STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on April 18, 2007

COMMISSIONERS PRESENT:

Patricia L. Acampora, Chairwoman
Maureen F. Harris
Robert E. Curry, Jr.
Cheryl A. Buley

CASE 03-E-0640 – Proceeding on Motion of the Commission to Investigate Potential Electric Delivery Rate Disincentives Against the Promotion of Energy Efficiency, Renewable Technologies and Distributed Generation.

CASE 06-G-0746 – In the Matter of the Investigation of Potential Gas Delivery Rate Disincentives Against the Promotion of Energy Efficiency, Renewable Technologies and Distributed Generation.

ORDER REQUIRING PROPOSALS FOR REVENUE DECOUPLING MECHANISMS

(Issued and Effective April 20, 2007)

BY THE COMMISSION:

SUMMARY

Programs that promote cost-effective energy conservation, increase the use of renewable resources and otherwise reduce or eliminate barriers to the installation of distributed generation can reduce pollution, conserve natural resources, decrease dependence on foreign sources of fossil-fuels, promote price stability, improve fuel diversity, and create significant cost savings opportunities for customers. Energy efficiency improvements, in particular, limit unnecessary

load growth and can avoid or delay installation of costly, new distribution, transmission or generation facilities.

These proceedings were instituted to examine potential delivery rate disincentives against the utilities' promotion of energy efficiency, renewable technologies and distributed generation. They are undertaken as part of an overall State program to facilitate customer access to existing and developing technologies for the clean production and/or conservation of energy. In addition to this proceeding, this Commission is engaged in a comprehensive program for enabling efficiency and alternative resources, including adopting mandatory hourly pricing for the State's largest customers; directing utilities to consider and implement advanced metering for customer classes as appropriate; implementing renewable energy, efficiency and energy research and development programs; encouraging the cost effective use of customer-owned electric generation, and providing more accurate price signals to customers.

While significant progress has been made by the utilities in shifting recoveries of utility fixed delivery costs from volumetric rates or marginal consumption blocks to fixed charges or initial consumption blocks, concerns remain that, for at least some classes of customers, existing rate designs still may discourage utilities from actively promoting energy efficiency, renewable technologies and distributed generation. To the degree that utility fixed delivery costs are recovered from customers on a volumetric or marginal consumption basis, there remains a net lost revenue and profit effect that could act as a disincentive. In furtherance of the State's energy policy objectives, there is a need to identify the degree to which this may be the case at each of the utilities and to identify appropriate remedies.

In this Order, we require utilities to develop and implement mechanisms that true-up forecast and actual delivery service revenues and, as a result, significantly reduce or

eliminate any disincentives caused by the recovery of utility fixed delivery costs via volumetric rates or marginal consumption blocks. These revenue decoupling proposals should be filed in ongoing and new rate cases, whereby the utilities, Department of Public Service staff (Staff) and interested parties can address specific design details.

PROCEDURAL BACKGROUND

Case 03-E-0640 was instituted by an Order[1] issued on May 2, 2003. An all-party technical conference was held in that proceeding on June 16, 2003. Thereafter, on September 22, 2003, the electric utilities submitted "typical bill" analyses highlighting the relationship between fixed charges and the potential for lost revenues. Comments were received on October 10, 2003, and reply comments were received on November 7, 2003. On July 9, 2004, Staff submitted a Staff Report. Comments on the Staff Report were received on July 29, 2004. On June 26, 2006, a Notice[2] was issued that the Commission was expanding the inquiry to gas utilities, in Case 06-G-0746, and soliciting additional comments. A Notice of Proposed Rulemaking concerning each of the two proceedings was published in the State Register on July 12, 2006 in accordance with the State Administrative Procedure Act. The minimum period for the receipt of public comments expired on August 28, 2006. Initial comments were received on August 28, 2006 from Brooklyn Union Gas Company d/b/a KeySpan Energy Delivery New York and KeySpan Gas East Corporation d/b/a KeySpan Energy Delivery Long Island (KeySpan), Central Hudson Gas & Electric Corporation (Central Hudson), the City of New York (NYC), Consolidated Edison Company of New York,

[1] Case 03-E-0640, supra, Order Instituting Proceeding (issued May 2, 2003).

[2] Case 06-G-0746, supra, Notice Soliciting Comments (issued June 26, 2006).

Inc. and Orange and Rockland Utilities (Con Edison/O&R), Consolidated Edison Solutions (Con Ed Solutions), Multiple Intervenors (MI), National Fuel Gas Distribution Corporation (NFG), Natural Resources Defense Council and Pace Energy Project (NRDC/Pace), New York Energy Consumers Council, Inc. (NYECC), New York Municipal Power Agency (NYMPA), New York Power Authority (NYPA), New York State Consumer Protection Board (CPB), New York State Department of Environmental Conservation (DEC), New York State Electric & Gas Corporation and Rochester Gas and Electric (NYSEG/RG&E), New York State Energy Research and Development Authority (NYSERDA), Niagara Mohawk Power Corporation d/b/a National Grid (National Grid), Nucor Steel Auburn, Inc. (Nucor), Office of the New York State Attorney General (AG), and Public Utility Law Project (PULP). Reply comments were received on September 11, 2006 from Con Edison/O&R, MI, National Grid, NFG, NRDC/Pace, and NYSEG/RG&E. The most recent set of comments is summarized in Appendices A and B attached to this Order.

DISCUSSION

As the Commission noted in the Order Instituting Proceeding in Case 03-E-0640:

> In an effort to reverse a growing dependence on foreign oil in the 1970s and the ineffectual supply side planning strategies in the 1970s and 1980s preferring development of large-scale power production facilities that were subject to protracted construction schedules and significant uncontrolled cost escalations, the Commission instituted "integrated resource planning" policies. These policies required utilities to integrate consideration of demand side options on an equal footing with supply side options to arrive at "least cost" planning solutions. To that end, the electric utilities were directed[3] to encourage their retail customers' to participate in utility-sponsored end-use energy efficiency and peak-load

[3] Case 29409, Plans for Meeting Future Electricity Needs in New York State, Opinion No. 88-20 (issued July 26, 1988).

> reduction demand side management programs.
>
> The implementation of load reduction initiatives meant a corresponding reduction in electric sales revenues and profits for utilities, putting the financial interests of electric utility shareholders at odds with their customers' interests.
> In order to re-align those interests, the Commission adopted various alternative ratemaking models, combining sales revenue adjustments with outright financial incentive payments to utilities, in essence giving utilities a share of the savings resulting from demand reductions to offset lost revenues and profits.
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> When the Commission decided to restructure the electric market to wholesale and retail competition, utility-sponsored demand side management programs were largely discontinued, along with the alternative ratemaking models. In their place, demand side and renewable energy projects are now implemented through NYSERDA programs funded by a System Benefits Charge collected from delivery utility customers. The electric delivery function remains a regulated monopoly service.

Although energy markets have been restructured, the Commission has continued to support energy efficiency and peak demand reduction programs, renewable technologies and distributed generation options, and provide to utilities and end-users incentives to pursue such opportunities. For example, the electric System Benefits Charge (SBC) provides funding, currently $175 million per year, and a framework for the delivery of energy efficiency and other public benefit programs. Administration of customer end-use energy efficiency programs is delegated to the New York State Energy Research and Development Authority (NYSERDA), in effect, reducing the utilities' potential internal conflict between sales growth and the promotion of programs or technologies that reduce sales. A second major initiative, the Renewable Portfolio Standard (RPS), was established by the Commission in 2004 and is an aggressive long-term procurement program for acquiring electricity from renewable resources.

Other initiatives undertaken by the Commission in its efforts to remove hurdles to the adoption of energy efficiency,

renewable energy and distributed generation include: promulgation of streamlined interconnection rules for distributed generation; establishment of special natural gas delivery rates to encourage development of distributed generation; institution of a proceeding to promote distributed generation options; establishment of the Environmental Disclosure program upon which “green” marketing is based; support for the New York State Independent System Operator (NYISO) demand reduction initiatives; and several utility-specific energy efficiency programs. Also, the establishment of electric standby delivery rate structures for customers pursuing their own distributed generation installations has done much to encourage utility support for cost effective behind-the-meter electricity production by such facilities.

To the extent the current design of delivery service rates continues to link the recovery of utility fixed costs, including profits, to the volume of actual sales, utility disincentives remain. Energy efficiency programs designed to conserve energy reduce electric utility sales and corresponding delivery revenues relative to what they would have otherwise been.[4] Similarly, customer-sited renewable resource technologies[5] and the installation of distributed generation technologies reduce electric utility sales and corresponding revenues, by replacing utility sales with customer-generated power.

[4] Delivery rate designs do not generally provide a significant financial disincentive to the promotion of load-shifting type energy efficiency programs which can be distinguished from energy conservation type energy efficiency programs.

[5] Delivery rate designs do not generally provide a significant financial disincentive to the promotion of wholesale purchases of power from renewable resources which can be distinguished from customer-sited PV, wind and biogas technologies.

Mechanisms have been established and implemented that attempt to break the link between utility sales and revenues. These include incorporating anticipated energy efficiency and price elasticity effects into rate case forecasts, excluding profits from dual-fueled load in gas utility revenue requirements, and employing weather normalization clauses that decouple the effects of weather on firm gas sales load.

Utilities can also petition for recovery of verified net lost revenues resulting from participation in demand response and energy efficiency programs. However, program-specific lost revenue mechanisms can be complex and challenging, both in design and implementation, as well as verification of actual net lost revenues associated with specific energy efficiency or demand response programs. The more programs a utility offers, the more complex and potentially inaccurate the mechanism could become. Further, lost revenue mechanisms may not address lost revenues attributable to policies and technologies not associated with specific utility-supported efficiency programs.

The implementation of fully cost-based rates is another means of eliminating utility disincentives. However, the rapid effectuation of such rate design approaches, especially for mass market customers, could result in significant bill impacts and potential customer harm. Additionally, in the short-term, the immediate reduction of current energy charges could diminish the incentive for certain higher use customers to conserve energy, since the potential bill savings would be reduced.

A revenue decoupling mechanism (RDM) is a ratemaking approach designed to eliminate or substantially reduce the linkage between sales and utility revenues and/or profits. An RDM is used because existing utilities' delivery rate designs are, in most cases, not "optimal" in that they do not always

collect fixed costs through fixed charges and variable costs through variable charges. RDMs remove the disincentive a utility has to promote energy conservation by removing the link between sales and profits. Mechanically, RDMs function by comparing actual versus authorized revenues or revenues per customer and either crediting or collecting any differences from customers in a subsequent period. This true-up would include, among other things, any net lost revenues attributable to the implementation of energy efficiency programs. The true-up should occur no less frequently than once per year.

New York has experience using revenue decoupling mechanisms to achieve two primary objectives: to remove utility opposition to customer investments and efforts to reduce energy consumption; and to reduce the risk to utilities of lost fixed cost revenue recoveries, such as during multi-year rate plans, or for utilities facing significant financial challenges. While such measures alone may not produce demonstrable increases in the utilities' promotion of energy efficiency, they can be an effective tool in reducing utilities' resistance to the implementation and promotion of such programs.

There are a number of design and implementation issues that would need to be considered in the development of an effective revenue decoupling mechanism. These include: whether the mechanism is applied to all or only some customer classes; whether allowed revenues are calculated on a per customer basis (i.e., encourage economic development by allowing utilities to collect revenues for new customers); which indices (e.g., inflation, productivity), if any, are incorporated in the mechanism; and whether to include or exclude weather related sales fluctuations. The frequency and allowed level of true-up would also need to be considered to avoid amassing significant revenue deferrals. The intent should be to avoid the

accumulation of large liabilities and the ensuing bill impacts and general price instability for ratepayers.

Disincentives Due to Delivery Rate Designs

A number of parties, including Keyspan, NFG, AG and NRDC/Pace, claim that existing gas and electric utility delivery rates do, in some cases, result in the recovery of a portion of the utilities' fixed costs through volumetric charges, thereby linking utility profits to volumetric sales. National Grid specifically notes that a ten percent reduction in gas sales correlates to a loss of delivery revenues of approximately three percent for residential classes and approximately six and a half percent for small commercial classes. Accordingly, many parties believe that since energy efficiency programs and the installation of customer sited renewable technologies or distributed generation will ultimately reduce sales, the inherent link between sales and revenues could provide a disincentive for utilities to actively promote such programs. Some parties claim that this has been evidenced by various utility behaviors including opposition to net metering, appliance energy efficiency standards, the system benefits charge program, and distributed generation.

Existing utilities' delivery rate designs are, in most cases, not theoretically optimal, in that they do not generally fully collect fixed costs through fixed charges or initial consumption blocks, and variable costs through variable charges. The parties' arguments are convincing that these suboptimal rate designs may provide utilities with a disincentive to promote programs that would result in lower sales and, therefore, lower revenues. MI argues that the disincentive toward the utilities' promotion of energy efficiency, renewable generation resources and distributed generation has been diminished as a result of restructuring - including the adoption of rate unbundling, the

establishment of the System Benefits Charge, the Renewable Portfolio Standard, and the New York Independent System Operator demand response programs. However, the distribution rate disincentive remains. This remaining disincentive can be addressed in a number of ways, including the implementation of cost-based rates, but there is no perfect solution. Some parties, including CPB and NRDC/Pace, argue that moving more fixed costs into fixed charges could increase bills for low income and low usage customers, and reduce the appropriate response to prices by others. MI argues, on the other hand, that fully cost-based, time-differentiated rates, provide the most accurate price signals and will ultimately provide the greatest benefits to New York consumers. Given the potential harm to certain customers resulting from too rapid an implementation of more cost-based rate designs, and recognizing the time required for their development and implementation, we believe it is now more appropriate to implement a true-up based revenue decoupling mechanism which would establish certainty with respect to utility revenues regardless of the level of commodity sales realized. It is still a worthy long-term objective to continue moving towards more cost-based rates, where appropriate, to provide customers with appropriate price signals. But such long-term rate redesign objectives do not obviate the current need for a more broad-based revenue decoupling approach.

With respect to the different customer classes and whether the rate design impacts are more prominent for certain classes than others, we recognize that more movement toward fully cost-based rates has been or can more easily be accommodated within the larger commercial and industrial classes, thereby largely breaking the link between utility sales and profits attributable to these customers. On the other hand, lost revenue and profits due to reduced sales can be significant

for residential and small commercial classes. On the electric side, in large part due to the absence of demand meters for these smaller customers, a much more substantial portion of "fixed" distribution delivery costs, in general, continue to be recovered in volumetric charges. On the gas side, delivery rates continue to be predominantly volumetric. KeySpan notes that between 50 percent and 75 percent of its margin is recovered through the tail block rate and penultimate block and less than 50 percent of its minimum cost to serve is recovered through its minimum charge.

Delivery Rate Redesign

National Grid and Con Edison/O&R support the application of standby rate design principles set forth by the Commission in designing cost-based rates for all customer classes in general. The utilities, along with other parties, recommend that interested parties be afforded the opportunity to consider specific rate design proposals and bill impacts on customers within service classifications before the implementation of revised rate structures. Other parties assert that standby ratemaking principles should not be applied generally to all utility rate classes. Central Hudson claims that the standby rate design principles are not generally applicable to other service classifications since standby service customers have different load shapes and impose costs on the utility in a different manner. NRDC/Pace claims that the implementation of standby rates does not address utility lost revenues and disincentives since customers would have an incentive to reduce their contract and as-used demands. KeySpan claims that the standby rate principles do not resolve the issues for gas utilities since most gas utilities do not use demand meters. However, Keyspan states that cost-based rate designs that collect more fixed costs through the minimum charge and head block would minimize lost revenues attributable to

energy efficiency measures.

Regarding the timing of rate redesign changes and interim steps, National Grid, Con Edison/O&R, Central Hudson and NYSEG/RG&E generally suggest that rate changes, including the implementation of a revenue decoupling mechanism, be addressed in a rate case, and that such changes not be made in the interim. KeySpan and National Fuel claim that a revenue decoupling mechanism, once designed, could be implemented in a relatively short time period and without a major rate change. NRDC/Pace suggests that each electric and gas utility be required to include a revenue decoupling mechanism in its next rate case but also be allowed to request implementation sooner. MI indicates that, if a revenue decoupling mechanism is adopted, all industrial and large commercial customers should be exempt. Several parties recommend a collaborative process for addressing either or both utility delivery rate redesign as well as revenue decoupling mechanism design and implementation.

With respect to various delivery rate design initiatives already underway, some parties support the continued movement toward time-differentiated rates and interval metering. As stated previously, we agree that these initiatives have merit. A number of parties further suggested that a true-up based delivery service revenue decoupling mechanism, alone or in conjunction with rate design changes, would realign utility incentives to support energy efficiency, renewable technologies and distributed generation. We agree, and find that the development of a delivery service revenue decoupling mechanism

beyond the adoption of more cost-based rates to address existing delivery rate disincentives is appropriate.

We believe that the proper forum for designing an appropriate delivery service revenue decoupling mechanism is in utility rate cases. Various parties have had experience with revenue decoupling mechanisms, and have presented some suggested design criteria and principles in this proceeding. Sharing this and other information with all interested parties in the context of a utility rate case would be beneficial and most expedient.

With respect to utility delivery rate redesign, we believe that the utilities are best suited, at this time, to examine existing rate designs and propose necessary changes as appropriate. We remain committed, however, to the continued implementation of cost-based hourly pricing tariffs for commodity service where appropriate, especially for larger commercial and industrial energy users.

Low Usage/Low Income

NRDC/Pace and CPB state that rate redesign that shifts fixed costs into fixed charges could be harmful to low usage or low income customers. NYSEG/RG&E point out that there is not a clear link between low income and low usage and that no special treatment is necessary, given that low income programs are already in place. National Grid, Con Edison/O&R, Keyspan, NFG, AG and other parties support targeted approaches to addressing the impacts of rate redesign or the implementation of a revenue decoupling mechanism on low income customers. They cite low income programs, including targeted energy efficiency and weatherization programs. Some parties also note that, to the extent that the implementation of a revenue decoupling mechanism results in the expansion of energy efficiency programs, low income customers may benefit in the long run.

We agree that a rapid shift of fixed costs from volumetric to fixed customer charges could especially harm low

usage and low income customers. While a targeted approach to addressing potential bill impacts on low income customers would help mitigate those impacts, our preference at this time is not to pursue such a rapid shift of fixed costs from volumetric to customer charges. We do recognize, however, that low income programs may need to be expanded and energy efficiency programs further targeted, in any case, regardless of the decoupling approach adopted.

Revenue Decoupling Mechanism Design

The parties suggest very divergent approaches to the development of a revenue decoupling mechanism. Some propose targeted mechanisms that account for lost revenues attributable to only specific energy efficiency or demand management programs while other parties propose more comprehensive mechanisms. Consequently, parties have suggested a number of design variables that should be considered. With respect to implementation of a revenue decoupling mechanism, some parties recommend that both the design and implementation occur in the context of individual utility rate cases. NRDC/PACE recommend that generic guidelines be established through a collaborative process.

Given the need to move expeditiously in addressing remaining disincentives to the implementation of energy efficiency and public benefit programs, we support the proposal of the parties recommending that both the design and implementation takes place in the context of individual utility rate cases.

Allowed Rate-of-Return Changes

The commenting parties generally agree that the extent to which the implementation of a revenue decoupling mechanism should affect a utility's allowed rate of return is better addressed in individual rate proceedings. Parties point out that while decoupling of utility sales and delivery revenues

shifts some business risk from the utility to customers, without examining the specific delivery revenue design mechanism in conjunction with other factors and terms of a given rate plan, it is unclear to what extent, if any, utility risk is affected.

We agree that the effect of a delivery service revenue decoupling mechanism on utility rate of return should be considered, to the extent appropriate, along with other factors, in the context of individual rate proceedings.

Conclusion

The public benefits resulting from energy efficiency programs, renewable technologies and distributed generation could be substantial. Nevertheless, a link continues to exist between utility sales and delivery service revenues, due to the current design of utility delivery rates, which could influence utility behavior by providing disincentives that impede their promotion of these initiatives. Rate design changes can significantly reduce such utility disincentives, but are often effectuated gradually due to customer bill impact concerns. While the eventual implementation of more cost-based rate designs remains an important long-term objective, especially for larger more price responsive customers, it appears that properly designed revenue decoupling mechanisms are needed at this time to address disincentives that may still exist, given present delivery service rate designs.

Therefore, we are directing the major electric and gas utilities to file proposals, in ongoing and new rate cases, for true-up based revenue decoupling mechanisms, in the manner contemplated in the body of this Order. The filings shall include proposals for limiting customer bill impacts and price volatility, to the extent practical, and address other implementation issues raised during the course of this proceeding. In addition, parties should consider, propose and develop new approaches that encourage utility and energy service

company promotion of, and customer participation in, energy efficiency programs, and also address the issues raised herein.

The revenue decoupling mechanism design should incorporate the following factors:

- The mechanism should be designed to true-up forecast and actual utility delivery service revenues for a given time period.

- The mechanism should be designed to prevent gaming by the utility (e.g., shifting customers to different classes).

- The recovery of any net lost revenues component of the mechanism should not, in and of itself, produce inter-class revenue re-allocations between customer classes (such re-allocations should only be made purposefully after considering a current fully-allocated cost of service study).

- All remaining design and implementation issues should be addressed in individual rate proceedings

In addition to the implementation of broad-based revenue decoupling mechanisms that incorporate appropriate true-ups, the promotion of customer-sited renewable resources and distributed generation technologies should be addressed through greater vigilance on the part of the utilities regarding the proper application and supervision of utility interconnection rules and procedures, and the expanded application of existing electric and gas standby delivery rate structures.

The Commission orders:

1. At the time of their next rate case, or in an on-going rate case if one exists, the Brooklyn Union Gas Company d/b/a KeySpan Energy Delivery New York, Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., Corning Natural Gas Corporation, KeySpan Gas East Corporation d/b/a KeySpan Energy Delivery Long Island, National Fuel Gas Distribution Corporation, New York State Electric & Gas

Corporation, Niagara Mohawk Power Corporation d/b/a National Grid, Orange and Rockland Utilities, Inc., Rochester Gas and Electric Corporation and St. Lawrence Gas Company, Inc. shall develop proposals for true-up based delivery service revenue decoupling mechanisms for consideration in individual utility rate cases as discussed in the body of this Order.

2. In existing rate cases, where there may be insufficient time to develop and incorporate revenue decoupling proposals, the rate cases should provide for supplemental procedural phases to address and develop revenue decoupling mechanisms.

3. This proceeding is continued.

By the Commission,

(SIGNED) JACLYN A. BRILLING
Secretary

Summary of Responses to Notice Soliciting Comments

Background

Comments were received from various utilities, government agencies, energy retailers and end-use customers, and customer groups. Below are summaries of the initial comments received on August 28, 2006 and the reply comments received on September 11, 2006.

Initial Comments: Statements in Opposition

1. Central Hudson Gas & Electric Corporation (Central Hudson)

Central Hudson does not believe the Commission should focus its attention on developing new revenue decoupling mechanisms (RDMs); it suggests a focus on methods of providing customers contemporaneous commodity cost price signals.

Central Hudson states that the delivery portion is less than the commodity cost portion of customers' energy bills. Thus, customers already have incentive to conserve energy. Central Hudson believes recognition of full price elasticity coupled with advanced metering technologies will bring about desired customer conservation.

Central Hudson does not categorically preclude utility specific RDM development but states that there is no evidence that development of a generic RDM would be a wise use of pubic resources.

2. Consolidated Edison (Con Edison) and Orange and Rockland Utilities (O&R)

Con Edison/O&R declares:

Utilities do not have material disincentives to promote energy efficiency (EE) or distributed generation (DG) for either gas or electric service.

There are mechanisms that can more effectively achieve the Commission's energy efficiency goals.

If deemed appropriate RDM development and design should be resolved in utility specific rate proceedings.

3. Consolidated Edison Solutions

Con Edison Solutions emphasizes the importance of designing incentive programs (including any lost revenue mechanisms) in a competitively neutral fashion.

4. New York Municipal Power Agency (NYMPA)

While NYMPA does not oppose the use of RDMs in principal, it does not believe it is necessary for municipal systems at this time, stating that municipal systems have a long history of promoting energy efficiency.

5. New York State Electric & Gas Corporation (NYSEG) and Rochester Gas and Electric (RG&E)

NYSEG/RG&E states the Commission should refrain from making any generic determinations in these proceedings. According to the companies, the Commission should find that a variety of programs and rate options to support energy efficiency and conservation is more desirable. NYSEG and RG&E comment that utilities do not have a material disincentive associated with promoting EE, DG, or renewable initiatives. The companies support rate changes designed to recover fixed costs in the fixed component of rates.

With respect to gas service, NYSEG and RG&E state the consideration of a more broad-based approach may be warranted as gas rates are predominantly volumetric. However, any broad-based mechanism (including a gas RDM) should be tailored to each company's circumstances.

6. Niagara Mohawk Power Corporation d/b/a National Grid (National Grid)

National Grid states the best approach to balance benefits and incentives associated with implementation of various energy efficiency and distributed generation programs is to maintain flexibility to tailor specific policy solutions which address associated revenue losses.

National Grid emphasized that addressing energy efficiency should be done in individual rate proceedings, not generically.

7. Nucor Steel Auburn, Inc (Nucor)

Nucor urges the Commission to reject revenue decoupling as a viable mechanism for promoting energy efficiency. Nucor stated, historically, RDMs have produced significant weather-related accruals creating rate instability. Nucor stated further that utility "throughput disincentives" are exaggerated and that greater recovery of fixed costs in fixed charges will minimize lost revenue due to energy consumption. Nucor supports the use of advanced metering and rate design improvements to send price signals to customers.

8. Multiple Intervenors (MI)

MI states there is no evidence justifying the need for dramatic changes to utilities' existing rate structures and financial disincentives are inconsequential; thus, RDMs should not be required. MI also explains that rate disincentives are further diminished due to NYSERDA's administration of the System Benefits Charge (SBC) and Renewable Portfolio Standards (RPS) programs and the New York Independent System Operator operates customer demand reduction programs. Like Nucor, MI voices concern over potential weather related accruals produced by RDMs.

Specific to gas LDCs, MI states fluctuations in weather related usage far outweigh energy efficiency opportunities, and instituting a gas RDM would be inconsistent with efforts to promote certain types of gas consumption. MI would exempt industrial and large customers from revenue impacts if RDM is imposed.

Initial Comments: Statements in Support

1. NYS Attorney General

The Attorney General's office supports a revenue decoupling mechanism and prefers the use of a revenue target based on the utilities cost of service and profit.

2. Brooklyn Union Gas Company d/b/a KeySpan Energy Delivery New York and KeySpan Gas East Corporation d/b/a KeySpan Energy Delivery Long Island (KeySpan)

KeySpan supports implementing energy efficiency initiatives, including a revenue decoupling mechanism that will align the interests of utilities and customers while benefiting customers and society. KeySpan supports moving toward cost-based rate design in coordination with the establishment of a mechanism that allows for recovery shortfalls resulting from lower use per customer. KeySpan advocates recovery of lost revenue if customers' use declines more than is assumed in its rate plans.

3. The City of New York (City)

The City supports development of revenue decoupling mechanisms in individual rate case proceedings. The City concludes that revenue decoupling development should begin with gas distribution utilities, and electric distribution utilities should draw from their experience.

4. Department of Environmental Conservation (DEC)

DEC supports removing delivery rate structures that may discourage utilities from investing in cost-effective EE, renewable energy, and clean DG.

5. National Fuel Gas Distribution Corporation (NFG)

NFG states that current LDC programs that promote energy conservation penalize gas LDCs by reducing LDC revenues; and, there is ample support for adopting appropriate incentives for LDCs to promote energy efficiency. NFG advocates using an annual reconciliation charge mechanism which would recover lost revenues associated with declines in customers' use.

6. Consumer Protection Board (CPB)

CPB supports a well designed revenue decoupling mechanism. CPB states the RDM should recognize true lost revenue due to EE, not losses due to a faltering economy. CPB notes that, if the RDM is limited to EE measures, common equity rates of return would not need to be reduced due to decreased company risks. CBP would like staff to form a straw man proposal in a generic proceeding.

7. Natural Resources Defense Council (NRDC) and Pace Energy Project (Pace)

NRDC/Pace states the Commission should require New York gas and electric utilities to adopt revenue decoupling mechanisms as the only full and comprehensive method to align the economic interests of utility and shareholders with the interests of New York State and its citizens to invest in energy efficiency and distributed generation.

NRDC and Pace state the Commission should convene a collaborative process to design electric and gas RDMs. NRDC and PACE state further the Commission should direct each gas and

electric utility to propose a revenue adjustment mechanism in its next rate case.

NRDC also filed a statement of agreement in support of RDMs that would align interests of shareholders and customers that was signed by 67 parties.

8. New York Energy Consumers Council, Inc. (NYECC)

NYECC claims utility companies should be encouraged to support investments related to EE, DG, and renewable energy sources, while aligning shareholder and customer interest. NYECC supports the Total Resource Cost Test established by the Commission in Case No. 29409 in 1988. The Total Resource Cost Test measures the net costs of a demand-side management program as a resource option based on the total costs of the program, including both the participants' and the utilities' costs. established by the Commission in Case No. 29409 in 1988.

9. New York Power Authority (NYPA)

NYPA urges the Commission to encourage energy efficiency and distributed generation, and claims RD is necessary if EE and DG are to be further encouraged in NY.

Initial Comments: General Statements

1. New York State Energy Research and Development Authority (NYSERDA)

NYSERDA acknowledges the merits of any strategy to allowing a utility to earn its return without discouraging investments in energy efficiency. However, it maintains that measures that may alleviate disincentives but, at the same time dampen customers' incentives may be counter productive to energy system efficiency and reliability.

2. Public Utility Law Project (PULP)

PULP was not a participant in the original proceeding. It, petitioned to intervene at a later stage of the proceeding.

Reply Comments

Reply comments were received on September 11, 2006 from Con Edison/O&R, National Grid, NFG, NRDC/PACE, NYSEG/RG&E, and MI. Some parties offered additional information beyond their original comments; and, it is summarized below.

1. National Grid

The rate of return on equity should not be modified should an RDM be implemented.

2. NFG

Supports MIs' exclusion of large-volume industrial and commercial classes from RDM impacts.

3. NRDC/Pace

NRDC/Pace re-files their statement of agreement in support of RDMs with additional signatures. It has now been signed by 89 parties, rather than 67.

4. NYSEG/RG&E

NYSEG/RG&E states NFG and KeySpan may have poor rate designs that are impediments to promotion of EE, Renewables, and DG; however, these material disincentives may not exist for all companies. NYSEG and RG&E also state delivery utilities have a financial incentive to consider EE, Renewables and DG, especially if they present a cost-effective supply alternative.

Responses to Revenue Decoupling Questions

Questions Contained in Notice Soliciting Comments
Issued June 26, 2006

Question No. 1.

Do the current delivery rate structures of the electric and/or gas delivery utilities still contain a net lost revenue and profit effect that is significant enough to discourage some or all electric and/or gas delivery utilities from promoting energy efficiency, renewable technologies and distributed generation? Or, conversely do the current rate structures in effect encourage the utilities to promote the incremental use of electricity?

National Grid:

- National Grid has, over several years, implemented cost-based rate designs for its delivery service that reflect most costs in the initial blocks of the company's rates, and lower the loss of margin in tail block rates, thereby reflecting the high proportion of fixed costs associated with delivery service.
- National Grid recovers commodity revenues for its sales of both electricity and natural gas as a supply charge through separate reconciling mechanisms.
- The SC-7 Standby Electric Service rate design and the deferral of lost revenues also initially addressed the disincentives associated with renewable energy and distributed generation.
- National Grid's main points in its earlier comments (2004) were (1) industry restructuring and competitive commodity markets have eliminated the disincentive to National Grid from reduced commodity sales; and (2) rate design can mitigate lost revenues as fixed costs can be recovered through greater reliance on fixed components of a customer's bill.
- For gas, National Grid implemented a declining block rate structure as a way of setting rates more closely to the way costs are incurred on the system. This approach has been implemented with usage blocks because certain customer charges (i.e., service charges) are not allowed for gas customers under Public Service Law.
- For gas, a ten percent reduction in gas deliveries correlates to a loss of delivery revenues of approximately three percent for residential classes and approximately six and a half percent for small commercial classes.

Con Edison/O&R:

- The delivery rates do not result in significant or material disincentives to promoting EE/DG.
- General rate design changes or different revenue recovery methods should be considered in individual rate cases because utility rates are designed to balance a broad range of differing objectives, such as providing proper price signals, avoiding subsidies to certain groups of customers, enabling utility investors to earn a fair return, and achieving environmental goals.
- Whether a particular utility has a significant disincentive can and should be adjudicated in a utility rate case, and not merely adopted as a general statement of policy.

KeySpan Energy Delivery New York and Long Island:

- KeySpan's current gas delivery rate structures still contain large net lost revenue and profit effects that are significant enough to discourage it from promoting energy efficiency, and encourage it to promote the incremental use of gas.
- 50% - 75% of the companies' margin (revenue less gas costs) is recovered through the tail block and penultimate block.
- The companies' minimum charges do not recover even half of their minimum costs to serve.

New York Power Authority:

- NYPA is unable to assess the degree to which electric delivery utilities in New York are encouraged or discouraged in promoting energy efficiency and related practices as a result of current delivery rate structures.

National Fuel:

- Its current delivery rate structure contains a net lost revenue profit effect that is significant enough to discourage the company from promoting energy efficiency.
- The company also has a significant incentive under current rate structures to increase the usage per account of its customers.

NYS Attorney General:

- The current delivery rate structures of the electric and gas delivery utilities still contain a net lost revenue and profit effect that is significant enough to discourage electric and gas delivery utilities from promoting energy efficiency and distributed generation.

Central Hudson:

- There are neither material disincentives to conservation and energy efficiency, nor incentives to promote the incremental use of energy.
- Notable rate design changes include: movement of gas revenue recovery into fixed rate components; rate unbundling, including separation of merchant function charges into sales and non-sales customer groupings; no volumetric component for SC Nos. 3 and 13; 90% of SC No. 2 load is on demand rates, and the usage rates reflect unbundled usage-related costs and flow through of variable energy supply costs.
- An advanced metering pilot program would allow use of time differentiated, demand-based rates in the SC Nos. 1 and 2 classes that currently do not have demand meters.

NRDC/Pace:

- The current delivery rate structures continue to link distribution utilities' revenues and their profits to sales.
- Fixed charges send the wrong price signals to customers, eliminating a large portion of their incentive to use electricity efficiently or invest in technologies even when these investments would reduce the long-term costs of the distribution system.
- High fixed charges are inequitable for low or fixed-income customers and customers that use less than the average amount of energy.
- The Commission's movement toward shifting costs from volumetric to fixed charges for residential customers has been relatively limited and still leaves substantial volumetric recoveries.

Nucor Steel Auburn, Inc.:

- In NYSEG's rate case, the Commission approved rate design changes that will recover most revenues from NYSEG's larger customers through fixed charges. Consequently, there should be no appreciable net lost revenue issue to address and an RDM-type vehicle cannot be justified in that context.

Question No. 2.

To the extent that the current delivery rate structures of the electric and/or gas delivery utilities still contain a net lost revenue and profit effect that is significant enough to create these impacts, is the effect more predominant or more of a concern for particular types of customers (i.e., industrial and commercial general service versus smaller commercial and

residential)?

National Grid:

- For the electric non-demand-metered service classes, the distribution delivery charges are in customer and energy charges.
- For gas, the net lost revenue from energy efficiency and conservation efforts is most apparent in the residential natural gas market.

Con Edison/O&R:

- The companies do not believe that their current rate structure provides a material disincentive.

KeySpan Energy Delivery New York and Long Island:

- KeySpan's primary concern is the effect on the residential heating class, as these customers account for approximately 60% of KeySpan's total firm throughput and margin.

New York Power Authority:

- NYPA is unable to assess the degree to which electric delivery utilities in New York are encouraged or discouraged in promoting energy efficiency and related practices as a result of current delivery rate structures.

National Fuel:

- The lost revenue and profit effect is the most significant for residential and small volume non-residential customers.

NYS Attorney General:

- While not uniform, the current delivery rate structures across all rate classes contain a net lost revenue and profit effect.

Central Hudson:

- The current impracticability of demand meters in residential and small commercial (non-demand) classes has led to those classes having recovery of both fixed and variable costs in "volumetric" rates. This is because of a limitation of pre-existing technologies.

NRDC/Pace:

- Utilities' incentive to sell more energy and to discourage investment in energy efficiency continues to be a major concern for all types of customers, since all classes of customers pay at least a portion of their bills based upon volumetric charges.

Nucor Steel Auburn, Inc.:

- In NYSEG's rate case, the Commission approved rate design changes that will recover most revenues from NYSEG's larger customers through fixed charges. Consequently, there should be no appreciable net lost revenue issue to address and a RDM-type vehicle cannot be justified in that context.

Question No. 3.

In October 2001 the Commission issued an Opinion and Order in Case 99-E-1470 approving Guidelines for the Design of Electric Standby Service Rates. As stated on page five of that Order, "The Guidelines recommend fundamental cost-based rate design principles that in most cases avoid reliance on measurements of energy consumed (kWh) for charges for delivery service." In compliance with this Order, all major New York State regulated electric utilities filed class-revenue-neutral Electric Standby Delivery Service tariffs that were subsequently approved by the Commission and remain in effect today. Could the ratemaking principles reflected in the utilities' redesigned cost-based electric standby delivery rates be applied to standard delivery rates to address any existing disincentives, or be used as a target in setting future delivery rates, so as to eventually eliminate the net lost revenue and profit effect of current delivery rates? What would be the barriers to implementing such a methodology for setting future delivery rates?

National Grid:

- The standby rate design principles can be used as guidance for rate design, generally. However, immediate movement for all customer classes requires a balance of competing cost and non-cost objectives, including the attributes of simplicity, understandability, customer acceptability, and administrative feasibility.
- Their implementation will require considerations of rate impacts on specific customers within the service classes.

Con Edison/O&R:

- The companies favor cost-based rates.
- It is vitally important that interested parties have an opportunity to consider specific proposals (as opposed to general proposals or concepts) so that the potential impacts of specific proposals on the customers within a specific utility's service territory can be vetted and studied before they are implemented.

KeySpan Energy Delivery New York and Long Island:

- These principles do not resolve the issue for gas utilities.
- KeySpan and most other gas utilities do not use demand meters, as gas service is not priced on an hourly or daily basis.
- Another potential barrier centers on the bill impacts for certain classes of customers, or certain groups of customers within a class.
- A revenue-neutral, cost-based rate redesign that brings class returns closer to the average return and collects fixed costs in the minimum charge and head block would allow the companies to minimize lost margin and to maintain recovery of the costs to serve each rate class within the rate class.
- The potential bill impacts on customers within the class experiencing rate redesign may pose a barrier to implementation.

New York Power Authority:

- NYPA has not done an analysis of the delivery service tariffs of most of the electric delivery utilities.
- NYPA has done a substantial number of energy efficiency projects in the Con Edison service area with no objections and the full cooperation of Con Edison.
- It is not clear that comparable tariff provisions would work for other kinds of load reduction efforts – or even other distributed generation projects if the load profiles are substantially different, and the imposition of this tariff design might even be counter productive to the institution of some other energy efficiency programs.

National Fuel:

- Rate design changes could be implemented to mitigate the negative consequences of energy efficiency promotion on utility earnings.
- The complexity of explaining such rate changes as well as the billing system upgrade would need to be considered.
- A more practical approach would be to include an annual reconciliation charge mechanism similar to the current gas costs reconciliation mechanism.

NYS Attorney General:

- While severing the link between utility profits and throughput, standby rates still link utility revenues and profits to a volumetric measure – the total load.

- While diminished, the disincentive for utilities to encourage standby customers to reduce power use continues to exist.

Central Hudson:

- This issue is logically flawed in suggesting that the special case of standby customers be generalized. The cost-based rate design principles applied to the special case of standby rates are not generally applicable to "regular" delivery service.
- Standby customers, by definition, do not impose the same relationship between fixed and variable costs on the utility as "regular" customers. Standby customers do not share the same load shapes as "regular" customers and the costing and rate design principles applicable to standby customers differ from those applicable to "regular" customers.

NRDC/Pace:

- The standby ratemaking principles should not be applied to standard delivery rates.
- Application of the standby rates would have the counter productive effect of decreasing investment in energy efficiency and load management by many customers, since the rates superficially appear to be "fixed" and unavoidable.
- Unless the Commission implements a revenue decoupling mechanism to fix this disincentive, the utility incentives to oppose permanent efficiency improvements will remain.
- The standby rate model does not sever the link between customer efficiency investments and behavior and utility revenue.

Nucor Steel Auburn, Inc.:

- Opinion No. 01-4, Standby Rate Guidelines, took pains to make clear that "consideration of changes in delivery service rate design for full-service delivery customers was not the subject of this proceeding and it would, therefore, be inappropriate to conclude that these principles should be applied to delivery service other than standby service at this time."
- The Commission should consider whether all loads that have monthly demands of 50 kW or more, not only those receiving standby service, should be interval metered so that they may take service under more appropriate time based rates.

Question No. 4.

Are there other approaches to redesigning delivery rates that should be considered to further these goals?

National Grid:

- National Grid believes its recommendation for targeted approaches, including revenue reconciliation and its rate designs provide the appropriate platform to achieve the Commission's goals in these policy areas.

Con Edison/O&R:

- While the companies are not aware of any other approaches at this time, it is willing to consider approaches that satisfy the Commission's goal of promoting EE and DG and are consistent with the general principles of rate design.

KeySpan Energy Delivery New York and Long Island:

- Two approaches to redesigning delivery rates that should be considered, preferably in combination, to further these goals are a move toward cost-based rate design, and the establishment of a tracking mechanism that would recover the margin shortfall resulting from lower use per customer.
- A move toward cost-based rate design would shift the fixed costs of providing service out of the tail and penultimate blocks and into the minimum charge or initial rate blocks.
- A mechanism that allows utilities to recover margin lost as a result of energy efficiency programs would remove the utilities' disincentive in the interim.

New York Power Authority:

- Revenue decoupling is an approach whose time has come if energy efficiency and distributed generation is to be further encouraged in New York State.
- There may be other approaches used in other states to further the goal of encouraging greater energy efficiency and the Commission should carefully study these.

National Fuel:

- A combination of greater minimum charge increases and a lost revenue recovery mechanism as mentioned in the previous response, would be a reasonable approach consistent with the gradualism principle of designing utility rates.

NYS Attorney General:

- The goal to remove disincentives can be done through a fixed charge approach or an adjusted rate approach, or some combination of the two.

- The detail of the rate system would be established in a Commission proceeding.

Central Hudson:

- The most appropriate approach is to properly design programs for energy efficiency, renewable technologies, and distributed generation based on correct economic principles, and to provide improved time-of-use price signals to consumers.

NRDC/Pace:

- A revenue decoupling mechanism is the best and only comprehensive approach to realigning utility incentives to support energy efficiency and distributed generation.
- Lost-revenue recovery mechanisms are open to gaming and do not address the revenues lost from policies and technologies that are not part of specific efficiency programs.
- There is no way under a lost-revenue recovery mechanism to recover revenues lost due to drivers of energy efficiency that are external to the utility.

Nucor Steel Auburn, Inc.:

- The Commission should consider whether all loads that have monthly demands of 50 kW or more, not only those receiving standby service, should be interval metered so that they may take service under more appropriate time-based rates.

The following parties did not specifically address Question Nos. 1-4 contained in the Commission's June 26, 2006 Notice Soliciting Comments:

New York State Energy Research and Development Authority
Con Edison Solutions Joint Petition of Various Stake Holders
New York Energy Consumer's Council, Inc.
Multiple Intervenors
New York State Electric & Gas Corporation/Rochester Gas and Electric Corporation
NYS Department of Environmental Conservation
NYS Consumer Protection Board
Public Utility Law Project, and
City of New York and New York Municipal Power Agency

Question No. 5.

What changes, if any, in programs and rate provisions to protect low-usage and low-income customers should be considered in conjunction with any of these proposed changes in rate design?

National Grid:

- The company supports targeted approaches to address the effects of implementing new rate designs or revenue decoupling mechanisms on low-income customers.
- It points out that in its experience, low-income customers are not always low-usage customers.
- It recommends implementation of rate design changes or RDMs gradually to produce acceptable bill impacts for all customers.
- Commission could encourage the utilities or NYSERDA to expand participation in existing low-income efficiency programs, similar to programs recently expanded for National Grid's low-income customers.
- It recommends increasing discounts to low-income customers to mitigate the effects of a rate design change, as National Grid recently expanded a discount from the customer charge for certain of its low-income electric customers.

Con Edison/O&R:

- The companies are not aware of any rate design changes that would be necessary to protect low-income customers. They suggest that targeted programs, like weatherization, are the best ways to promote energy efficiency for low-income customers.

KeySpan Energy Delivery New York and Long Island:

- The companies recommend protections for low-income customers from unacceptable bill impacts.
- They suggest expansion of low-income rate eligibility and periodic review of the parameters of the low-income program, as the company proposed in National Grid/KeySpan merger case, and targeting energy efficiency programs to low-income customers, as KeySpan has done in New England.

New York Power Authority:

- The Commission should be cautious with regard to the impacts of any procedures implemented such that a disproportionate burden is not shifted to low-income customers.

- Mechanisms which include higher minimum charges have a disproportionate effect on low-income customers and discourage individual conservation.
- Although decoupling may have an impact on low-income customers unwilling or unable to participate in energy efficiency programs, it will incent utilities to undertake more low-income energy efficiency programs.

National Fuel:

- The Commission recognized the concerns of low-income customers with implementation of specific rates for NFG.
- Low-income rate concerns are best addressed through rate programs designed specifically for this class of customers.
- In National Fuel territory, low-income customers tend to use more gas for heating than higher income customers because they typically live in older housing stock and are less able to afford energy efficiency improvements.
- Less costly conservation measures already available and low-income energy efficiency education should be incorporated in any outreach plan.

NYS Attorney General:

- Although delivery rates would be adjusted upward should demand be reduced as a result of energy efficiency and distributed generation improvements, bills would tend to stabilize long-term as a result of these efficiencies and improvements.
- Delivery portion of the bill is less than half of the total bill. The supply portion of the bill is subject to most volatility. Reducing the demand for electricity will put downward pressure on wholesale prices and moderate volatility. The resulting effect of reduced consumption on supply price can offset increases in the delivery rate.
- The Commission should continue and expand efforts to provide energy efficiency savings to low-income customers using the Systems Benefits Charge, weatherization, and other energy efficiency upgrades in low-income housing.

NYS CPB:

- Although the NYS CPB does not specifically address Question No. 5 its general comments indicate that a shift from volumetric to fixed delivery rates may not be warranted for public policy reasons since it would result in higher unavoidable charges for low-energy use customers, particularly low-income consumers.

Central Hudson:

- Most rate plans already include extensive low-income programs.
- It is preferable to design energy efficiency, renewable technologies, and DG programs correctly, independent of low-income customer programs.

NRDC/Pace Energy Project:

- Low-income customers benefit most from energy efficiency because their utility bills are disproportionately high.
- Decoupling will assist in further development of energy efficiency programs for low-income customers by facilitating greater utility support for and investment in, energy efficiency.
- Low-usage and low-income customers are harmed by rate design shifts of cost recovery to fixed charges. Higher fixed charges are counter productive since they remove the incentive to conserve. A decoupling mechanism is consistent with current low-income provisions, which include lower fixed charges.

NYSEG/RG&E:

- Although NYSEG/RG&E does not specifically address Question No. 5, they indicate in reply comments that:
  - The link between low-income customers and low usage is incorrect.
  - No special treatment for either low-income or low-usage customers is warranted.
  - Programs to assist low-income are already in place and modification of those initiatives are most appropriately considered in the context of an individual utility rate proceeding.

The City of New York, Con Edison Solutions, Joint Petition of Various Stake Holders, Multiple Intervenors, New York Energy Consumer's Council, Inc., New York Municipal Power Agency, New York State Department of Environmental Conservation, New York State Energy Research Authority, Nucor Steel Auburn, Inc., and Public Utility Law Project did not specifically address Question No. 5.

Question No. 6.

If a utility revenue mechanism is necessary to offset a residual net lost revenue and profit effect that is still significant enough to discourage some electric and/or gas delivery utilities from promoting energy efficiency, renewable technologies and distributed generation, how might such a mechanism be designed to focus better on the desired objectives

and minimize past flaws with general mechanisms of that type? What specific components are necessary to ensure that the mechanism only affects the efficiency disincentives, accounts for larger factors like weather and economic development/load growth, minimizes rate volatility, and minimizes or eliminates longer-term deferrals and true-ups? Are there models in place in other jurisdictions that have addressed these issues?

National Grid:

- In the past, decoupling mechanisms were broadly applied without appropriate rate design to mitigate the level of deferrals. Future decoupling mechanisms should take a focused approach to revenue reconciliation.
- Improved rate designs have mitigated lost revenues.
- Similar to the weather normalization adjustment for gas, decoupling mechanisms should be implemented for costs that are (1) uncontrollable by the utility, (2) variable and unpredictable, and (3) material and of a recurring nature.
- The company believes the Commission can design rates and RDMs that normalize for declining use per customer and facilitate the implementation of policies to promote efficient and environmentally sound energy usage by customers.

Con Edison/O&R:

- The State has already implemented different kinds of decoupling mechanisms, such as decoupling through the use of revenue per customer incentives. The current Con Edison rate plan has lost revenue recovery for specific programs that can be considered a form of "decoupling" that, combined with incentives, provide an appropriate incentive to aggressively implement demand management programs.

KeySpan Energy Delivery New York and Long Island:

- The companies describe two approaches: rate redesign and a revenue recovery mechanism.
- A cost-based rate design effort with customer related costs captured in minimum charge and demand related costs in the initial block would minimize the revenue shortfalls when consumption declines.
- Revenue recovery mechanisms should be designed to recover only the margin lost as a result of energy efficiency programs. Companies could monitor the impact of utility sponsored energy efficiency measures on average customer consumption (margin shortfall from lower use per customer) and calculate the margin reduction associated with those specific measures. Any deficiencies could be recovered in rates in subsequent periods.

- RDM should be designed to retain incentives to add new customers. Absent these incentives, the environmental benefits of promoting energy efficiency may be negated. Growth related margin allows utilities to stay out of rate cases for longer periods of time and lowers rates to all customers in the long term.
- Phase in rate redesign would minimize bill impacts and apply margin adjustment over a past one-year period so deferrals would only extend fifteen months beyond the time of the margin impact.

National Fuel:

- A unit rate annual reconciliation mechanism based on usage per account maintains a utility's incentive to expand customer base while also providing an incentive to promote energy efficiency. Annual variance from usage per account imputed in a rate case would be multiplied by the average margin per account to determine average change in margin per account. The decline in margin per account is multiplied by total accounts to determine total annual margin to be reconciled. Total margin to be recovered would be divided by normalized volumes to determine an annual reconciliation unit charge to be added to the delivery charge.
- It is important to maintain the incentive to connect natural gas customers to the system. Natural gas continues to be the lowest cost, cleanest burning fuel for heating homes and small businesses. The existing earnings sharing mechanisms protect customers from any earnings growth related to economic development/load growth.

NYS Attorney General:

- Revenue decoupling of delivery charges would have little effect on bill volatility because delivery charges represent only a small portion of the bill. Most of the bill volatility continues to be in supply portion.
- Under a fixed delivery rate approach, there will be less volatility in the bills. Under a volume based adjusted rate approach, volatility would not be expected to increase.
- A weather normalization adjustment is an example of an adjustment directly related to power and natural gas use that can be tied to objective records. The Commission already has existing experience in designing and implementing weather normalization clauses. The Commission could tie power and natural gas deliveries to cooling degree days and heating degree days.

Nucor Steel Auburn, Inc.:

- Significant and varied problems in past RDM efforts point to basic error of a blanket approach.
- Any effort to accommodate sales variability factors in order to isolate efficiency effects requires acceptance of a series of forecasts, estimates, and adjustments that are themselves targets of controversy and gaming.
- RDM would be an overly complicated response to an exaggerated problem.

Central Hudson:

- No empirical evidence shows that a "utility revenue mechanism" is necessary on a generic basis.
- Difficulties in designing a generic approach outweigh any potential benefits.
- It is more appropriate to address potential use of a RDM in individual rate proceedings.

NRDC/Pace:

- A significant historical record and large number of examples can be reviewed to develop a RDM that works for NY. Concerns relate to the effects of weather, economic development, volatility, and the resulting long-term deferrals can be addressed.
- Appendix A of the National Action Plan is helpful guidance to designing an RDM and the different options that can be used.
- Lost revenue mechanisms are open to gaming; they also do not address revenues lost from policies and technologies not part of specific efficiency programs. In reply to Con Edison criticism, NRDC/Pace notes that lost revenue mechanism are likely more complex than RDMs, citing recent Con Edison experience with its own highly complex electric lost revenue mechanism which continues to be in dispute.
- NRDC/Pace outlines key design variable alternatives to aid in design of an effective revenue true up mechanism, depending on the goals of the designers:
  - Mechanism
    - Allowed revenues calculated on per customer basis.
    - All classes, or just some, can be included or a different approach for each.
    - Adjustments for changes in number of customers can be incorporated.
  - Indices
    - Allowed revenues generally indexed for predictable changes in cost.

- Include inflation index (national, local, or specific market sectors) that captures the change in cost of utility programs.
- Include productivity index with a fixed level of productivity gains that are expected of the utility, i.e., few tenths of a percent to over one percent annually.
- Allowed revenues can also be adjusted to reflect existing incentives and penalties.

o Weather
- Include or exclude weather related sales fluctuations.
- In its simplest form, RDM shifts all the risk of weather related revenue fluctuations to the customer. The utility always recovers same amount of revenue after true-up and customers face larger true-ups with longer periods between true-ups. This can result in larger swings in bills. However, in the long run customer bills even out just as utilities revenues even out.
- Shifting weather risk back on utilities protects customer in the long term from fluctuations, but does not necessarily minimize bill swings if true-up is still annual or longer.

o Economic Development
- Revenue adjustments can be designed to encourage economic development, i.e., revenue per customer approach.
- Most adjustment mechanisms recouple revenues to some partially, or largely, exogenous measure of growth. This should be done carefully, since the goal of a decoupling mechanism is to encourage the utility to invest in the least cost way of meeting increasing demands for energy services.
- Regional job growth measurement could be incorporated with the utility as an agent for economic development, or conversely, preventing high utility rates from further slowing job growth in recessionary periods.
- RDM should preserve utility incentive to invest in the broad economic health of the service territory.
- RDM should not protect the utility from bearing any of the burdens in an economic downturn.
-

o True-ups
- The more frequent the true-up, the smaller the size. True-up limits can also be set on the size

in any given period so as to provide sensitivity to local economic conditions.
        - True-ups should be done as frequently as necessary to minimize bill fluctuations.
    - Periodic Review
        - Should include a provision that allows for periodic modification, if necessary. However, any party calling for modification bears burden of proof that rates are not just and reasonable.
        - The alternative is periodic Commission reviews of the mechanism.

- In reply to several of the opponents, NRDC/Pace indicates that adoption of an RDM in individual rate cases is an unacceptable option. The Commission should adopt a revenue decoupling mechanism policy due to the disincentive created by existing rate structures, task a working group to develop generic design principles, and then work out details of implementation for each utility as soon as possible.
- In reply to Multiple Intervenors argument that industrial and large commercial users should be exempt from RDM because they are already incented to invest in energy efficiency measures, NRDC/Pace indicate that an RDM is not intended to encourage customers to do energy efficiency, but intended to remove the utilities' incentive to block or hinder anything that will reduce energy use. NRDC and Pace acknowledge that decoupling through increased reliance on fixed charges will reduce customer incentive to invest in energy efficiency, but prefer approach of collecting a true-up through volumetric rates which would increase the incentive.
- In reply to Multiple Intervenors' concern about the rate impacts and rate uncertainty associated with RDM, NRDC and Pace argue that truing up utilities actual revenue recovery to their allowed revenue should on average have no impact on rates and should provide business customers with greater certainty regarding annual bills.

New York Power Authority:

- Indicates it has not studied the issue sufficiently to adequately address Question No. 6.

The City of New York, Con Edison Solutions, Joint Petition of Various Stake Holders, Multiple Intervenors, New York Energy Consumer's Council, Inc., New York Municipal Power Agency, NYS Consumer Protection Board, New York State Department of Environmental Conservation, New York State Electric & Gas Corporation/Rochester Gas & Electric Utility, New York State Energy Research and Development Authority, and Public Utility Law Project did not specifically address Question No. 6.

Question No. 7.

What changes, if any, to the rate of return for the utilities would be appropriate in connection with the implementation of such a mechanism?

National Grid:

- The effect of a change in Commission policy on a utility's return is generally a matter of substantial debate in the context of a rate filing. A rate filing is the time the experts would evaluate the impacts of the changes on the risks and required returns. The resulting terms of a rate plan and the rate order also have significant impact on investors.
- RDMs may lower return requirements by reducing the risk of revenue erosion or increase return requirements by reducing expected revenue growth of the company. However, until the program is finally designed, it is difficult to determine the impact on the utility's return.
- Analyses used to assess utility returns include many risks other than revenue volatility. The effect of an RDM may not be significant to the investment community compared to other business risks, including market/competitive position, fuel/power supply, operating efficiency, regulatory treatment, construction risk/asset concentration, non-utility activities, management, other financial risks including earnings protection, capital structure, cash flow adequacy, and financial flexibility/capital attraction.
- RDM simply changes the method of revenue recovery and does not guarantee a specific revenue stream. The risks to utility revenues will remain, but slightly different than before, i.e., movement to fixed charges may increase regulatory risks due to more frequent revenue requests to offset forgone revenue growth, or increase investment risk associated with adding new customers or with investing in infrastructure to address load increases to existing customers.
- In reply to various parties, NRDC/Pace reiterates that rate of return on equity should not be modified if a revenue

decoupling mechanism is implemented and should be reviewed after thorough consideration of all risks to the utility.

Con Edison/O&R:

- The particular design of a RDM significantly impacts cost recovery, utility investment programs, reliability, economic development, and investor confidence.
- A RDM could increase cost of capital, i.e., increased sales increase utility revenues, but also increase utility expenses. A RDM could eliminate ability to retain increased revenues necessary to meet increased expenses resulting from increased sales or meet costs of load or reliability driven capital investment programs.
- A RDM could protect against revenue loss, but eliminate the ability to increase earnings. That loss of increased earnings opportunity should be taken into account in determining an appropriate return.
- These return issues should be addressed in utility rate cases.

KeySpan Energy Delivery New York and Long Island:

- No adjustment to allowed rate of return should be made with the implementation of a RDM.
- A RDM would not materially change the risk profile of the utility.
- For example, because credit rating agencies assign bond ratings to utilities based on many factors including both business and financial risks, a RDM in and of itself would not be significant enough to cause an upgrade in bond ratings. The impact would actually offset downward pressure on existing ratings by the negative cash flow and earnings impacts of the recent volatility of gas prices. A recent statement from Moody's: "LDCs that have, or soon expect to have, RD (revenue decoupling) stand a better chance than others in being able to maintain their credit ratings or stabilize their credit outlook in the face of adversity."

National Fuel:

- A RDM based on usage per account in the base rate proceeding recognizes the level of usage used in a base rate proceeding where a reasonable rate of return was established.
- Utility still bears all the other financial risks, i.e., general economic conditions, demographic trends in the service territory, connecting accounts, efficient management of the operation of the system, and failure to achieve the imputed level of accounts in a rate case, among others.

- Reductions in return would discourage expansion of the delivery system in the long run and have negative consequences for the competitiveness of the region.

NYS Attorney General:

- Revenue decoupling would shift risk from utilities to customers by unlinking cost recovery and profit from consumption.
- Unclear whether a RDM would make such a difference that there should be a different rate of return.
- Commission should monitor the effects of decoupling and take appropriate action if warranted.

Nucor Steel Auburn, Inc.:

- By design, a RDM transfers the business risk of sales variations from the utility to the customers and, since risk is a significant element in the earnings of a utility, transferring that risk to ratepayers should be reflected in a comparable reduction in the utility's cost of capital and rate of return.
- Exact nature of the risk shift should be a function of the RDM actually proposed.

Central Hudson:

- More appropriate to address potential use of a RDM in individual rate proceedings than to attempt to design a generic solution for the concern that has been hypothesized in the Commission Notice.

NRDC/Pace:

- Due to the limited RDM experience with New York electric and gas utilities, a material change in risk profile cannot be determined without company specific experience.
- RDMs create both upside and downside exposure for shareholders. The utility no longer under-recovers authorized fixed costs if sales fall below expectations, but also loses the opportunity for gains from sales increases.
- Goal of decoupling is to encourage the utility to devote resources to energy efficiency. The imposition of a shareholder return reduction would be counterproductive.
- The only instance of a lowered rate of return as a result of the establishment of a RDM: Maryland Commission imposed a reduction in return linked to adoption of a decoupling mechanism (Baltimore Gas & Electric – 50 basis points) and, in a recent case, overturned the return reduction even though the Commission acknowledged that the RDM insulated

the utility from revenue recovery risks associated with abnormal weather.

- Commission here should not reduce returns due to decoupling. If over time and experience with RDMs, the utilities are better able to manage their assets and risks, the Commission could reconsider the issue.

NYS CPB:

- If well designed, so that ratepayers fund lost profit attributable to utility energy efficiency and load reduction programs, no adjustment to the utility's rate of return is necessary.
- If the mechanism is designed such that it shifts the risks of sales variations due to other factors from the utilities to rate payers, then an adjustment for rate of return is required.

Multiple Intervenors:

- Although Multiple Intervenors does not specifically address this question, in general reply comments, they argue that an RDM should not result in a transfer of business risk from utility shareholders to customers.

New York Power Authority:

- Indicates it has no opinion on Question No. 7.

The City of New York, Con Edison Solutions, Joint Petition of Various Stake Holders, New York Energy Consumer's Council, Inc., New York Municipal Power Agency, New York State Department of Environmental Conservation, New York State Electric & Gas Corporation/Rochester Gas & Electric Corporation, New York State Energy Research and Development Authority, and Public Utility Law Project, did not specifically address Question No. 7.

Question No. 8.

For each rate class, how quickly could the necessary changes in rate design be put into place? Would interim steps in rate design change be necessary or desirable?

National Grid:

- Electric service – The company has no plans to modify current rate designs, which remain in effect through 2011 under the current Merger Rate Plan. Merger Rate Plan does allow certain rate design modifications, generally revenue neutral, but, at this time, the company has no plan to use this provision during the term of the Plan.
- Gas service – Any new mechanism would require negotiation in an individual rate proceeding. The company has no plan

to propose any new rate redesign until next gas rate filing. It is not opposed to considering targeted approaches or limited rate design under current gas rate plan.

- In general reply comments, the company notes that each utility and each industry face differing circumstances. Natural gas service is experiencing declining use per customer due to more efficient appliances and the rise in prices, while electric residential use has increased. Therefore, implementation of an RDM or other rate design changes should be undertaken on an individual company basis in the context of a utility-specific rate proceeding. The company urges that the Commission maintain flexibility in its approach to these policy issues.
- Also in general reply comments, the company indicates it believes that a collaborative process may provide a better understanding of the divergent views and could be used to help develop guiding principles for future rate proceedings that may consider a RDM.

Con Edison/O&R:

- It is inappropriate to make interim changes in the existing rate plans because of the unexpected rate impacts which would be viewed by customers as changing existing rate plan.
- It is difficult to demonstrate the need for a RDM outside of a rate case.

KeySpan Energy Delivery New York and Long Island:

- Once any necessary rate design changes are identified, a RDM mechanism could be put in place in a relatively short time.
- There are no mechanical or logistical barriers.
- Interim steps may be necessary to minimize bill impacts on certain customer classes, or spread the bill impacts over a period to reduce rate shock.

National Fuel:

- Using the approach of a true-up to use per customer, a major rate change would not be required for implementing a RDM (e.g., could be implemented outside of a rate proceeding). It could be implemented on relatively short notice and the company recommends such an approach be implemented as soon as reasonably possible.
- In reply to Multiple Intervenors, the company supports exclusion of large volume commercial and industrial classes.

- In a general reply comment, the company indicates that a gas RDM should be implemented either generically or on an individual utility basis.

NYS Attorney General:

- Commission should institute a proceeding to formulate guiding principles and policies for developing a RDM, which can be implemented at the time a utility applies for a new rate plan. Most of the NY utilities are in existing rate plans through 2007, or later, allowing ample time for the Commission to develop a well-designed RDM.

Central Hudson:

- Central Hudson fundamentally believes that a material disincentive to conservation has not been established (and does not exist), that aside:
  - Changes in rate design should be made consistent with the principle of "gradualism" as part of a case-by-case approach.
  - A RDM is inappropriate in the context of utilities with existing approved rate plans. These plans should not be disturbed during their terms by attempting to overlay a generic RDM.

NRDC/Pace:

- The Commission should require each electric and gas utility to include a RDM in its next rate case and also provide the opportunity to request a mechanism sooner.
- The National Grid/KeySpan merger, and the current Con Ed electric and gas rate plans expiring in 2008 are opportunities for adoption of a RDM.
- The Commission's authority to set just and reasonable rates allows for the ability to impose an alternative rate design mechanism even during the term of existing rate plans.

NYS CPB:

- Although the NYS CPB does not specifically address this question, as next steps they advocate initiating a generic proceeding to establish a general frame work for RDMs in NY.
- Staff of the DPS should develop a "straw man" proposal to present to interested parties as a prelude to development of a proposed framework to be submitted for Commission decision.
- Specific details and utility-specific circumstances would be addressed in rate cases for individual utilities.

Multiple Intervenors:

- Although Multiple Intervenors does not specifically address this question, and they are opposed to the implementation of a RDM, they do indicate in their general comments that if, *arguendo,* RDMs are implemented, industrial and large commercial customers should be exempted from the RDM.
- In general reply to proponents of a generically imposed RDM, they urge the Commission not to require revenue decoupling or any other particular rate design incentives in this proceeding, but if the Commission decides to pursue decoupling, any proposed changes should be addressed in separate utility-specific proceedings where the results of cost of service studies can be evaluated and customer impacts can be considered.

NYSEG/RG&E:

- Although NYSEG/RG&E does not specifically address this question, they indicate delivery utilities do not have a material disincentive against promotion of energy efficiency and, therefore, additional immediate or accelerated action or rate design changes outside the context of an individual utility's rate proceeding are not warranted.
- Examination of additional mechanisms or rate design modifications, including quantitative costs and benefits, should be undertaken on an individual company basis in the context of a utility-specific rate cases. The assessment of comprehensive rate plans appropriately takes into account the impact of any initiative or rate design options on specific customers affected.
- The NYS Attorney General and NRDC/Pace calls for implementation of a RDM in the company's next rate proceeding and the NYS CPB suggestion for institution of a generic proceeding to establish an RDM framework lack merit, since a generic mandate is not likely to achieve the Commission's goals to promote energy efficiency, renewables, and distributed generation.

The City of New York:

- Although The City of New York does not specifically address this question, they recommend in their comments that any RDM program should be fully examined in the context of utility-specific rate cases to begin with rate cases involving natural gas distribution. A second phase should then be established examining electric decoupling measures, and be informed by the gas RDM experience.

New York Power Authority:

- Indicates it has no opinion on Question No. 8.

Con Edison Solutions, Joint Petition of Various Stake Holders, New York Energy Consumer's Council, Inc., New York Municipal Power Agency, Nucor Steel Auburn, Inc., New York State Department of Environmental Conservation, New York State Energy and Research Development Authority, and PULP did not specifically address Question No. 8.