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December 12, 2000

VIA OVER NIGHT MAIL

Hon. Janet Hand Deixler
Secretary
Public Service Commission
Three Empire State Plaza
Albany, New York 12223

Re: Case 96-E-0891 - New York State Electric & Gas Corporation – Electric
Rate/Restructuring - RETAIL ACCESS CREDIT PHASE

Dear Secretary Deixler:

Enclosed are an original and 25 copies of Strategic Power Management's ("Strategic") letter-form Initial Brief in the above referenced proceeding. All parties have been served in accordance with Judge Bouteleiller's December 8, 2000 briefing schedule and service conventions.

The Record Support for an Increased Retail Access Charge is Uncontroverted

In a nutshell, NYSEG has argued that there is insufficient data on which to base an increase in the Retail Access Charge ("RAC") and it should remain at the fixed 3.56 cents per kwh level (exclusive of revenue taxes). Based upon the testimony of NYSEG's own witnesses and the testimony of other Energy Service Companies ("ESCOs") it is abundantly clear that the 3.56 cent RAC is below the current and forward market for energy.

Relying on Natsource¹, a well known electric and gas broker, Drs. Gordon and Kathan accepted subject to check that the Natsource indicative pricing sheet, Exhibit R-8, dated November 22, 2000, revealed the following:

	Calendar Year 2001 (\$ per MWH)	
	<u>Bid</u>	<u>Asked</u>
On Peak	\$49.50	\$51.50
Off Peak	\$28.25	\$32.00

¹ Drs. Gordon and Kathan used Natsource in their pre-filed testimony "because it is a brokerage and it collects data on the forward contracts." SM. 5523.

SM. 5475. This produces an weighted average price of \$40.70. See Appendix A hereto. This is the energy only price and does not include the required installed capacity which is presented as follows:

Calendar Year 2001 (\$ per kw-month)		
	<u>Bid</u>	<u>Asked</u>
Dec-Apr.	\$0.65	\$1.00
May - Oct	\$1.40	\$1.60

The December 8, 2000, Natsource indicative pricing sheet, attached hereto, for Zone A, shows the following pricing:

Calendar Year 2001 (\$ per MWH)		
	<u>Bid</u>	<u>Asked</u>
On Peak	\$52.00	\$55.00
Off Peak	\$31.00	\$37.00

This produces an average price of \$43.17, \$2.47 higher than the November 22 average price for Calendar Year 2001. I-Cap for December 8, 2000 is the same as that quoted for November 22 for the summer capability period.

In just 16 days the weighed average price of energy has increased by \$2.47 per MWH (using the average of the bid-ask prices as the indicative forward price as did Drs. Gordon and Kathan, SM. 5523). Appendix A, attached hereto presents the arithmetic supporting the weighted average price calculations.

Dr. Alan Rosenberg also found Natsource quotes in October, 2000 to indicate forward prices for Calendar Year 2001 to be in excess of \$43.00 per MWH. SM 5851.

Since Natsource is an accepted authority on forward prices, Strategic asks that Your Honor consider this more recent data which confirms the already apparent trend of increasing wholesale energy prices. Accordingly, the market data does not support NYSEG's position that the RAC should be kept at 3.56 cents per kwh.

Moreover, L. Mario DiValentino, Vice President of Strategic, testified as follows:

SPM has been constantly in the market trying to secure a supply of capacity and energy. Based on the number of suppliers we have talked with, both generators and power marketers, we have not been able to receive a supply bid that is less than the NYSEG backout rate.

SM. 5544.

The RAC Should be Based on Actual Market Prices

As is obvious, divining the "correct" fixed RAC is impossible. No market can be predicted in this manner. The electricity markets are even more volatile than most because electricity is a commodity that cannot be stored. Therefore, the sensible approach to the NYSEG RAC is to adopt the Con Edison and Orange and Rockland Market Supply Charge backout methodology. Specifically,

An estimate is made of the month's MSC which is posted and billed to non-retail access customers. At the end of the month, the actual prices are available and the MSC is revised to provide the utility with the opportunity to recover any over or under collections in subsequent periods.

* * * *

... all customers would be charged the NY ISO administered market price for energy and capacity. The resulting MSC would be compared to the current backout rate which is acceptable to NYSEG and the difference would be credited to all customers through the delivery rate.

SM 5545. The MSC methodology has a number of benefits. It eliminates the guess work of arbitrarily trying to predict the market which is required when a fixed or a shaped backout credit is used. Of course, fixed RACs are totally insensitive to changing market conditions, particularly one that is so volatile. The utilities that use the MSC approach seem to have greater success in maintaining or increasing retail access customer participation. Finally, it is noted that the NYSEG retail access customer participation levels are static or declining slightly. This is consistent with the fact that the market price is significantly higher than the backout and it is expected based on forward price data to remain that way.

NYSEG has argued that the RAC should not be changed because the NY ISO administered markets are defective. Strategic agrees that the NY ISO markets continue to need improvement. However, the defects in the marketplace apply to all market participants. There is no such thing as a perfect market. For example, it has been observed that the New York Stock Exchange provides better execution as measured by the bid-asked spread than NASDAQ. See, for example, The New York Times, Business Section, December 11, 2000. To fail to fix the RAC until the NY ISO markets are less defective or near perfect is nothing more than a red-herring. NYSEG's position is no doubt inspired by the fact that NYSEG is economically harmed if, nothing else changes, and the RAC is increased. SM. 5434. That financial harm can be mitigated as the following section reveals.

NYSEG's Actual Over Earnings Can Support a Market Supply Charge RAC

Notwithstanding the NYSEG restructuring settlement, this Commission has a statutory obligation to ensure, to the best of its ability, that the rates all customers pay are just and reasonable. There is little doubt that courts in this state will not overturn a Commission modification to a settlement agreement where the circumstances are so changed from that which was originally contemplated or an oversight occurred when the agreement was approved. In this case, the record reflects actual earnings in excess of 24% on equity based on NYSEG's capital structure for the twelve months ended, December 31, 1999. Exh. R-10. The "as calculated" ROE in accordance with the settlement agreement uses the pre-divestiture rate base and, thus, shows earnings at more traditional levels. The problem with this calculation is that it produces unjust and unreasonable rates. Rates that are too high. Rates that do not reflect the constitutional standards that protect both the shareholders and the ratepayers as discussed many years ago in the seminal *Hope* and *Bluefield* cases.

Further compounding the over earnings situation is the fact that not even a single penny of the merger savings that will accrue due to the acquisition of several New England utilities has been identified. In fact, it appears that NYSEG has not complied with the settlement agreement since it has failed to file with this Commission the contemplated merger savings report. Strategic suggests that this default provides the Commission with more than ample grounds to fashion a remedy that could produce just and reasonable rates while simultaneously stimulating the retail access program. Specifically, the Commission should order that any excess earnings or projected merger savings be used first to offset the financial harm that would be experienced by NYSEG if the current backout is increased as it must.

Respectfully submitted,



Daniel P. Duthie

cc: Service List.

Institutional Energy Brokers

Natsource, Inc.

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(212) 232-5380 or (888) 562-8797

Eastern Power Markets Price Sheet

Dec 8 2000

Notation Guide

1. All prices are 100% firm system power except if noted otherwise;
e.g. 90% means that there is a 90% availability on the power.
2. ICAP= Installed capacity is priced as a function of Kilowatt month
3. Indicative Levels
4. Daily prices are a function of the daily low trade and the daily high trade

NYPP

Month(s)	Demand	Bid (MWh)	Ask (\$/MWh)
Zone A			
Bal Dec	5x16	\$60.00	\$64.00
Bal Dec	5x8,2x24	\$40.00	\$46.00
Jan-Feb	5x16	\$62.00	\$68.00
March	5x16	\$49.00	\$53.00
June	5x16	\$62.00	\$67.00
July-Aug	5x16	\$77.00	\$84.00
Cal 01	5x16	\$52.00	\$55.00
Cal 01	5x8,2x24	\$31.00	\$37.00
Zone G			
Bal Dec	5x16	\$76.00	\$82.00
Jan-Feb	5x16	\$89.00	\$93.00
July-Aug	5x16	\$117.00	\$124.00
Q4	5x16	\$55.00	\$60.00
Cal 01	5x16	\$75.00	\$80.00
Zone J			
Bal Dec	5x16	\$85.00	\$90.00
Jan-Feb	5x16	\$97.00	\$104.00
March	5x16	\$68.00	\$72.00
July-Aug	5x16	\$144.00	\$154.00
Q4	5x16	\$61.00	\$65.00
Cal 01	5x16	\$85.00	\$90.00
ICAP			
May-Oct		\$1.40	\$1.80

CALL Greg Woysner or Tom Kelly at
888-674-7693 or 212-232-5380 FOR UPDATED MARKETS.
Please Note: All prices are for indication purposes only.

Appendix A

CALCULATION OF NATSOURCE DECEMBER 8, 2000 AVERAGE PRICE ZONE A

	Weeks	Days	Hours	Bid	Asked	Mid-point	Total
On Peak	52	5	16	\$52.00	\$55.00	53.5	\$222,560
Off Peak	52	2	24	\$31.00	\$37.00	34	\$84,864
	52	5	8	\$31.00	\$37.00	34	\$70,720
				Weighted Average			\$43.17

CALCULATION OF NATSOURCE NOVEMBER 22, 2000 AVERAGE PRICE ZONE A

	Weeks	Days	Hours	Bid	Asked	Mid-point	Total
On Peak	52	5	16	\$49.50	\$51.50	50.5	\$210,080
Off Peak	52	2	24	\$31.00	\$28.25	32	\$79,872
	52	5	8	\$31.00	\$28.25	32	\$66,560
				Weighted Average			\$40.70
				Increase			\$2.47