year. Likewise, if KEDLI fails to replace 4,000 bare-steel services in a calendar year, it incurs a negative revenue adjustment of $480,000.

Staff reports to us that the Company's bare steel services program is now complete. Thus, we will now eliminate that program requirement as it is no longer necessary. For the Company's leak prone pipe replacement program, we will modify the negative revenue adjustment should the Company fail to meet our new calendar year targets as we believe the existing level of adjustment is too low for such a critical public safety program.

To this end, we are considering a modification to the safety metrics applied to the Company as follows: as the service portion of the replacement plan is complete, we will combine the two incentive levels to bring the combined targets more in line with our existing current incentive levels for the removal of leak prone pipe imposed on KEDLI's peers. Thus, beginning in

[16] This requirement insures that we will be able to review the Company's progress at some point in 2016, whether it be in a rate filing, or through a filing requesting the extension of the surcharge and/or deferral we authorize in this order.

calendar year 2015, should the Company fail to replace the required annual miles of 77.5 miles in CY 2015 and 95.0 miles in CY 2016 in its service territory, it would incur a negative revenue adjustment of $960,000 in each year that it fails to meet the requirement.

We also believe that it is appropriate to review KEDLI's other gas safety performance targets and their associated revenue adjustments. KEDLI's existing gas safety performance targets were established in 2007 and, in many cases, the Company is currently held to a lower standard than other New York natural gas distribution companies because of the extended period of time it has gone without a rate filing.

Accordingly, we will consider imposing the following on the Company in our order when we take action on the Company's filing tariff leaves to create a surcharge to collect for its accelerated leak prone pipe removal program: updating the current gas safety targets in the areas of damages due to Mismarks, damages due to Company and Company Contractors, total damages, and emergency response times to leak and odor calls.

In addition, and consistent with measures adopted in other rate plans, including National Grid's two other operating companies in New York, we will examine KEDLI's large backlog of known leaks and likely impose a targeted reduction that should be aided by the ramp up of the leak prone pipe replacement program. Moreover, we anticipate including a violations performance measure to address any instances of non-compliance findings with the pipeline safety regulations. To address our concerns, KEDLI should examine all of these important gas safety performance measures and, when it files its tariff amendments to create the surcharge mechanism discussed herein, it should propose for our consideration reasonable and meaningful targets.

Network Development Investments

KEDLI claims it must make significant capital investments in mains, services and system reinforcements to serve new customers and realize the benefits of distribution network development stemming from low gas commodity prices. KEDLI claims that its efforts to promote increased customer growth will provide significant societal benefits in the form of energy savings to its customers, reductions in emissions of greenhouse gas, and increases in state and local tax revenue. We agree.

Staff's review of KEDLI's Neighborhood Expansion Program included an examination of the Company's historic customer additions and projected new services forecast. Staff advises us that the Company may have an optimistic forecast of new customer additions based on its proposed programs. An analysis of historical data shows that the Company has increased its total firm customers at a three year average rate of approximately 5,400 per year with approximately 3,900 additional residential non-heating customers per year converting to heating service. Furthermore, when customers are added, they create a need for system improvements to support the change in load to the distribution system. This observation is manifest in the Company's demonstration of recent growth in peak sendout. The Company must ensure that minimum system design pressures can be maintained throughout the distribution network during periods of peak demand.

The promotion of energy affordability is an important policy goal. Nearly 2.4 million New York households use fuel oil, kerosene and propane to heat their homes. These types of fuels are expensive and they produce significant greenhouse gases. Natural gas continues to have a price advantage that is projected to remain for the foreseeable future. Homeowners or businesses in KEDLI’s service territory that convert their heating system from #2 oil to natural gas can save hundreds of dollars a year and reduce emissions of carbon dioxide, with no production of sulfur dioxide.

Staff also reports that it receives many customer inquiries and complaints from customers who want gas service from KEDLI. While we believe that some of these inquiries could be alleviated through better communication from the Company, we also recognize that all too often the upfront costs create a barrier to distribution network development and without our intervention addressing such requirements, the Company cannot be as effective as it otherwise might be if the cost issues remain unaddressed.

We consequently direct the Company to implement its proposed Neighborhood Expansion program because it will aid in customer conversions to natural gas while testing KEDLI’s ability to identify potential neighborhoods, as well as its proposed approach to customer entitlements. The program will test the Company’s density and propensity modeling. Such modeling generates maps of potential gas load in relationship to the Company’s existing facilities, to assist the Company in determining potential areas for economic distribution network development by showing areas where the anticipated additional load is of sufficient size to justify network development. We are also interested to see how, over time, the Company’s marketing efforts help to achieve the projected levels of saturation in the development areas.

To further our policy goals to provide safe and reliable service, as well as create economic growth and lower air emissions, we direct KEDLI to undertake its proposed growth program and authorize it to spend up to its forecasted growth budget of $202.694 million over CY 2015 and CY 2016 to reach its forecasted number of customers (see Attachment II, page 5). The capital expenditure budgets include the Neighborhood Expansion program, modeled after Niagara Mohawk Power Corporation's (NMPC) program, in order to enhance customers' opportunity to connect to the distribution system.

As with our gas safety performance targets, we find that providing the Company with this extraordinary relief requires an incentive for the Company to achieve its stated goals of connecting new customers. We believe it is fair to allow the full deferral of carrying charges associated with growth and reinforcement capital expenditures if the Company meets its new accounts forecast (excluding non-heat to heat conversions) of 10,930 accounts in CY 2015 and 11,634 accounts in CY 2016 (see Attachment II, page 5). If the Company does not meet the new account goal each year, the allowed carrying charges will be reduced proportionally by the number of accounts under the target (see Attachment II, page 6 for a sample calculation).

Request for Deferral Treatment

Initially, we note that KEDLI's request for the deferral of forecast pre-tax revenue requirements rather than actual costs does not conform to our established deferral criteria:

1. The current standard for materiality is 5% of income available to shareholders.
2. Evidence that the costs were beyond management's control or could not have been reasonably forecasted in setting rates.
3. The reported earnings are on an adjusted ratemaking basis, and do not exceed the allowed return on equity.

Further, the deferral request is based upon a forecast of expenditures which are estimated to be made in CY 2014, CY 2015 and CY 2016. Because we do not authorize deferrals based upon estimates, rather, we authorize deferrals based upon the difference between the amount reflected in rates and the amount actually incurred, the Company's request to defer these costs would be considered premature.

For example, in Case 07-E-1533, we considered a similar petition filed by NMPC for pre-authorization to defer electric transmission and distribution investment costs for calendar years 2008 through 2010. The December 2007 petition requested a deferral based on forecasted future 2008 expenditures rather than any actual levels of past expenses. We declined NMPC's request reasoning that granting such would authorize deferrals based not on the difference between the amount reflected in rates and an amount actually incurred, but on future expenses not yet realized.[17] As a result, we considered the petition premature and directed NMPC to submit a future filing that included actual expenditures to supplement its deferral request. Subsequently, we did grant NMPC deferral treatment for the years 2008, 2009 and 2010, but for the actually incurred expenditures it was later able to demonstrate.

Thus, we would not usually grant a deferral in this situation, and we reinforce here that such continues to be our policy. In this case, however, exigent circumstances exist such that we want the Company to make these investments and, to do

[17] Case 07-E-1533, Niagara Mohawk Power Corporation – Petition for Deferral, Order on Deferral of Electric Transmission and Distribution Costs at 10 (issued September 5, 2008) (stating "we do not authorize deferrals based upon estimates; rather, we authorize deferrals based upon the difference between the amount reflected in rates and the amount actually incurred") (emphasis in original).

so, we need to direct KEDLI to make the proposed investments. Once we make this directive, however, the Company is entitled under the Exogenous Cost provisions of its rate plan to create a deferral mechanism it otherwise had to request permission for, absent our Order.

Such a deferral, however, brings with it additional costs to the ratepayers in the form of carrying charges for the time value of money that the Company would also be entitled to accrue so long as the balance remains deferred. Recovery of the additional costs plus carrying charges would then be included in the Company's next rate filing.

To avoid the potential for rate shock that could result from the deferral, especially given KEDLI's acknowledged difficulties in preparing and presenting a rate case, we believe a surcharge for at least a portion of the costs to be incurred is an appropriate mechanism to fund the Company's compliance with our Order (see Attachment II, page 7). The cost of the leak prone pipe program, estimated to be $23.6 million, should be recovered through a surcharge. The surcharge shall not exceed $23.4 million, and we anticipate it will begin April 1, 2015 and end December 31, 2016 following the filing, by KEDLI, of tariff amendments implementing such surcharge.[18]

For the balance of expenses, the Company, pursuant to our regulatory action, may create a deferral. Given our strong desire to see this work undertaken, and our directives to the Company to implement its capital plans, the Company's rate plan

[18] Capital Expenditures made prior to January 1, 2015 shall be excluded in the carrying charge calculation for CY 2015. The approximate $200,000 difference between the cost of the leak prone pipe project and the amount collected through the surcharge will be covered by the carrying charges customers should earn at the beginning of the surcharge period, when collections initially exceed program costs.

creates a form of future deferral that we would not otherwise consider. Through these means, we find that in this particular instance we can forego requiring that KEDLI file for rate relief inasmuch as such a filing could become an exercise in futility. Therefore, we find extenuating circumstances sufficient to modify the Company's rate plan, an action we are generally reluctant to take. In accordance with our action here, we will require KEDLI to file the accounting procedures it plans to have in place to track which expenses are recorded in the deferral categories, leak prone pipe surcharges, distribution network development and City/State expenditures. In addition, a reconciliation of the surcharges collected and the actual deferred costs incurred.

Surcharge Mechanism

In light of the foregoing, we believe that KEDLI's proposed accelerated leak prone pipe removal and replacement program is necessary to KEDLI's provision of safe and reliable service. As such, we hereby direct the Company to undertake the accelerated leak prone pipe removal program as outlined in its verified petition for the next two years, CY 2015 and CY 2016.

A forecasted surcharge calculation reflects the estimated calendar year revenues for 2015 (nine months) and 2016 of $10.0 million and $13.4 million respectively (see Attachment 1, pages 3 and 4 of 8), which accounts for book depreciation expense, and carrying costs at the pre-tax return on capital expenditures net of tax depreciation benefits (SIT and FIT) associated with the leak prone pipe replacement program.[19] The

[19] The tax depreciation benefits in the forecasted surcharge are based on currently-enacted tax rates and, should bonus tax depreciation be extended or re-enacted in the future, those tax benefits should be captured for customers.

estimated carrying costs are calculated using a pre-tax rate of return of 10.27% for 2015 and 10.23% for 2016 based on the most current cost of money information, assuming a three-year extension of the current rate plan and a 48% equity ratio, the return on equity equals 9.0%. This is an appropriate return given the current interest rate environment and comparable returns recently authorized by the Commission when considering the risks of the Company's operations and the duration of the work being ordered. The leak prone pipe surcharge should be calculated as follows: Average Capital Expenditures (associated with leak prone pipe) less Accumulated Depreciation less Accumulated Deferred Taxes (SIT and FIT) multiplied by the pre-tax rate of return plus the Annual depreciation expense on the plant additions divided by the projected annual base revenues.

Forecasting KEDLI's returns on equity for calendar years 2015 and 2016 and reflecting the growth investment deferral and surcharge earnings yields 6.57% and 7.50% (assuming a 48% equity ratio) and 6.77% and 7.76% (assuming a 45% equity ratio), respectively (see Attachment 1, pages 5 and 6 of 8).

The Company shall file proposed tariff amendments designed to collect from all firm customers the estimated carrying charges associated with the leak prone pipe replacement program beginning April 1, 2015.[20] In addition, the Company shall file an example of the surcharge calculation, the associated deferrals (over/under), the carrying charges, the accounting entries, and the accounting procedures that will identify and separate the deferrals for leak prone pipe surcharges and distribution network development deferrals, within sixty (60) days from the date of this Order.

[20] The surcharge shall exclude carrying charges and depreciation expense associated with leak prone pipe achieved in the city-state budget.

A reconciliation between actual surcharge revenue and the actual deferral will be conducted annually and filed with the Commission within sixty (60) days at the end of each calendar year. Any over-collection or under-collection will accrue interest at the pre-tax rate of return of 10.27% for 2015 and 10.23% for 2016. Adjustments for over-collections will be reflected in the next surcharge filing. This surcharge will sunset at the earlier of December 31, 2016, the Commission issues a decision in its next general rate case and approved rates are effective, or the Commission orders an end to the surcharge.

If KEDLI files for a gas base rate increase effective January 1, 2017, assuming the forecasted capital revenue requirement deferral mirror actual results, there will be $26.5 million deferral plus an additional revenue requirement of $23.9 million to reflect the increase in rate base for the capital expenditures receiving deferral treatment (CY 2015-CY 2016) which will need to be recovered from customers. The forecasted change in base delivery rates at that time, assuming the deferred costs are amortized over a three year period, is an increase of 5.21% (2.7% bill impact) for residential customers.

Deferral Mechanism

As indicated above, in requiring investments in growth expenditures, the Exogenous Cost under the Company's existing rate plan will be triggered. Specifically, the Company shall defer the pre-tax revenue requirements associated with growth expenditures, up to a maximum capital expenditure of $202.694 million made in CYs 2015 and 2016. Attachment 1, pages 7 and 8 of 8 show the deferrals which are forecast ($7.165 million in CY 2015 and $19.315 million in CY 2016). These deferrals reflect book depreciation expense and carrying costs at the pre-tax rate of return on capital expenditures net of tax depreciation benefits (SIT and FIT) associated with growth investments and neighborhood expansion made in these time periods.[21] The carrying costs are calculated using a pre-tax rate of return of 10.27% for 2015 and 10.23% for 2016 based on a 9.0% return on equity and a 48% equity ratio.

The Company shall file an example of the deferral calculation, the carrying costs, the associated accounting entries, and the accounting procedures that will identify and separate the deferrals for distribution network development, leak prone pipe expenditures and surcharge revenues, within sixty (60) days of the effective date of this Order.

Term of Surcharge and Deferral Authority

One of the issues raised by NYC in its comments concerned the term for which any such authority we grant to KEDLI be allowed to last. NYC urged that we allow such authority for only the time necessary for the Company to "develop, file and litigate a new rate case." We agree with NYC that the authority we grant here today requires some temporal sunset provision by which the Company should either have a new rate plan in place, or have to file for a renewal of the authority.

NYC recommended a period of 18 months to two years. We agree with NYC that two years should be enough time for the Company to get its financial records in order and to develop, file and litigate a rate case. In any event, we believe that the authority granted here today for both the surcharge

[21] The tax depreciation benefits in the forecasted deferrals are based on currently-enacted tax rates and, should bonus tax depreciation be extended or re-enacted in the future, those tax benefits should be captured for customers.

mechanism and deferral should not be allowed to last beyond that two years without providing us another opportunity to examine this extraordinary relief. Therefore, in the event that the Company is unable to secure a new rate order in such time, it should file a plan for continuing its leak prone pipe removal and any relief that it wants to recover the costs related thereto.

Other Revenue to Offset the Surcharge

In its petition, KEDLI requested that the Commission afford the Company the flexibility to use new or expanding revenue sources to reduce its future deferred cost balance, particularly if these refunds, margins, and credits increase over the next few years. The Company proposed several possible revenue sources that could be used to reduce its deferred balance: (1) revenues from certain new charges being assessed to electric generation customers under Service Classification Nos. 7 and 14, (2) a portion of pipeline refunds, (3) the customers' share of off-system sales margins, and (4) the customers' share of capacity release credits.[22]

The capital plan benefits all customers. However, the revenue sources that could be used to reduce the deferral may not be derived for both firm sales and firm transportation customers. Pipeline refunds are unknown and are passed back in the gas adjustment clause (GAC) to firm sales customers as the refunds arise. Off-system sales credits and capacity release credits derived from off-system capacity release transactions are passed back to firm sales customers only through the GAC as a credit to fixed gas costs. We, therefore, believe there would

[22] KEDLI currently shares off-system sales margins and capacity release credits with customers on an 85% customer/15% Company basis.

be a cross subsidy if these revenues were used to offset the carrying charges and depreciation expense associated with the deferral because firm transportation customers would avoid paying for the deferral, but would receive the benefits of the expenditures. We will deny the Company's request to use pipeline refunds, off-system sales or capacity release credits to offset the deferral.

Revenues from electric generation customers are credited to firm sales customers and to ESCOs that serve firm transportation customers at the same unitized per therm credit. Firm customers are credited through the GAC reducing fixed gas costs and to ESCOs via their monthly bill as a credit to swing service demand charges. Over the last five years, the average revenue from electric generation customers has been about $25.8 million. The Company estimates that not passing the revenues associated with electric generation customers will increase a typical residential heating customer's bill by $32 per year or 2%. The revenues from electric generation customers, therefore, could be considered a reasonable and fair offset to the growth capital expenditure deferral. However, due to our implementation of a surcharge for the recovery of carrying charges for leak prone pipe, we find that using the full amount of revenue from electric generation customers to offset the deferral would cause a bill impact that is too high. We also are concerned with the impacts of this deferral in a future rate case. We, therefore, will require that any revenue from certain new charges being assessed to electric generation customers under Service Classification Nos. 7 and 14 above $25.8 million be used to offset the deferral balance. Beginning April 1, 2015, the Company shall defer these revenues as an offset to the growth capital expenditure deferral and will accrue carrying charges at 10.27% for 2015 and 10.23% for 2016.

Earnings Sharing Mechanism

KEDLI anticipates a continuation of the current earnings sharing provision for 2014, 2015 and 2016 rate years. Currently, the KEDLI rate plan provides for various levels of sharing between customers and shareholders for earnings exceeding 10.5% return on equity (45% equity ratio). KEDLI proposes to limit the revenue requirement deferrals in any year its return on equity exceeds 9.15% (48% equity ratio) or 9.53% (45% equity ratio). The Company's proposed treatment of capital expenditure revenue requirements can never cause KEDLI's earned return on equity to exceed 9.15% against a 48% equity ratio, or 9.53% against a 45% equity ratio. Under the current rate plan, the 9.53% return on equity falls below the sharing threshold of 10.5%. We agree that the earnings sharing mechanism shall be modified to reflect the current cost of capital. Thus, KEDLI shall limit the revenue requirement deferrals in any year its return on equity exceeds 9.00% (48% equity ratio).

Reporting Requirements

With the new mandates to replace leak prone pipe and distribution network development, as well as creating new deferrals and allowing a new surcharge, it is important for Staff to monitor the Company's implementation of its investment plan. To that end, the Company shall make the following regular filings: (1) prior to the start of each CY; (2) quarterly during the CY; and (3) after the end of the CY.

Prior to the CY

A future deferral mechanism may relax the discipline the Company would normally have to control its capital costs to meet our goals. This predicament requires that the Company provide further reporting and monitoring. To that end, thirty days prior the beginning of the calendar year the Company will file its leak prone pipe prioritization summary identifying the proposed projects and their estimated costs. The Company shall file its CY 2015 leak prone pipe prioritization summary and a report on the total average accounts ending December 31, 2014 by month by service classification, on or before February 2, 2015.

In addition, we require the Company to create and submit to Staff on an annual basis a strategic implementation plan and progress report for its distribution network development initiative. The strategic implementation plan shall provide a three year forecast of projects included in the new distribution network development program and any franchise and/or major line extension projects not included in the Neighborhood Expansion program. The implementation plan shall include a summary for each project within the current and following year of the plan. Each summary shall provide a description of the project, location description and the resulting data of the density and propensity modeling. The progress report shall include the necessary resulting data for each completed project in order to gauge the success of the program. This shall include the customer growth rates and patterns associated with this distribution network development program.

The Company shall file an example of the deferral calculation, the carrying costs, the associated accounting entries, and the accounting procedures that will identify and separate the deferrals for distribution network development and leak prone pipe expenditures and surcharge revenue, within sixty (60) days of the effective date of this Order.

Quarterly Reports

The Company will submit a quarterly report to Staff detailing leak prone pipe removal mileage, main locations, ranking on the Company's risk model and costs, and the number of new customers, non-heat to heat conversions and Neighborhood Expansion customers. In addition, the Company should track inquiries for new service and show how the targeted Neighborhood Expansion Program was focused on those areas where the most inquiries came from. Moreover, KEDLI will report on the revenues from electric generation customers. The Company will submit these quarterly reports no later than 30 days following the three-month reporting periods ending March 31, June 30, September 30 and December 31.

After the CY

The Company shall file annually, within sixty days after the end of the calendar year, (1) a reconciliation between actual surcharge revenue and actual carrying charges, (2) an earnings report with any impacts from our revised earnings sharing mechanism, (3) the actual deferral from our approved capital expenditures, (4) a showing that the non-growth provision was exceeded, and (5) a report on total average accounts reported by month by service classification.

By June 1 of each year, the Company will file with the Commission a report on its capital expenditures during the prior fiscal year (to be consistent with the KEDNY rate case requirements). The report will include: (1) the capital costs incurred for each of the projects and programs; (2) a list of new projects and programs added to the Company's capital projects program during the fiscal year with an explanation as to why the project or program was included; (3) for each of the projects and programs in the Company's capital program, including any new or delayed/eliminated projects and programs, the actual amount spent as compared to the forecast amount in the Company's capital budget. The Company is also required to file the list of leak prone pipe projects it actually replaced in the calendar year in its June 1st report.

For any project or program where the actual cost varies from the forecast amount by more than 10 percent, the Company will provide an explanation of the variance. The report will also include a description of the Company's efforts to coordinate City/State Construction activities and the Neighborhood Expansion program with the rest of its capital programs during the prior fiscal year. The Company will also schedule a meeting with Staff and any interested parties to discuss the report within sixty days of filing with the Commission.

If the total average cost per mile exceeds the projections include in Exhibit A of its verified petition, the Company is to provide a detailed explanation for the costs overruns, and the excess carrying costs will not be allowed to be recovered from customers.

Likewise, where the capital expenditures associated with installing 8,650, 9,450 and 9,430 new services exceeds the projections included in Exhibit A of KEDLI's verified petition for its average cost per service, the Company is to provide a detailed explanation for the costs overruns. The excess carrying costs will not be allowed to be recovered from customers. Capping the unit cost is reasonable in this unique circumstance to force cost controls and synergistic opportunities.

CONCLUSION

KEDLI is directed to implement its proposed capital plan, to account for such costs through the mechanisms discussed herein, and to make the required filings consistent with the body of this order.

The Commission orders:

1. KeySpan Gas East Corporation d/b/a National Grid (KEDLI) is directed to replace 77.5 miles of leak prone pipe in calendar year (CY) 2015 and 95.0 miles in CY 2016. KEDLI is authorized to spend up to its forecasted budget of $211.728 million over the two-year period to reach the required number of replacement miles.

2. KEDLI, in its next filing, shall address its leak prone pipe removal program and propose, at a minimum, the removal of 115 miles for CY 2017.

3. KEDLI is directed to undertake its proposed Neighborhood Expansion and other related programs. KEDLI is authorized to spend up to its forecasted budget of $202.694 million over CY 2015 and CY 2016 to reach its forecasted number of accounts of 10,930 in CY 2015 and 11,634 in CY 2016.

4. KEDLI is directed to file, on not less than 30 days notice to become effective on April 1, 2015, tariff amendments creating a surcharge mechanism consistent with the discussion in this Order.

5. In its surcharge filing, KEDLI shall include a proposal to update its existing gas safety performance measures, including a proposal for a violations performance measure, as well as updated negative revenue adjustments for all of its measures.

6. KEDLI is directed to establish a new deferral accounting mechanism, consistent with the discussion in this Order, for the balance of the costs not covered by the surcharge.

7. KEDLI, within 60 days of this order, shall file an example of the surcharge calculation, the associated deferrals (over/under), the carrying charges, the accounting entries, and the accounting procedures that will identify and

separate the deferrals for leak prone pipe surcharges, distribution network development deferrals, and City/State expenditures.

8. KEDLI, within 60 days of this order, shall file an example of the deferral calculation, the carrying costs, the associated accounting entries, and the accounting procedures that will identify and separate the deferrals for distribution network development, leak prone pipe surcharge and the City/State expenditures.

9. The surcharge and deferral mechanisms created herein will expire as of January 1, 2017 absent any further action by the Commission to extend such mechanisms.

10. KEDLI's existing City/State deferral mechanism is ended as of January 1, 2015.

11. KEDLI's existing Non-growth deferral mechanism is continued.

12. All other provisions of the KEDLI's existing rate plan are continued, unless specifically modified herein.

13. KEDLI's proposal to use capacity release, off system sales and pipeline refunds to offset the deferrals established or continued in this Order is denied.

14. KEDLI is authorized to use revenues collected from electric generation to offset the deferrals established in this Order consistent with the discussion in this Order.

15. KEDLI is required to fulfill the reporting obligations established in the discussion in this Order.

16. In the event that KEDLI does not file for new rates to become effective by January 1, 2017, KEDLI shall file a plan, consistent with the body of this Order, for accelerating its leak prone pipe removal program for CY 2017 by August 1, 2016.

17. The Secretary may extend the deadlines set forth in this Order upon good cause shown, provided the request for such extension is in writing and filed on a timely basis, which should be on at least one day's notice, For any granted extension, the Secretary may also require status reports during the extension.

18. This proceeding is continued.

By the Commission,

(SIGNED) KATHLEEN H. BURGESS
Secretary

Case 14-G-0214

KeySpan Energy Delivery of Long Island
Estimated Operating Revenues , Expenses, Rate Base & Rate of Return
12 Months Ended December 31
$(000)

	2014 Estimated Amount Per Company	2015 Estimated Amount Per Company	2016 Estimated Amount Per Company
Operating Revenues:			
Margins	$ 534,829	$ 542,813	$ 550,924
Cost of Gas	331,890	336,845	341,878
Revenue Taxes	9,381	9,521	9,663
Other Operating Revenue	89,844	90,391	90,951
Total Operating Revenues	**$ 965,943**	**$ 979,570**	**$ 993,416**
Operating Expenses:			
Less: Purchased Gas & Other Gas Supply Expenses	331,890	336,845	341,878
Less: Revenue Taxes	9,381	9,521	9,663
Total - Cost of Gas & Revenue Taxes	**$ 341,271**	**$ 346,366**	**$ 351,541**
Net Revenues	**$ 624,672**	**$ 633,204**	**$ 641,875**
Other Operation &Maintenance Expenses (Less: Cost of Gas)	244,111	249,629	254,543
Depreciation	63,233	66,713	70,082
Amortizations	37,195	37,195	37,195
Taxes other than Income Taxes (Less: Revenue Taxes)	119,729	119,728	119,727
Total - Other Operating Expenses	**$ 464,268**	**$ 473,265**	**$ 481,547**
Operating Income Before Income Taxes	**$ 160,404**	**$ 159,939**	**$ 160,328**
State Income Tax	8,520	8,156	7,909
Federal Income Tax	31,573	30,222	29,309
Total - Income Tax	**$ 40,093**	**$ 38,377**	**$ 37,219**
Utility Operating Income	**$ 120,311**	**$ 121,562**	**$ 123,109**
Rate Base	**$ 1,960,718**	**$ 2,078,957**	**$ 2,180,887**
Rate of Return	**6.14%**	**5.85%**	**5.64%**
Return of Common Equity (@ 45% Equity Ratio)	**6.57%**	**5.93%**	**5.48%**

KEDLI'S PROJECTED COST OF SERVICE WITH CAPEX REVENUE DEFERRALS AS FILED
($000)

	CY 2014	CY 2015	CY 2016
Operating Revenues:			
Margins	$ 534,829	$ 542,813	$ 550,924
Cost of Gas	331,890	336,845	341,878
Revenue Taxes	9,381	9,521	9,663
Other Operating Revenue	89,844	90,391	90,951
Capex Revenue Requirement Deferral	1,134	16,737	35,893
Total Operating Revenues	**$ 967,077**	**$ 996,307**	**$ 1,029,309**
Operating Expenses:			
Less: Purchased Gas & Other Gas Supply Expenses	$ 331,890	$ 336,845	$ 341,878
Less: Revenue Taxes	9,381	9,521	9,663
Total- Cost of Gas & Revenue Taxes	**$ 341,271**	**$ 346,366**	**$ 351,541**
Net Revenues	**$ 625,806**	**$ 649,941**	**$ 677,768**
Other Operation &Maintenance Expenses (Less: Cost of Gas)	$ 244,111	$ 249,629	$ 254,543
Depreciation	63,233	66,713	70,082
Amortizations	37,195	37,195	37,195
Taxes other than Income Taxes (Less: Revenue Taxes)	119,729	119,728	119,727
Total - Other Operating Expenses	**$ 464,268**	**$ 473,265**	**$ 481,547**
Operating Income Before Income Taxes	**$ 161,538**	**$ 176,676**	**$ 196,221**
State Income Tax	$ 8,618	$ 9,600	$ 11,007
Federal Income Tax	31,935	35,574	40,788
Total - Income Tax	**$ 40,554**	**$ 45,174**	**$ 51,795**
Utility Operating Income	**$ 120,984**	**$ 131,502**	**$ 144,426**
Rate Base	**$ 1,960,718**	**$ 2,078,957**	**$ 2,180,887**
Rate of Return	**6.17%**	**6.33%**	**6.62%**
Return of Common Equity At 45% Equity Ratio	**6.65%**	**6.99%**	**7.65%**

Returns Calculated At 48% Equity Ratio

	CY 2014	CY 2015	CY 2016
State Income Tax	$ 8,923	$ 9,923	$ 11,346
Federal Income Tax	33,064	36,771	42,043
Total - Income Tax	**$ 41,987**	**$ 46,694**	**$ 53,389**
Utility Operating Income	**$ 119,551**	**$ 129,983**	**$ 142,832**
Rate Base	**$ 1,960,718**	**$ 2,078,957**	**$ 2,180,887**
Rate of Return	**6.10%**	**6.25%**	**6.55%**
Return of Common Equity At 48% Equity Ratio	**6.45%**	**6.78%**	**7.39%**
Return on Equity Cap	**9.15%**	**9.15%**	**9.15%**

Case 14-G-0214

KeySpan Energy Delivery of Long Island
Estimated Operating Revenues , Expenses, Rate Base & Rate of Return
(Surcharge - Leak Prone Pipes)
$(000)

	2015 Estimated Amount	2016 Estimated Amount
Revenues:		
Revenues for Book Depreciation	$ 1,749	$ 3,860
Revenues for Carrying Costs	4,346	13,702
Total Operating Revenues*	**$ 6,095**	**$ 17,562**
Depreciation	1,749	3,860
Total - Other Operating Expenses	**$ 1,749**	**$ 3,860**
Operating Income Before Income Taxes	**$ 4,346**	**$ 13,702**
State Income Tax	$ 265	$ 778
Federal Income Tax	984	3,117
Total - Income Tax	**$ 1,249**	**$ 3,895**
Utility Operating Income	**$ 3,097**	**$ 9,807**
Rate Base	**$ 42,321**	**$ 133,942**
Rate of Return	**7.32%**	**7.32%**
Return of Common Equity (at 48% Equity Ratio)	**9.00%**	**9.00%**

*2015 Revenues	$10,041
2015 Expenses	(6, 095)
Deferred Revenues	3,946
Carrying Cost	228
Total	$4,174

*2016 Revenues	$13,388
Deferred Revenues	4,147
Total	$17,562

Case 14-G-0214

KeySpan Energy Delivery of Long Island
Estimated Operating Revenues , Expenses, Rate Base & Rate of Return
(Surcharge - Leak Prone Pipes)
$(000)

	2015 Estimated Amount	2016 Estimated Amount
Revenues:		
Revenues for Book Depreciation	$ 1,749	$ 3,860
Revenues for Carrying Costs	4,346	13,702
Total Operating Revenues *	**$ 6,095**	**$ 17,562**
Depreciation	1,749	3,860
Total - Other Operating Expenses	**$ 1,749**	**$ 3,860**
Operating Income Before Income Taxes	**$ 4,346**	**$ 13,702**
State Income Tax	$ 259	$ 758
Federal Income Tax	959	3,040
Total - Income Tax	**$ 1,218**	**$ 3,798**
Utility Operating Income	**$ 3,128**	**$ 9,904**
Rate Base	**$ 42,321**	**$ 133,942**
Rate of Return	**7.39%**	**7.39%**
Return of Common Equity (at 45% Equity Ratio)	**9.36%**	**9.36%**

*2015 Revenues	$10,041
2015 Expenses	(6, 095)
Deferred Revenues	3,946
Carrying Cost	228
Total	$4,174

*2016 Revenues	$13,388
Deferred Revenues	4,147
Total	$17,562

KeySpan Energy Delivery of Long Island
Estimated Operating Revenues , Expenses, Rate Base & Rate of Return
12 Months Ended December 31
$(000)

	2014 Estimated Amount	2015 Estimated Amount	2016 Estimated Amount
Operating Revenues:			
Margins	$ 534,829	$ 542,813	$ 550,924
Cost of Gas	331,890	336,845	341,878
Revenue Taxes	9,381	9,521	9,663
Surcharge - Leak Prone Pipes	-	6,095	17,562
Gas Expansion - Revenue Requirement Deferral	-	7,165	19,315
Other Operating Revenue	89,844	90,391	90,951
Total Operating Revenues	**$ 965,943**	**$ 992,830**	**$ 1,030,293**
Operating Expenses:			
Less: Purchased Gas & Other Gas Supply Expenses	331,890	336,845	341,878
Less: Revenue Taxes	9,381	9,521	9,663
Total- Cost of Gas & Revenue Taxes	**$ 341,271**	**$ 346,366**	**$ 351,541**
Net Revenues	**$ 624,672**	**$ 646,464**	**$ 678,752**
Other Operation &Maintenance Expenses (Less: Cost of Gas)	244,111	249,629	254,543
Depreciation	63,233	66,713	70,082
Amortizations	37,195	37,195	37,195
Taxes other than Income Taxes (Less: Revenue Taxes)	119,729	119,728	119,727
Total - Other Operating Expenses	**$ 464,268**	**$ 473,265**	**$ 481,547**
Operating Income Before Income Taxes	**$ 160,404**	**$ 173,199**	**$ 197,205**
State Income Tax	8,825	9,623	10,636
Federal Income Tax	32,701	35,659	42,636
Total - Income Tax	**$ 41,526**	**$ 45,282**	**$ 53,272**
Utility Operating Income	**$ 118,878**	**$ 127,918**	**$ 143,933**
Rate Base	**$ 1,960,718**	**$ 2,078,957**	**$ 2,180,887**
Rate of Return	**6.06%**	**6.15%**	**6.60%**
Return of Common Equity (@ 48% Equity Ratio)	**6.38%**	**6.57%**	**7.50%**

Case 14-G-0214

Attachment 1
Page 6 of 8

KeySpan Energy Delivery of Long Island
Estimated Operating Revenues , Expenses, Rate Base & Rate of Return
12 Months Ended December 31
$(000)

	2014 Amount	2015 Amount	2016 Amount
Operating Revenues:			
Margins	$ 534,829	$ 542,813	$ 550,924
Cost of Gas	331,890	336,845	341,878
Revenue Taxes	9,381	9,521	9,663
Surcharge - Leak Prone Pipes	-	6,095	17,562
Gas Expansion - Revenue Requirement Deferral	-	7,165	19,315
Other Operating Revenue	89,844	90,391	90,951
Total Operating Revenues	**$ 965,943**	**$ 992,830**	**$ 1,030,293**
Operating Expenses:			
Less: Purchased Gas & Other Gas Supply Expenses	331,890	336,845	341,878
Less: Revenue Taxes	9,381	9,521	9,663
Total - Cost of Gas & Revenue Taxes	**$ 341,271**	**$ 346,366**	**$ 351,541**
Net Revenues	**$ 624,672**	**$ 646,464**	**$ 678,752**
Other Operation &Maintenance Expenses (Less: Cost of Gas)	244,111	249,629	254,543
Depreciation	63,233	66,713	70,082
Amortizations	37,195	37,195	37,195
Taxes other than Income Taxes (Less: Revenue Taxes)	119,729	119,728	119,727
Total - Other Operating Expenses	**$ 464,268**	**$ 473,265**	**$ 481,547**
Operating Income Before Income Taxes	**$ 160,404**	**$ 173,199**	**$ 197,205**
State Income Tax	8,520	9,300	10,321
Federal Income Tax	31,573	34,462	41,372
Total - Income Tax	**$ 40,093**	**$ 43,762**	**$ 51,693**
Utility Operating Income	**$ 120,311**	**$ 129,437**	**$ 145,512**
Rate Base	**$ 1,960,718**	**$ 2,078,957**	**$ 2,180,887**
Rate of Return	**6.14%**	**6.23%**	**6.67%**
Return of Common Equity (@ 45% Equity Ratio)	**6.57%**	**6.77%**	**7.76%**

Case 14-G-0214

KeySpan Energy Delivery of Long Island
Deferral - Distribution Network Development Plant
$(000)

	2015 Estimated Amount	2016 Estimated Amount
Costs:		
Book Depreciation	$ 2,056	$ 4,156
Carrying Cost	5,109	15,159
Total Costs	**$ 7,165**	**$ 19,315**
Depreciation	2,056	4,156
Net Operating Expenses	**$ 2,056**	**$ 4,156**
Operating Income Before Income Taxes	**$ 5,109**	**$ 15,159**
State Income Tax	$ 312	$ 860
Federal Income Tax	1,157	3,449
Total - Income Tax	**$ 1,469**	**$ 4,309**
Utility Operating Income	**$ 3,640**	**$ 10,850**
Rate Base - Deferral	**$ 49,743**	**$ 148,190**
Rate of Return	**7.32%**	**7.32%**
Return of Common Equity (@ 48% Equity Ratio)	**9.00%**	**9.00%**

Case 14-G-0214

KeySpan Energy Delivery of Long Island
Deferral - Distribution Network Development Plant
$(000)

	2015 Estimated Amount		2016 Estimated Amount	
Costs:				
Book Depreciation	$	2,056	$	4,156
Carrying Cost		5,109		15,159
Total Costs	**$**	**7,165**	**$**	**19,315**
Depreciation		2,056		4,156
Net - Other Operating Expenses	**$**	**2,056**	**$**	**4,156**
Operating Income Before Income Taxes	**$**	**5,109**	**$**	**15,159**
State Income Tax	$	304	$	839
Federal Income Tax		1,128		3,363
Total - Income Tax	**$**	**1,432**	**$**	**4,202**
Utility Operating Income	**$**	**3,677**	**$**	**10,957**
Rate Base- Deferral	**$**	**49,743**	**$**	**148,190**
Rate of Return		**7.39%**		**7.39%**
Return of Common Equity (@ 45% Equity Ratio)		**9.36%**		**9.36%**

KeySpan Energy Delivery of Long Island

Joint Proposal Capital Expenditures 2007-2012
($000)

Calendar Year	2007	2008	2009	2010	2011	2012
City/State	$ 8,479	$ 9,746	$ 9,746	$ 9,746	$ 9,746	$ 9,746
Non-Growth	$ 49,442	$ 72,091	$ 56,124	$ 58,113	$ 58,113	$ 58,113
Growth Capital	$ 39,189	$ 34,468	$ 32,609	$ 30,750	$ 30,750	$ 30,750
Safety Replacement Program	$ 13,071	$ 28,008	$ 28,008	$ 28,008	$ 28,008	$ 28,008
Islander East Alternative*	$ -	$ 23,000	$ -	$ -	$ -	$ -
Information Technology, Facilities, and Other Capital Expenditures	$ 20,081	$ 43,551	$ 11,359	$ 11,697	$ 11,697	$ 11,697
Total	$ 130,262	$ 210,864	$ 137,846	$ 138,314	$ 138,314	$ 138,314
Total Less IT, Facilities and Other Capex	$ 110,181	$ 167,313	$ 126,487	$ 126,617	$ 126,617	$ 126,617

* This amount shall increase to a total of $46.9 Million if construction is approved and completed for Islander East Project.

Source: JP 2, Appendix 3, Page 21

KeySpan Energy Delivery of Long Island

Historic, Actual and Forecast Capital Expenditures by Budget Category

($000,000's)

HISTORIC BUDGETS	FY10	FY11	FY12	FY13	FY14	Total
Development	$ 30.1	$ 44.9	$ 40.7	$ 40.7	$ 58.4	$ 214.7
Mandated	$ 77.3	$ 91.2	$ 93.2	$ 82.6	$ 97.3	$ 441.6
Reliability	$ 28.4	$ 6.6	$ 32.6	$ 33.3	$ 42.4	$ 143.2
Discretionary	$ 0.7	$ 1.2	$ 1.2	$ 1.1	$ 15.1	$ 19.3
TOTAL	$ 136.5	$ 143.9	$ 167.6	$ 157.7	$ 213.2	$ 818.8

ACTUAL SPENDING	FY10	FY11	FY12	FY13	FY14	Total
Development	$ 28.6	$ 44.1	$ 48.1	$ 70.0	$ 67.9	$ 258.7
Mandated	$ 86.9	$ 94.5	$ 85.8	$ 64.6	$ 58.6	$ 390.4
Reliability	$ 17.2	$ 7.7	$ 6.3	$ 7.8	$ 25.5	$ 64.6
Discretionary	$ 2.7	$ 0.9	$ 0.7	$ 2.3	$ 52.6	$ 59.2
TOTAL	$ 135.4	$ 147.3	$ 140.8	$ 144.7	$ 204.7	$ 772.9

COMPANY'S FORECAST	FY15	FY16	FY17	FY18	FY19	Total
Development	$ 107.0	$ 101.4	$ 106.2	$ 97.2	$ 99.5	$ 511.2
Mandated	$ 96.4	$ 106.9	$ 125.0	$ 157.2	$ 184.7	$ 670.2
Reliability	$ 35.5	$ 11.3	$ 9.3	$ 9.2	$ 9.2	$ 74.5
Discretionary	$ 1.1	$ 1.2	$ 1.2	$ 1.2	$ 1.2	$ 5.9
TOTAL	$ 240.0	$ 220.7	$ 241.7	$ 264.8	$ 294.6	$ 1,261.9

Notes:

The historic FY 14 Discretionary budget included $14 million for AMR.

The actual FY 14 Discretionary spending included $15 million for AMR, $20 million for Super Storm Sandy and $16 million for US Foundations.

The forecasted FY 15 Reliability budget includes $19 million for AMR.

KeySpan Energy Delivery of Long Island

Forecast Capital Expenditures Detailed by Budget Category

'($000)

	FY 2015 Forecast	FY 2016 Forecast	FY 2017 Forecast	FY 2018 Forecast	FY 2019 Forecast
Development					
Main & Service Install (incl Cust Contribution)	55,261	59,227	60,685	66,036	68,244
Neighborhood Expansion Program (Main/Services)	2,796	8,689	16,102	17,719	19,540
Meter Purchase & Installation	2,844	2,998	2,999	3,316	3,437
Gas System Reinforcement (planned)	18,836	10,478	6,851	6,900	5,060
LI East End Reinforcement Program	19,783	19,964	19,569	3,200	3,200
Hicksville / Westbury Reinforcement	7,511	-	-	-	-
Total Development	**107,031**	**101,356**	**106,206**	**97,171**	**99,481**
Mandated					
City/State Construction	9,089	9,629	9,366	10,492	10,492
Proactive Main Replacement (53mi, 72mi, 92mi, 112mi, 132mi)	54,320	73,793	94,846	124,186	149,149
Proactive Service Replacement	7,661	-	-	-	-
Corrosion	929	893	925	1,054	1,075
Pipeline Integrity	7,685	6,540	4,461	5,500	7,647
Main Replacements - (Reactive Programs)	2,671	2,760	2,792	2,928	2,987
Service Replacement - Reactive Leak Programs	4,625	4,643	4,803	4,979	5,079
Service Replacements- Non Leak Other	2,587	2,622	2,704	2,814	2,870
Atmospheric Corrosion Inside Inspect's	490	498	488	500	510
Meter Changes	3,167	3,204	3,315	3,407	3,475
Purchase Meters (Replacements)	3,152	2,305	1,345	1,374	1,401
Total Mandated	**96,376**	**106,887**	**125,045**	**157,234**	**184,685**
Reliability					
Control Line Integrity Program	294	601	301	335	335
Gas Facility Reliability - I&R	529	536	548	677	691
CNG	50	50	50	-	-
Gas Facility Reliability - Production/LNG	375	550	325	325	325
Holtsville LNG Truck Load/Unload Station	6,139	-	-	-	-
Gas System Reliability - Gas Control	162	947	1,149	272	176
Gas Control / Dispatch Relocation	3,000	-	-	-	-
Gas System Reliability - Service	20	20	21	23	23
Heater Installation Program	675	1,118	888	1,200	1,200
Reg Station (Pressure Reg Facilities)	2,162	1,656	1,847	1,900	1,900
Water Intrusion	886	904	881	1,000	1,020
Gas Planning Reliability	-	494	484	500	510
RCV Program	-	1,839	1,808	2,000	2,040
Value Installation/Replacement	130	130	130	130	130
System Automation	250	250	250	250	250
BQI Phase I	2,236	-	-	-	-
AMR (LIPA Separation) Program	18,572	2,188	610	620	620
Normac	-	-	-	-	-
FSM Replacement Program	-	-	-	-	-
Scada Security	-	-	-	-	-
Scada Modernization	-	-	-	-	-
Total Reliability	**35,480**	**11,283**	**9,292**	**9,232**	**9,220**
Non-Infrastructure					
All Other (Equipment, etc)	1,136	1,159	1,182	1,206	1,230
Total Non-Infrastructure	**1,136**	**1,159**	**1,182**	**1,206**	**1,230**
Total Direct	**240,023**	**220,685**	**241,725**	**264,843**	**294,616**

KeySpan Energy Delivery of Long Island

Forecast Capital Expenditures Converted to Calendar YearDetailed by Budget Category

Applicable to Deferral Mechanisms

'($000)

	FY 2015 Forecast	FY 2016 Forecast	FY 2017 Forecast	CY 15 Forecast	CY 16 Forecast
Development					
Main & Service Install (incl Cust Contribution)	55,261	59,227	60,685	58,236	60,321
Neighborhood Expansion Program (Main/Services)	2,796	8,689	16,102	7,216	14,249
Meter Purchase & Installation	2,844	2,998	2,999	2,960	2,999
Gas System Reinforcement (planned)	18,836	10,478	6,851	12,568	7,758
LI East End Reinforcement Program	19,783	19,964	19,569	19,919	19,668
Hicksville / Westbury Reinforcement	7,511	-	-	1,878	-
Total Development	**107,031**	**101,356**	**106,206**	**102,775**	**104,994**
Mandated*					
Proactive Main Replacement	54,320	73,793	94,846	68,925	89,583
Proactive Service Replacement	7,661	-	-	1,915	-
Main Replacements - (Reactive Programs)	2,671	2,760	2,792	2,738	2,784
Service Replacement - Reactive Leak Programs	4,625	4,643	4,803	4,639	4,763
Service Replacements- Non Leak Other	2,587	2,622	2,704	2,613	2,684
Meter Changes	3,167	3,204	3,315	3,195	3,287
Purchase Meters (Replacements)	3,152	2,305	1,345	2,517	1,585
Total Mandated	**78,183**	**89,327**	**109,805**	**86,541**	**104,686**
Reliability					
Water Intrusion	886	904	881	900	887
Total Reliability	**886**	**904**	**881**	**900**	**887**
Mandated + Reliability	**79,069**	**90,231**	**110,686**	**87,441**	**105,572**
LPP in Mandated City/State Capex	6,653	6,786	6,922	6,753	6,888
Capex Cap	**192,753**	**198,373**	**223,814**	**196,968**	**217,454**
Total Budget	**240,023**	**220,685**	**241,725**	**225,520**	**236,465**
% of Capex Cap as compared to the Total Budget	80%	90%	93%	87%	92%

*Excludes City/State

KeySpan Energy Delivery of Long Island

Forecast Capital Expenditures Converted to Calendar Year Detailed by Budget Category
Applicable to Deferral Mechanisms
'($000)

Development and Reinforcement Capex			
Year	**CY 15**	**CY 16**	**Total**
Miles of Main	57.5	67.5	125
New Services	9,250	9,435	18,685
Neighborhood Expansion Services	375	810	1,185
Total New Services	9,625	10,245	19,870
Total New Accounts	10,930	11,634	22,564
Development Capex	$ 61,195	$ 63,319	$ 124,514
Neighborhood Expansion Capex	$ 7,216	$ 14,249	$ 21,465
Reinforcement Capex	$ 34,364	$ 27,426	$ 61,790
Total Development and Reinforcement Capex	$ 102,775	$ 104,994	$ 207,768
LPP in Reinforcement	$ 2,491	$ 2,583	$ 5,074
Development and Reinforcement Capex Cap	$ 100,284	$ 102,410	$ 202,694

Leak Prone Pipe Breakdown				
Year	**CY 15**		**CY 16**	
Budget Category	**Miles**	**Capex**	**Miles**	**Capex**
Proactive/Storm Hardening	69.5	$ 68,925	87.0	$ 89,583
City/State	4.0	$ 6,753	4.0	$ 6,888
Reliability/Reinforcement	1.5	$ 2,491	1.5	$ 2,583
Leak/Reactive	1.5	$ 2,738	1.5	$ 2,784
Water Intrusion	1.0	$ 900	1.0	$ 887
Total Mileage	**77.5**	$ 81,806	**95**	$ 102,725
plus Services		$ 9,167		$ 7,447
plus Meters		$ 5,712		$ 4,872
Leak Prone Pipe Capex Cap		$ 96,684		$ 115,044

Capex Caps			
Year	**CY 15**	**CY 16**	**Total**
Development & Reinforcement Cap	$ 100,284	$ 102,410	$ 202,694
LPP, Services & Meters Cap	$ 96,684	$ 115,044	$ 211,728
Total Capex Cap	$ 196,968	$ 217,454	**$ 414,422**

KeySpan Energy Delivery of Long Island
Development & Reinforcement Incentive Mechanism
Example Calculation

CY 2015 Target New Accounts	10,930
Total Average Accounts 12ME December 31, 2014	500,000
Total Average Accounts 12ME December 31, 2015	509,500
Total New Accounts	9,500
Accounts Under Target	1,430
Adjustment to Actual CY 2015 Deferral	-13%
CY 2016 Target New Accounts	11,634
Total Average Accounts 12ME December 31, 2015	509,500
Total Average Accounts 12ME December 31, 2016	522,500
Total New Accounts	13,000
Accounts Under Target	-
Adjustment to Actual CY 2016 Deferral	0%

KeySpan Energy Delivery of Long Island

Bill Impacts

Scenario 1: Defer All Carrying Charges Associated with Capex

			CY 2015 - CY 2016			
Projected Carrying Charges						
Leak Prone Pipe, Services and Meters			$ 23,400,000			
Development and Reinforcement			$ 26,500,000			
		Total	$ 49,900,000			
Three Year Amortization			$ 16,633,333			
Rate Base Impact on Investments in the Next Case			$ 23,900,000			
		Total	$ 40,533,333			
Development of the Rate						
Estimated Firm Sales & Transportation Volumes (therms)			887,068,310			
Total Carrying Charges			$ 40,533,333			
Estimated Rate per therm			$ 0.0457			
					Increase	
	Therms		**Current Annual Bill**	**Adjusted Annual Bill**	**$**	**%**
Annualized Bill Impacts						
Residential Heating	1000		$ 1,376.00	$ 1,376.00	$ -	0.0%
Annualized Bill Impacts In Next Case Assumed Effective 1/1/17						
Residential Heating	1000		$ 1,376.00	$ 1,421.69	$ 45.69	3.3%

Scenario 2: Surcharge Carrying Charges Associated with LPP Capex and Defer Carrying Charges Associated the Development Capex

			CY 2015 - CY 2016			
Projected Surcharges						
Estimated Firm Sales & Transportation Volumes (therms Apr 15 - Dec 16)			1,419,309,296			
Leak Prone Pipe, Services and Meters Carrying Charge			$ 23,400,000			
Estimated Rate per therm			$ 0.0165			
Projected Carrying Charges						
Leak Prone Pipe, Services and Meters			$ -			
Development and Reinforcement			$ 26,500,000			
		Total	$ 26,500,000			
Three Year Amortization			$ 8,833,333			
Rate Base Impact on Investments in the Next Case			$ 23,900,000			
		Total	$ 32,733,333			
Development of the Rate						
Estimated Firm Sales & Transportation Volumes (therms)			887,068,310			
Total Carrying Charges			$ 32,733,333			
Estimated Rate per therm			$ 0.0369			
					Increase	
	Therms		**Current Annual Bill**	**Adjusted Annual Bill**	**$**	**%**
Annualized Bill Impacts						
Residential Heating	1000		$ 1,376.00	$ 1,392.49	$ 16.49	1.2%
Annualized Bill Impacts In Next Case Assumed Effective 1/1/17						
Residential Heating	1000		$ 1,392.49	$ 1,412.90	$ 20.41	1.5%