BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

In the Matter of

Corning Natural Gas

Case 16-G-0369

October 2016

Prepared Testimony of:

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Department of Public Service
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Q. Please state your name and business address.

A. My name is Allison Esposito. My business address is Three Empire State Plaza, Albany, NY 12223.

Q. By whom are you employed and in what capacity?

A. I am employed by the Department of Public Service as a Utility Supervisor in the Office of Accounting, Audits and Finance.

Q. What is your educational and business experience?

A. I graduated from Cornell University in 2001 with a Bachelor's degree in Government. I received a Master's degree in Accounting in 2004 from the State University of New York at Albany. In 2005, I became a certified public accountant in New York State. From July 2004 through May 2007, I worked as an auditor for PricewaterhouseCoopers in Albany, NY. In this position, I performed financial statement audits and Sarbanes-Oxley compliance audits for a number of companies in various industries. From May 2007 through May 2008, I supervised the expenses' department at the Golub Corporation in Schenectady, NY. I joined the Department of

Public Service in May 2008. Since that time, I have testified in the St. Lawrence Gas Company, Inc. (St. Lawrence) rate proceedings in Case 08-G-1392 and 15-G-0382, the Niagara Mohawk Power Corporation rate proceedings in Cases 10-E-0050, 12-E-0201 and 12-G-0202, and the United Water New York rate proceeding in Case 13-W-0295.

Q. Please explain the scope of your testimony.

A. I am testifying on Corning Natural Gas Corporation's (Corning or the Company) forecast of capitalized fringe benefits, pension and OPEB expenses, allocations, property tax expense and rate case expense.

Q. Are you sponsoring any exhibits?

A. Yes, I am sponsoring three exhibits.

Q. Please briefly describe Exhibit __ (AAE-1)?

A. Exhibit __ (AAE-1) contains the information request (IR) responses referenced in my testimony.

Q. Please briefly describe Exhibit __ (AAE-2)?

A. Exhibit __ (AAE-2) is a compilation of workpapers used to support my adjustment for cost allocations to affiliates.

Q. Please briefly describe Exhibit __ (AAE-3)?

A. Exhibit __ (AAE-3) is a compilation of workpapers used to support my proposed adjustments.

Capitalized Fringe Benefits

Q. Please explain what is included in the "Capitalized Cost" line on the Company's Other O&M schedule.

A. Capitalized Costs include capitalized fringe benefits, such as health insurance and pensions and OPEBs. Capitalized fringe benefits are those that have been incurred by employees while doing work on capital projects. These fringe benefits are capitalized as part of the asset and depreciated over time. The Company's response to IR DPS-348 provided a breakout of these capitalized costs by cost component.

Q. What do you recommend regarding these capitalized fringe benefits?

Q. I recommend that the Rate Year expense reductions associated with each capitalized fringe benefit be removed from Other O&M and identified in their separate costs components on the revenue requirement schedule. This adjustment increases Other O&M by $425,176, as the capitalization credit is no longer being used to decrease the expense, and reduces vacation accrual, insurance costs, pension expense and OPEB expense by $53,869, $165,511, $192,850 and $12,946 respectively.

Q. Why do you recommend this adjustment if there is no net revenue requirement impact?

A. This adjustment will increase transparency and will also improve the ability to audit the Company’s pension and OPEB deferrals going forward.

Q. How will this presentation improve transparency?

A. As previously stated, currently the lump sum “Capitalized Cost” credit includes all the capitalized fringe benefits. As such, there is no easy way to determine how much of the capitalized amount is attributed to each of the fringe benefits cost components. Additionally, by including the capitalized credits in a separate line item, the amount of expense shown for each fringe benefit is inherently overstated and is not a true representation of the Company’s expenses. My proposed presentation will clearly show the amount of each fringe benefit that is capitalized, in its appropriate line item, thereby increasing transparency and accuracy.

Q. How will this presentation improve the ability to audit the pension and OPEB deferrals going forward?

A. The Commission's "Statement of Policy and Order Concerning the Accounting and Ratemaking Treatment for Pensions and Postretirement Benefits Other Than Pensions" (Pension and OPEB Policy Statement) - from Case 91-M-0890 and issued September 7, 1993 - requires utilities to defer the difference between allowed and actual pension and OPEB expenses. Staff must audit these deferrals periodically to ensure compliance with the Pension and OPEB Policy Statement and to ensure overall accuracy. As the pension and OPEB expense allowance includes a reduction for capitalized benefits, the inability to easily discern this capitalized amount greatly impedes Staff's ability to complete its audit. My proposed presentation change will clearly show the amount of capitalized pension and OPEB expense, which will make auditing the deferrals more straightforward.

Q. Do you have any other comments on this issue?

A. Yes. For the reasons stated above, I recommend that the Company follow this presentation of capitalized fringe benefits in all filings with the Commission going forward.

Pension Expense and Deferrals

Q. What is the Company's Rate Year pension expense forecast?

A. As shown in Company Exhibit __ (CNG-5), Schedule 8, the Company's projection of the Rate Year pension expense is $1,067,583.

Q. How did the Company calculate this expense amount?

A. The Company forecast the Rate Year pension expense as equaling the net periodic pension cost for the year ending September 30, 2016, per its actuary's report.

Q. Does the balance include any amortization of the deferred pension balance?

A. No, according to the response to IR DPS-195, the

Company forecast a deferral balance of approximately zero as of the beginning of the Rate Year. Therefore, the Company did not include any amortization in the Rate Year expense forecast.

Q. Do you agree with the Company's Rate Year projection for pension expense?

A. No, I recommend three adjustments related to Rate Year pension expense.

Q. Please explain your first adjustment.

A. Currently all pension and OPEB expense, both the current portion and any amortizations, are included on one line item in the revenue requirement. I recommend that the Rate Year pension expense allowance and the Rate Year amortization of any pension deferral balance be removed from this combined line and identified in separate cost components on the revenue requirement schedule. This adjustment decreases the Pensions and OPEBs expense by $1,067,583 and increases Pension Expense – Current by $1,067,583.

Q. Why recommend this adjustment if there is no net revenue requirement impact?

A. This adjustment will increase transparency and also improve Staff’s ability to audit the Company’s pension and OPEB deferrals going forward. I previously explained these issues of transparency and ease of audit when I addressed capitalized fringe benefits.

Q. Please explain your second adjustment.

A. I recommend reclassifying $192,850 of capitalized Rate Year pension costs from Other O&M into the Pension Expense - Current line item. This adjustment is the same as the one I identified and explained earlier regarding capitalized fringe benefits.

Q. Please explain your third adjustment.

A. My third adjustment reduces the Rate Year amortization expense for the pension deferral balance, which was zero in the Company’s calculation, by $255,981, for a total Rate Year pension amortization expense of negative $255,981.

Q. What is the pension deferral and why is it needed?

A. The Commission's Pension and OPEB Policy Statement requires utilities to track the difference between pension and OPEB expense allowed in rates and pension and OPEB expense actually incurred. This difference is then recorded in a deferral account.

Q. How did you calculate this adjustment?

A. I began with the actual December 31, 2010 pension deferral credit balance of $654,505 that was allowed in Case 11-G-0280. Any deferral activity after that date has not yet been audited by Staff and, as such, I must begin my audit at that point. I then recreated the pension deferral schedule and calculation from that point through the Rate Year ending April 30, 2016. My analysis indicates that the correct deferred pension balance at April 30, 2016 should be a credit of $1,279,907. In other words, as of April 30, 2016, the Company has over-collected pension expense and owes ratepayers $1,279,907. I amortized this deferral balance over five years, which results in a Rate Year amortization expense of negative $255,981. This amortization lowers the overall pension expense. My calculation is included in Exhibit __ (AAE-3).

Q. What are the basic components of your deferral calculation?

A. My calculation includes the actual gross pension costs per the actuary report. These costs are reduced by the amount of pension costs capitalized and amount of pension costs transferred out to affiliates. That net actuarial pension expense is then compared to the pension expense rate allowance to determine the amount over- or under-collected for the period.

Q. Why did you create your own pension deferral schedule, rather than use Corning's schedule?

A. I had difficulty following the Company's schedule as I was unable to determine the exact starting point of the Company's calculation. Additionally, the Company's calculation was missing the capitalization components, which I will discuss later in testimony. As such, it was easier, and more accurate, to recreate the schedule myself, starting from the last approved balance.

Q. What is the cause of the significant difference between the Company's and your balances?

A. The main difference between the Company’s and my deferral balances is that the Company did not include capitalized pension costs in either the pension rate allowance or the actual pension costs incurred in its calculation. However, as the Pension and OPEB policy statement requires adjustments to the deferral for these capitalized costs, the Company’s calculation is incorrect.

Q. Where in the Pension and OPEB Policy Statement does it require accounting for capitalized costs?

A. Appendix A, Page 3 of 20, footnote 1 of the Pension and OPEB Policy Statement states, “For the purpose of calculating this deferral, both the ‘rate allowance’ and ‘pension expense’ shall only include the amount charged to expense accounts (i.e., not charged to construction, depreciation expense and rate base allowance related to capitalized pension costs.)”

Q. Why did you amortize the deferral balance over five years?

A. The five year period is consistent with both the treatment of the deferral balance in the most recent case in which Corning’s rates were set, as well as the Company’s request. I see no reason to change the period at this time.

Q. Does the Company agree with your methodology or calculations?

A. No. IR DPS-349 provided the Company with my calculation of the deferral balance and explicitly asked the Company to point out any errors, corrections or areas of disagreement. The Company responded that it did not agree with my calculation, as the calculation “amounts to the use of a new methodology for the Pension and OPEB reconciliations.” The Company continued that its reconciliation “is consistent with the methodology that has been used in at least the last two rate cases. That methodology was reviewed by Staff and approved by the Commission. Should Staff wish to propose a change in the methodology for Pension and OPEB reconciliation, it should be done on a prospective basis only.”

Q. Do you agree with the Company’s response?

A. No, I disagree with the Company’s response for two reasons. First, the Company is incorrect that my methodology is a “new methodology” for accounting for the Pension and OPEB deferrals. Second, the Company incorrectly states that any changes in methodology should only be done prospectively.

Q. Please explain your first statement, that the Company is incorrect that your methodology is a new methodology.

A. As I’ve previously discussed, the biggest difference between the Company’s and my calculations is that my calculation includes a reduction to both actual pension expense and allowed pension expense for capitalized pension costs, which is explicitly required in the Pension and OPEB Policy Statement. As the Pension and OPEB Policy Statement was approved by the Commission in 1993, it is not a “new” methodology.

Q. Did the Company explain how or why it believes that your methodology is inconsistent with the Pension and OPEB policy statement?

A. No. Although my IR explicitly asked the Company to point to areas of the calculation that are not consistent with the Pension and OPEB Policy

Statement, the Company did not do so. The Company’s IR response simply stated that its calculation was consistent with its prior cases.

Q. Is the Company correct that this is how it has been accounting for pension and OPEB deferrals in prior cases?

A. I cannot speak to the details of the prior cases the Company refers to as I was not a part of those proceedings. However, the fact remains that the Company’s proposed accounting is not consistent with the long-standing Commission policy for these costs and, as such, it must be corrected.

Q. Please explain your second statement that the Company incorrectly asserts that any changes in methodology should only be done prospectively.

A. As I previously stated, my calculation begins with the December 31, 2010 deferral balance that was previously allowed. No deferral activity after that point has been audited by Staff and as such, must be audited. To ignore errors from January 1, 2011 through April 30, 2016 would be negligent.

Q. Does Staff routinely audit deferral balances and make adjustments to those balances before reflecting those balances, whether a net regulatory liability, regulatory asset, or zero, in rates?

A. Yes. Staff and the Commission have an obligation to ensure that, when a company is able to avail itself of deferral authority, before deferred items are reflected in rates, the amount reflected in rates is accurate. In this instance, the accurate deferral balance creates a regulatory liability, however my review, and my and the Commission’s obligation remains the same whether the deferral results in a regulatory asset or liability. I should note that there are instances when a complete audit cannot be performed during the time constraints of a rate proceeding. In such instances, Staff will sometimes reserve its right to complete its audit at a later date and recommend adjustments to the deferral balance at that time.

Q. Please summarize your pension expense forecast for the Rate Year.

A. My projection of the Rate Year pension expense is $874,733 and includes net periodic pension cost of $1,067,583 and a reduction of $192,850 for allocation of the net periodic pension cost to capital. On a separate line item, I have included the Rate Year pension amortization expense of negative $255,981, representing a five year amortization of the deferred pension balance as of April 30, 2016.

OPEB Expense and Deferrals

Q. What is the Company's Rate Year OPEB expense forecast?

A. As shown in Company Exhibit __ (CNG-5), Schedule 8, the Company's projection of the Rate Year OPEB expense is $94,154.

Q. How did the Company calculate this expense amount?

A. The Company's projection of the Rate Year OPEB expense is made up of: (a) net periodic OPEB cost of $71,667; (b) a reduction of $3,096 for the allocation of the net periodic OPEB cost to capital operations at a projected allocation rate 4.32%; and (c) amortization expense of $25,584, which represents a five year amortization of the estimated deferred OPEB expense balance as of the beginning of the Rate Year.

Q. Do you agree with the Company's Rate Year projection for OPEB expense?

A. No, I recommend three adjustments related to OPEB expense.

Q. Please explain your first two adjustments.

A. My first two adjustments are consistent with the presentation adjustments made for pension expense. My first adjustment reclassifies the Rate Year OPEB expense of $68,571 and the Rate Year OPEB deferral amortization expense of $25,584 to their own line items in the revenue requirement. My second adjustment reclassifies $12,946 of capitalized Rate Year OPEB costs from Other O&M into the OPEB Expense - Current line item.

Q. Please explain your third adjustment.

A. My third adjustment reduces the Rate Year amortization expense for the OPEB deferral balance by $69,259 for a total amortization expense of negative $43,675.

Q. What is the OPEB deferral and why is it needed?

A. As with pension expense, the Commission's

Pension and OPEB Policy Statement requires utilities to track the difference between OPEB expense allowed in rates and OPEB expense actually incurred. This difference is then recorded in a deferral account.

Q. How did you calculate this adjustment?

A. I began with the actual December 31, 2010 OPEB deferral balance of $99,650 that was allowed in Case 11-G-0280. Any deferral activity after that date has not yet been audited by Staff and, as such, I must begin my audit at that point. I then recreated the OPEB deferral schedule and calculation from that point through the Rate Year ending April 30, 2016. My analysis indicates the correct deferred OPEB balance at April 30, 2016 is a credit of $218,377. In other words, as of April 30, 2016, the Company has over-collected OPEB expense and owes ratepayers $218,377. I amortized this deferral balance over five years, which results in a Rate Year amortization expense of negative $43,675. This amortization lowers the overall OPEB expense. My calculation is included in Exhibit __ (AAE-3).

Q. What are the basic components of your deferral calculation?

A. My calculation includes the actual gross OPEB costs per the actuary report. These costs are reduced by the OPEB costs capitalized and the OPEB costs transferred out to affiliates. That net actuarial OPEB expense is then compared to the OPEB expense rate allowance to determine the amount over or under collected for the period.

Q. Why did you create your own OPEB deferral schedule, rather than use the Company's schedule?

A. I had difficulty following the Company's schedule as I was unable to determine the exact starting point of their calculation. Additionally, the Company's calculation was incorrectly accounting for the capitalization components, which I will discuss later in testimony. As such, it was easier, and more accurate, to recreate the schedule starting from the last approved balance.

Q. What is the cause of the significant difference between the Company's and your balances?

A. There are two main differences between the

Company's and my balances. First, the Company did not correctly account for capitalized OPEB costs in its deferral calculation. Second, the Company incorrectly accounted for healthcare costs for current retirees, otherwise referred to as pay as you go costs or PAYGO.

Q. Please explain your first point that the Company did not correctly account for capitalized OPEB costs in its deferral calculation.

A. The Company's analysis includes a reduction to the OPEB rate allowance and actual OPEB costs for capitalized costs at a rate of 4.32%. However, the fringe benefit rate should be the same as the capitalized labor rate, which, as shown in the response to IR DPS-275 has ranged from 17.5% to 20.8% since 2011 and is projected to be 19% in the Rate Year.

Q. Why has the Company been using a rate of 4.32%?

A. In response to IR DPS-195, the Company stated that, "The amount is the historical amount and has not changed since at least 2005." However, this response is clearly incorrect as seen in the data provided in response to IR DPS-275.

Q. Please explain your second point that the

Company incorrectly accounted for healthcare care costs for current retirees, otherwise referred to as pay as you go costs or PAYGO.

A. Similar to past practice, the Company has included the cost of postretirement health insurance and life insurance benefits expense for current retirees in health insurance expense. As these are OPEB costs, the rate allowance for these expenses must be included in the OPEB deferral calculation, as required in the Pension and OPEB Policy Statement.

Q. Do these costs need to be included in the actual OPEB expense portion of the deferral calculation as well?

A. No. According to the Statement of Financial Accounting Standards No. 106 - “Employers’ Accounting for Post-Retirement Benefits Other Than Pensions,” otherwise referred to as FAS 106, any OPEB expense should be fully accrued by the date an employee attains full eligibility for the benefit. As such, the actuarial calculation of the net periodic OPEB expense should only include the expense associated with the accrued liabilities for current employees.

Q. Do you have any other comments on the Company's accounting for PAYGO costs?

A. Yes. As I stated, the Company has included PAYGO costs in health insurance expense. I propose a separate adjustment for these costs. I will discuss this adjustment in further detail later in my testimony.

Q. Why did you amortize the deferral balance over five years?

A. Similar to my recommendation for the pension deferral, the five year period is consistent with both the treatment of the deferral balance in the prior case, as well as the Company's request. I see no reason to change the period at this time.

Q. Has the Company found any errors in either your methodology or calculations?

A. No. IR DPS-349 provided the Company with my calculation of the deferral balance and explicitly asked the Company to point out any errors, corrections or areas of disagreement. The Company responded that my calculation is a "new methodology" and should only be applied on a prospective basis. However, the Company did not point out any areas where my calculation was incorrect or inconsistent with the Pension and OPEB Policy Statement.

Q. Do you agree with Corning's assertion that this is a new methodology and should only be applied on a prospective basis?

A. No. I discussed the Company's response to this IR earlier in my testimony on the Pension Expense and Deferrals.

Q. Please summarize your OPEB expense forecast for the Rate Year.

A. I project Rate Year OPEB expense of $58,721, which includes net periodic OPEB cost of $71,667 and a reduction of $12,946 for the allocation of the net periodic OPEB cost to capital. On a separate line item, I include Rate Year expense of negative $43,675, representing a five year amortization of the deferred OPEB balance as of April 30, 2016.

Pension / OPEB Internal Reserve Funding

Q. Please describe the pension and OPEB internal reserve accounts.

A. As explained in the Commission's Pension and

OPEB Policy Statement, companies are expected to make maximum use of tax effective external funding vehicles for both pension and OPEB funds. Funds collected for pension or OPEB costs that are not deposited into external trusts, or dedicated pension or OPEB accounts, must be maintained in internal reserve accounts.

Q. Did the Company provide internal reserve account computations for its pension and OPEB balances?

A. Yes, the Company’s workpapers include its computation of the internal reserve account balances, beginning with the date of inception, January 1, 1993, through September 2015.

Q. Did you audit the Company’s Pension and OPEB internal reserve accounts?

A. No, although I did a cursory review of the internal reserve account calculations, due to the time constraints of the discovery period in this proceeding, I did not perform a complete audit the internal reserve balances.

Q. Did your cursory review indicate any potential issues?

A. Yes. My high level review indicated that there could be potential errors in the Rate Year allowance amounts and the actual cash contribution amounts that are used in the internal reserve balance computations.

Q. What do you recommend regarding the internal reserve?

A. I recommend that, prior to the next rate proceeding for Corning, Staff do a complete and thorough audit of the internal reserve. However, I want to make clear that I cannot agree with the Company’s reported internal reserve balances at this time.

Health Insurance – Pay As You Go

Q. Please explain your adjustment to Health Insurance for PAYGO costs.

A. As I previously discussed, the Company has included the cost of postretirement health insurance and life insurance expense for current retirees, or PAYGO, in health insurance expense. However, according to FAS 106, any OPEB expense should be fully accrued by the date an employee attains full eligibility for the benefit. Therefore, including these costs in health insurance expense is a double count as the expenses have already been recognized and recovered.

Q. How much PAYGO expense is included in health insurance?

A. According to the Company’s response to IR DPS-288, $38,278 of PAYGO costs are included in health insurance.

Q. Did you ask the Company about this apparent double count?

A. Yes. In IR DPS-326, I explicitly asked the Company whether or not this accounting was a double count and, if the Company believed it was not a double count, to explain its position.

Q. How did the Company respond?

A. Rather than answer the questions posed, the Company’s response to the IR stated that “The Company agrees that the retiree costs being recovered through insurance expense should be charged to the OPEB reserve.”

Q. What is your adjustment for the PAYGO costs in health insurance expense?

A. My adjustment reduces health insurance expense by $38,278 to remove the double count.

Affiliate Allocations

Q. Before you discuss the Company’s allocation process, do you have any Exhibits supporting your adjustments to affiliate allocations?

A. Yes. As this is a complicated series of adjustments that can be difficult to follow, I’ve included a number of workpapers in Exhibit __ (AAE-2) to accompany my testimony. Schedule 1 includes the Company’s allocation workpapers that were included in its revenue requirement model. Schedule 2 is a side-by-side comparison of the Company’s and my adjustments by area (i.e., payroll, fringe benefits). Schedule 3 includes workpapers supporting my calculations of the appropriate allocation credits.

Q. Please describe Corning’s corporate structure.

A. Corning is owned by Corning Natural Gas Holding Corporation (Corning Holdco). Other subsidiaries of Corning Holdco include Leatherstocking Natural Gas – Pennsylvania or LNG-PA, Leatherstocking Natural Gas – New York or LNG-NY, which is currently in the development process, and Pike Electric and Gas, which was purchased in September 2016.

Q. Does the Company currently share services and costs with any of these affiliates?

A. Yes, but only in a very limited manner. The Commission's Order Adopting Terms of a Joint Proposal and Approving Formation of a Holding Company, with Modifications and Conditions, issued in Case 12-G-0141 on May 17, 2013 provided that the Chief Executive Officer, Chief Financial Officer, two Vice Presidents and two clerical accountants, all of whom are employed by Corning, could perform services for LNG-NY. A reduction to expense of up to 5% of these employees' salaries was imputed in Corning's revenue requirement.

Q. Are any other Corning services and costs currently shared with any affiliates?

A. No. However, on November 12, 2015, Corning submitted a petition in Case 12-G-0141 - Petition of Corning Natural Gas for Modification of Affiliate Standards (2015 Affiliate Allocation Petition) - requesting the ability to use any of its office personnel to provide services to affiliates. The Company has not requested that it be allowed to use its field personnel to provide services to affiliates.

Q. What is the status of that petition?

A. The petition is currently still under review. However, as stated on page 18 of Company witnesses Sarhangi/Divalentino’s testimony in this proceeding, the Company expects the petition to be approved. As such, a reduction in expenses and capital costs must be imputed to account for the additional allocation of Corning costs to its affiliates in the Rate Year.

Q. Does the Company agree that such an imputation must be made?

A. Yes. As shown in Company Exhibit __ (CNG-5), Schedule 14 and Exhibit __ (CNG-4), Summary respectively, the Company’s Rate Year revenue requirement includes a credit of $469,694 to Other O&M expense and a credit of $439,072 to rate base to represent these additional allocations.

Q. What are the components of the Company’s proposed O&M credit?

A. The Company’s O&M credit includes (a) $313,331 of payroll costs; (b) $154,552 of fringe benefit costs; (c) $11,315 of LNG-NY costs allocated in the historic test year; (d) and $92,417 of accounts payable costs for a total credit of $571,616. This credit is then reduced by (a) $116,299 of payroll costs and (b) $57,365 of fringe benefits that the Company asserts are included in the historic test year for a Rate Year credit of $397,952. These credits are shown in the Company's workpapers, which I've included in Exhibit __ (AAE-2). The Company also has a separately identified credit of $71,742 for Leatherstocking Gas Allocations in its Other O&M schedule. These two credits total $469,694.

Q. What are the components of the Company's rate base credit?

A. The Company's rate base credit consists of $439,072 of land, office space, furniture, computers and other equipment allocated to affiliates.

O&M Credits

Q. Do you agree with the Company's presentation of Rate Year allocation credits to O&M in the revenue requirement?

A. No. As I previously stated, the Company has included the allocation of costs as a credit to Other O&M. However, this credit should be a line item in the O&M schedule to make the credit more clearly identifiable.

Q. Do you agree with the Company's calculation of Rate Year allocation credits to O&M of $469,694?

A. No, I disagree with the Company's calculation of the credits for payroll, fringe benefits, accounts payable and property taxes.

Payroll Allocation

Q. What is the Company's net payroll allocation credit?

A. The Company's net payroll allocation credit is $197,032. This is calculated by taking the calculated Rate Year payroll allocation credit of $313,331, which I will discuss in a moment, and subtracting $116,999 of allocation credits which the Company states was reflected in the historic test year.

Q. Please explain why you disagree with the Company's calculation of the payroll allocation credit.

A. I disagree with the Company's calculation for three reasons. First, the Company has incorrectly excluded a number of employees from its calculation. Second, the Company is comparing gross payroll, i.e., expensed and capitalized payroll, to expensed-only payroll in its credit calculation. And third, I disagree with some of the allocators the Company has used for specific positions.

Q. Please explain your position that the Company has incorrectly excluded a number of employees from its calculation.

A. The Company's Rate Year labor forecast includes 74.5 employees, consisting of 46.5 administrative employees and 28 union employees. The Company's calculation of the payroll allocation credit assumes that 32 of the administrative employees and zero union employees will be performing work for affiliates.

Q. Do you agree with these numbers regarding union employees?

A. Yes. I agree that no union employees will be performing work for affiliates. The union employees are primarily field personnel, which are expressly excluded in the Company's petition regarding cost allocations.

Q. Do you agree with these numbers regarding administrative employees?

A. I disagree with the number of administrative employees that the Company has included. The Company's analysis excludes eight employees that should be included – three customer service representatives, two cashiers, two billing clerks and an operations clerk.

Q. How did the Company explain why it excluded these employees from the calculation of the credit?

A. In response to IR DPS-289, the Company stated that, "The Company's allocation represents the Staffing that will provide services to subsidiary operations. As an example, the Billing Clerk will be hired and has been directly allocation to Pike operations. Pike has hired a general manager and is expected to add some operational personnel…."

Q. Does this explain why these employees will not be allocated?

A. No. For example, although the Company does show one billing clerk that is allocated 100% to Pike, it shows another billing clerk that is allocated to Corning and Pike and two others that are allocated just to Corning. The Company has not provided a reason for this inconsistency. Based on the Company’s response to IR DPS-347, the Pike billing clerk will be located in Corning’s office, along with the other billing clerks. As such, without a clear explanation from Corning, it is more reasonable to assume that all the billing clerks will be performing some work on both Corning and Pike and allocate all of the payroll for these employees accordingly.

Q. Does the Company’s explanation for why the remaining employees have not been allocated seem reasonable?

A. No. The Company did not provide any explanation or justification for excluding the remaining seven employees from the calculation.

Q. Will similar employees be hired to work exclusively at Pike?

A. No. According to the Company’s response to IR DPS-328, the only employees that have been or will be hired to work exclusively at Pike are a General Manager, two gas field personnel and four electric field personnel. Additionally, the Company has not provided any information on other employees that work exclusively for Pike.

Q. How are services currently being performed for Pike?

A. According to the Company’s response to IR DPS-328, services are currently being provided by Orange and Rockland Utilities, Inc., the previous owner of Pike, under a Transition Services Agreement for a maximum of 18 months, i.e., potentially until approximately March 2018. However, once the 2015 Affiliate Allocation Petition is addressed by the New York Commission, the Company plans to provide these services to Pike. As such, these remaining eight Corning employees will be working on Pike and should have their costs allocated.

Q. How much is your adjustment related to the allocation of these additional employees?

A. My adjustment reduces the costs to Corning, both capitalized and expensed, by approximately $188,000.

Q. Do you have any other reasons you disagree with the Company’s calculation of the payroll allocation credit?

A. Yes. The second reason I disagree with the payroll allocation credit is that the Company is incorrectly comparing gross payroll (expensed and capitalized payroll) to expensed-only payroll in its credit calculation.

Q. Please elaborate on this concern.

A. The Company’s calculation begins with gross payroll for the 32 employees previously discussed of $2,180,843. The Company then applies an 81% expense factor to calculate the total amount expensed for these employees of $1,777,138. The Company then allocated the gross payroll for each of these employees, total of $2,180,843, to its affiliates to determine that $1,463,807 should be charged to Corning. Lastly, the Company then compared this amount to the expensed amount of $1,777,138 to arrive at a credit of $313,331.

Q. Do you agree with this calculation?

A. No.

Q. Why not?

A. Comparing the total expensed payroll to the allocated gross payroll creates a mismatch. The correct calculation would be to compare total gross payroll to allocated gross payroll, and then apply the 81% expense ratio to the difference to determine the appropriate credit amount.

Q. Does the Company agree with this correction?

A. Yes, in response to IR DPS-325, the Company stated its agreement that a correction is necessary.

Q. How much is your adjustment to correct for the use of gross versus net figures?

A. My adjustment reduces the costs to Corning, both capitalized and expensed, by approximately $281,933.

Q. Do you have any other reasons you disagree with the Company’s calculation of the payroll allocation credit?

A. Yes. The third reason I disagree with the payroll allocation credit is that I disagree with some of the allocators the Company has used for specific positions.

Q. Please elaborate on this concern.

A. The Company has established a list of nine allocators to charge costs based on drivers such as number of invoices processed, total payroll, fixed assets, etc. It has also established a general allocator based on a three factor formula, as discussed more in Staff witness Malpezzi’s testimony. There were a number of positions that the Company allocated using the general allocator, however a more cost-causative allocator should have been used.

Q. Why is it important to use a cost-causative allocator?

A. It is important to ensure that customers of Corning only pay for costs Corning has incurred on their behalf. Corning’s customers should not be subsidizing the operations of Corning’s affiliates. The most straightforward way to do this would be to first determine if a direct charge to affiliates should be made. Directly charging for costs that can be identified and associated with a specific affiliate is the most appropriate method to charge costs when possible. If costs cannot be directly charged, then they should be allocated using a cost-causative allocator, such as payroll or fixed assets. If there is no obvious cost causation, then the general allocator should be used. The general allocator should only be used as a last resort.

Q. Can you give an example of a position that the Company allocated using the general allocator but that you believe should be allocated on a more cost-causative basis?

A. Yes. One example is the Engineering Manager. The Company allocated these costs using the general allocator. However, as the engineering manager deals with capital planning and plant investment, fixed assets would be a more appropriate allocator. Exhibit __ (AAE-2) shows a breakout of both the employees that I have allocated and the allocation factors I used in my analysis.

Q. How much is your adjustment to correct the use of certain allocators?

A. My adjustment reduces the costs to Corning, both capitalized and expensed, by approximately

$6,000.

Q. How did you calculate your payroll allocation credit?

A. I began with a listing of all employees whose payroll should be allocated to affiliates, which totaled $2,462,269. I then allocated each employee’s payroll based on the appropriate allocation factor, which resulted in Rate Year payroll costs allocated to Corning of $1,645,811 and total payroll allocated to affiliates of $816,458. I applied the payroll expense ratio of 81% to that decrease to arrive at an allocation credit to expense of $661,331 and an allocation credit to rate base of $155,127.

Q. What is your O&M expense adjustment to reflect the appropriate allocation of payroll costs?

A. My adjustment increases the payroll allocation credit by $464,299, from $197,032, which is the Company’s calculated payroll credit of $313,331 less the $116,299 already included in the historic test year, to $661,331. However, as I stated, in response to IR DPS-325, the Company agreed that it had made an error in the calculation of its payroll allocation credit.

In that response, the Company agreed with approximately $267,468 of the $464,299 adjustment, which results in a true contested difference of $196,831.

Q. What is your rate base adjustment to reflect an appropriate allocation of payroll costs?

A. As the Company did not include any allocation credits associated with capitalized payroll costs, my adjustment reduces rate base by the entire capitalized credit of $155,127. This will be discussed further in the rate base section below.

Fringe Benefits Allocation

Q. Please explain why you disagree with the Company’s calculation of the fringe benefits allocation credit?

A. The Company has calculated a fringe benefit overhead rate of 49%. This overhead rate includes the costs of pensions and OPEBs, injuries and damages and health insurance. However, the calculation should also include a component for payroll taxes.

Q. Why did Corning exclude payroll taxes from the rate?

A. According to the Company’s response to IR DPS-325, payroll taxes are capitalized separately by the Company. However, in the IR response, the Company agreed that the overhead rate should include payroll taxes. The Company calculated this updated overhead rate to be 52%.

Q. How did you calculate your fringe benefits allocation credit?

Q. I applied the fringe benefit overhead rate of 52% to the total payroll credit previously discussed of $816,458, to get total fringe benefits allocated to affiliates of $425,681. I then applied the Rate Year capitalization rate of 19% to get an allocation credit to expense of $344,802 and an allocation credit to capital of $80,879.

Q. What is your O&M expense adjustment to reflect an appropriate allocation of fringe benefit costs?

A. My adjustment increases the fringe benefit allocation credit by $247,615, from $97,187, which is the Company’s calculated fringe benefit credit of $154,552 less the $57,365 already included in the historic test year, to $344,802. However, as I stated, in response to IR DPS-325, the Company agreed that the fringe benefit rate should be 52%, rather than the 49% it had previously been using. This agreed to change accounts for approximately $8,631 of the $247,615 adjustment. Additionally, approximately $139,083 is the fringe benefit adjustment associated with the correction to the payroll allocation credit that the Company has already agreed to. Thus, the contested portion of the adjustment is $99,901.

Q. What is your rate base adjustment related to the allocation of fringe benefit costs?

A. As the Company did not include any allocation credits associated with capitalized fringe benefits, my adjustment reduces rate base by the entire capitalized credit of $80,879. This will be discussed further in the rate base section below.

Accounts Payable Allocation

Q. Please explain why you disagree with Corning's calculation of the accounts payable allocation amount of $92,417?

A. The Company’s accounts payable allocation calculation only includes three components – Corporate/SEC fees, Director’s expenses and Director’s fees. However, there are a number of other expenses, such as electricity, internet costs and office supplies that should be allocated to affiliates as well.

Q. Does Corning agree that these additional costs should be allocated?

A. In part. The Company’s response to IR DPS-325, stated that many of the cost components should be allocated to affiliates. However, the Company asserted that costs related to temporary help, petty cash and life insurance should be charged only to Corning.

Q. Why does the Company believe that these costs should be charged only to Corning?

A. In response to IR DPS-325, the Company stated that life insurance is included in the overhead assignment. For petty cash, the Company explained that new hires have no petty cash associated with their positions and that other positions have little or no petty cash or have assigned costs to subsidiary operations directly. The Company did not offer any explanation as to why the temporary help costs should be charged only to Corning.

Q. Why do you disagree with Corning's assertions for fringe benefit costs?

A. The fringe overhead calculation only includes life insurance that is included in the "Insurance" cost component. As such, the life insurance in the "Other O&M" cost component must be included in the allocation calculation.

Q. Why do you disagree with Corning's assertions for petty cash expense?

A. The Company has not offered any support for its assertions that new hires do not have petty cash, or that existing positions that little or no petty cash or that the costs have been directly assigned to affiliates. As there is no support for these statements, these costs should be included in the allocation calculation.

Q. Why do you disagree with Corning's position on temporary help costs?

A. The Company did not offer any explanation for why these costs should be excluded.

Additionally, the Company’s workpapers show that the temporary help expenses are from a temp agency called Express Employment Professionals. A review of this company’s website at www.expresspros.com, indicates that it provides administrative and professional services, as well as commercial services. As Corning will be providing administrative and professional services to its affiliates, these costs should be included in the allocation calculation.

Q. How did you calculate your accounts payable allocation credit of $394,457?

A. I began with a listing of all Rate Year expenses that should be allocated to affiliates, which totaled $1,155,204. I then allocated each expense based on the appropriate allocation factor, which resulted Rate Year expenses allocated to Corning of $760,747, which means that $394,457 must be allocated to affiliates.

Q. What is your adjustment to reflect an appropriate allocation of accounts payable costs?

A. My adjustment increases the accounts payable allocation credit by $302,040, from $92,417 to

$394,457. However, the Company has already agreed to $118,741 of the $302,040 in its response to IR DPS-325. Thus, the contested portion of the adjustment is $183,299.

Property Tax Allocation

Q. Please explain why you disagree with Corning's calculation of the property tax allocation credit.

A. The Company has only included a property tax allocation credit of $1,369, which is the historic test year allocation of property tax expenses to LNG-NY. However, the Company's allocation credit does not include any property taxes allocated to its other affiliates.

Q. How did you calculate your property tax allocation credit?

A. The Company's filing provided a breakdown of office space square footage by area (i.e., display area, customer service manager, open office space). I reviewed this breakdown to determine what space is used by employees that work on affiliates, for example an individual's office area or the restrooms, and what space is used for Corning-only purposes, for example the parts warehouse. For those spaces that are used by employees that work on affiliates, I applied the general allocator to determine how much space should be allocated to Corning and for the space that is Corning-only, I applied 100% to Corning.

Q. What was the result of your calculation?

A. My calculation allocates approximately 80% of the office square footage to Corning. I applied this rate to the property tax expense for the office buildings to arrive at property taxes allocated to affiliates of $20,712.

Q. What is your O&M expense adjustment to reflect the appropriate allocation of property taxes?

A. As the Company’s $1,369 of property tax expense adjustment is buried in the LNG-NY credits of $11,315, my adjustment increases the fringe benefit allocation credit by the entire $20,712.

O&M Allocations Summary

Q. Please summarize your O&M adjustments.

A. I recommend total Rate Year O&M allocation credits of $1,421,302, which consist of a payroll credit of $661,331, fringe benefits credit of $344,802, accounts payable credit of $394,457 and property tax expense credit of $20,712. When compared to the Company’s allocation credit of $469,694, this is an increase of $951,608. However, as I have previously discussed, the Company has already agreed to $533,923 of the $951,608. Therefore the true contested portion of the adjustment is $417,685.

Q. You previously stated that the Company asserts that $116,299 of payroll costs and $57,365 of fringe benefit costs have been allocated to its affiliates in the historic test year. Did you reduce your adjustment for these costs?

A. No. I was unable to determine exactly how much, if any, of these costs were truly allocated out to affiliates in the historic test year. As such, my Rate Year adjustment does not include a modification for these amounts. I will review any additional support for these costs that the Company may provide in its rebuttal testimony.

Rate Base Credits

Q. Do you agree with the Company’s calculation of Rate Year credits to net plant of $439,072?

A. No, I disagree with the Company’s calculation of the Rate Year credit to net plant as the Company’s calculation is based on an incorrect allocation of square footage of office and building space to Corning.

Q. Why is the Company’s calculation incorrect?

A. The Company excluded a number of office space areas from its calculation, for example, the display area, customer service representative space and a common area. In addition, the Company used an incorrect allocator for some of the square footage that it did include in the calculation. For example, the Company allocated 15.37% of the kitchen and second floor restrooms to its affiliates and 5.25% of a different common area and the first floor restrooms to its affiliates. However, the Company has not provided any explanation for these allocation rates, nor are they one of the cost-causative rates the Company developed.

Q. Please explain how you calculated the Rate Year net plant allocation amount.

A. I used the 80% Corning allocation rate of square footage previously discussed and applied that rate to the total net plant associated with land for the office building, office space, furniture, computers and other equipment, which totaled $4,949,093. This calculation resulted in Rate Year net plant allocated to Corning of $3,846,677, which means $1,102,417 should be allocated to affiliates.

Q. What is your adjustment to reflect the appropriate allocation of net plant costs?

A. My adjustment increases the net plant allocation credit by $663,345, from $439,072 to $1,102,417.

Rate Base Allocations Summary

Q. Please summarize your rate base adjustments.

A. I have calculated total Rate Year rate base allocation credits of $1,338,423, which consist of a net plant credit of $1,102,417 and the capitalized payroll credit and capitalized fringe benefit credit of $155,127 and $80,879, respectively, which I previously discussed. When compared to the Company's allocation credit of $439,072, this is an increase of $899,351.

Summary - Allocations

Q. Please summarize your adjustments related to the allocation credits.

A. In summary, I have three adjustments for allocations. My first adjustment simply reclassifies the Company’s credits related to allocations, $469,694, out of Other O&M and into its own line item on the income statement. This adjustment improves the transparency by making the credit more clearly identifiable to the user. Second, I increase the O&M allocation credit by $951,608, from the Company’s credits of $469,694 to $1,421,302. Third, I increase the allocation credit in rate base by $899,351, from the Company’s credit of $439,072 to $1,338,423.

Q. Do you have any other comments on this issue?

A. Yes, I have two additional comments. First, I want to note that as the new allocation structure is not yet in place, the costs both the Company and I have allocated for ratemaking purposes are estimates based on the information available at this time. In future rate proceedings, Corning's rates will be set on the basis of actual costs incurred, rather than estimates and the Company should allocate costs according to its cost allocation manual.

Q. What is your second comment?

A. Most of the Company's allocators do not include any charges to LNG-NY as that affiliate is still in the planning and approval stages. If the Commission approves LNG-NY during the Rate Year, Corning should file updated allocation factors with the Commission reflecting the addition of this affiliate and should use these updated factors to allocate costs.

Rate Case Expense

Q. What is the Company's projection of rate case expense for its efforts in this proceeding?

A. The Company has estimated that it will incur $1 million of rate case expense.

Q. Does any other Staff witness recommend an adjustment to rate case expense?

A. Staff witness Wright recommends an adjustment to remove Moonstone Consulting's fees from rate case expense as the inclusion of these costs in rate case expense would result in a double count. Wright's adjustment reduces rate case expense from the Company's requested $1 million to $702,900.

Q. Is this level of expense reasonable?

A. $1 million of rate case expense, or even the adjusted rate case expense of $702,900, for a company of this size seems excessive.

Q. How did you come to this conclusion?

A. I compared Corning's rate case expense to the rate case expense of St. Lawrence Gas, Inc. (St. Lawrence), which is a similarly-sized utility with recent rate case experience.

Q. How does this level of expenses compare to that of St. Lawrence?

A. As a comparison, in Case 15-G-0382, St. Lawrence requested $250,000 of rate case expense. St. Lawrence increased this requested amount for expenses actually incurred during that proceeding and the Commission Order Establishing Multi-year Rate Plan, which adopted a joint proposal and was issued on July 15, 2016, included an allowance for rate case expense of

$380,000, which is 62% lower than Corning’s request of $1 million.

Q. Is Corning significantly larger than St. Lawrence?

A. No, these two companies are similarly sized. In 2015, St. Lawrence Gas had an average of 15,922 customers and revenues, net of purchased gas costs, of $17,990,960. This is comparable to Corning’s average of 14,814 customers and net revenues of $15,374,006 during the same time period.

Q. Does St. Lawrence’s rate case expense include similar outsourced services?

A. Yes. St. Lawrence hires outside legal counsel, as well as consultants to perform various cost of service studies and to do the majority of the rate case work, such as creating the revenue requirement and responding to IRs.

Q. Are there more interveners in this Corning rate case, as compared to the St. Lawrence rate case?

A. No. In addition to Staff, there are two active parties in this Corning rate case – the Utility Intervention Unit, or UIU, and Multiple Intervenors, or MI. In the 2015 St. Lawrence

Gas rate case, there were three active parties – UIU, MI and Agri-Mark.

Q. Has there been more discovery in the Corning rate case?

A. In the St. Lawrence rate case, Staff issued 320 IRs. To date in the Corning case, Staff has issued 349 IRs. Although Corning has had more IRs, the increased level is not significant and certainly doesn’t justify the significant increase in rate case costs.

Q. Why does Corning believe that the $1 million of rate case expense is reasonable?

A. In response to IR DPS-334, the Company stated that the projected level of rate case expense is consistent with the expense it incurred in previous rate proceedings.

Q. Do you agree with this explanation?

A. I agree that the $1 million forecast is consistent with the expense Corning has incurred in prior cases. However, that fact alone does not support the Company’s assertion that the costs are reasonable.

Q. Please explain.

A. As explained in Corning’s response to IR

DPS-334, the Company has not done any analysis comparing its rate case expense to other utilities, nor has the Company solicited bids for any of the rate case services it utilizes, such as consulting or legal, to determine if the same services could be provided at less cost.

Q. Did Corning explain why it has not solicited bids for these services?

A. The Company states that it has a long standing relationship with its principal rate case service providers and that, despite not doing any solicitations, it believes that the charges by the various providers are consistent with others providing services in the industry. The Company states that it believes "…that it is receiving value from the providers it has retained and does not believe that it would be a worthwhile exercise to solicit bids for rate case services at this time."

Q. Does this demonstrate that the Company's rate case expenses are reasonable?

A. No. Despite these assertions, in actuality the Company has no way of knowing whether or not its costs are reasonable. Without doing any analysis or getting bids from other potential service providers, the Company's assertion that the costs are appropriate is not supportable.

Q. Does the Company offer any other explanation for its level of rate case expenses?

A. In response to IR DPS-334, the Company frequently mentions the significant "discovery demands" as a reason that rate case costs are high. In fact, the Company states that the $1 million of projected expense is "…conservative in that the projection was made before it became apparent that the discovery demands of the current case, which is typically a major driver of costs, would be significantly more onerous and time-consuming than in previous cases." The Company also states that costs could be reduced if "…other parties that generate those costs, especially through discovery, made a greater effort to ask only questions that are necessary and appropriate."

Q. Do you agree with these statements?

A. No. A review of the data provided in response to IR DPS-312, shows that the Company's assertion that discovery work is a major driver of rate case costs is not true. Discovery is only $215,000 of the $1 million forecast, or 22%. The largest driver of the rate case expense by far is the costs associated with litigation, settlement, briefs and statements in support, which constitute $455,000 or 45% of the total rate case expense forecast.

Q. Has the Company done anything to minimize rate case expenses?

A. In response to IR DPS-334, the Company states that it tries to avoid rate cases to minimize expenses. However, this response does not explain how the Company minimizes costs incurred when it actually has a rate proceeding. As the Company has been allowed to recover whatever costs it incurs from ratepayers, the Company has not been incented to try to minimize these costs.

Q. What is the largest driver of the Company’s proposed rate case costs?

A. The Company’s response to IR DPS-312 shows that legal fees are the biggest driver of these costs. Legal fees account for $572,900 of the $1 million of costs, or 57%.

Q. How do Corning’s legal fees compare to legal fees for St Lawrence Gas?

A. The $380,000 rate case allowance for St Lawrence Gas included approximately $121,600 of legal fees. As shown in Exhibit __ (AAE-2), St. Lawrence’s original rate case expense forecast of $250,000 included $80,000 of legal fees. If this $80,000 is increased by the 52% increase in total rate case expense, which is the $250,000 increased to the allowed $380,000, this $80,000 results in $121,600 of allowed legal expense. This $121,600 is $451,300, or 79%, less than Corning’s legal fees.

Q. Is Corning’s counsel located in a more expensive metropolitan area than St Lawrence Gas’s counsel?

A. No. Both St Lawrence and Corning have outside counsel located in a different, larger metropolitan area than the company itself. St. Lawrence’s counsel is located in Boston, Massachusetts and Corning’s counsel is located in Rochester, New York.

Q. Why do you think the Company’s legal costs are at the level they are at?

A. I don’t know. However, the Company has not justified why its costs are reasonable, nor has the Company undertaken the basic, common sense controls to ensure that the costs are not excessive. As such, rate payers should not have to shoulder the burden of these unsupported costs.

Q. What do you recommend regarding rate case expense?

A. I recommend an allowance of $200,000 for rate case legal costs, which is a reduction of $372,900.

Q. How did you arrive at this allowance?

A. My allowance is based on the $120,600 legal expense related to the recent St. Lawrence proceeding. I increased this allowance substantially, by 66%, to recognize that St. Lawrence is only one data point and to acknowledge the Company’s assertion that it has a long-standing relationship with its counsel and, as such, receives additional benefits that should be recognized.

Q. Why have you used St. Lawrence’s rate case allowance as a basis for Corning’s?

A. As I previously explained, St. Lawrence and Corning are similar in size and their rate cases had a similar number of interveners and discovery. Additionally, the rate case expense includes similar outsourced components. As such, St. Lawrence's rate case expense represents an apt comparison for what a company in Corning's position could incur for rate case expense.

Postage

Q. Please explain how the Company forecast Rate Year postage expense.

A. The Company began with the historic test year postage expense of $103,099 and increased that amount by inflation to arrive at a Rate Year forecast of $108,965.

Q. Do you agree with this forecast?

A. No.

Q. Why is this calculation incorrect?

A. On April 10, 2016, the United States Postal Service decreased its postage rate from $0.485 to $0.465 for first class metered mail. As such, there should be a decrease to postage expense to reflect this lower rate.

Q. Does the Company agree?

A. Yes. In response to IR DPS-345, the Company agreed that the Rate Year forecast should be reduced to account for this change. However, the Company’s calculation of this reduction included in its IR response is incorrect.

Q. How did the Company calculate the reduction?

A. The Company took the current Rate Year forecast of $108,965 and reduced it by the 4.1% decrease in postage expense to arrive at a new Rate Year forecast of $104,497.

Q. Why is this incorrect?

A. The Company’s analysis starts with the Rate Year forecast of $108,965, which includes inflation from the end of the historic test year through the Rate Year. However, the inflation must be removed as well. The correct calculation starts with the historic test year expense of $103,099 and reduces that expense by the 4.1% decrease in the postage rate. This results in a Rate Year forecast of $98,871.

Q. What is your adjustment to Rate Year postage expense?

A. My adjustment reduces Rate Year postage expense by $10,092.

Property Taxes

Q. Please explain how the Company derived its Rate Year forecast of property tax expense.

A. The Company began with historic test year property tax expense of $2,147,769 and increased it by its five year average annual property tax inflation rate of 7.5% to arrive at a Rate Year forecast of $2,559,741, as shown in Company Exhibit __ (CNG-3), Schedule 2.

Q. Do you have any adjustments to this forecast?

A. Yes, I have two adjustments to the Rate Year forecast of property tax expense.

Q. Please explain your first adjustment.

A. My first adjustment imputes a reduction to property taxes to account for the Company's recent economic obsolescence filing.

Q. What is economic obsolescence?

A. Economic obsolescence, or EO, refers to the loss in value of property resulting from factors external to the property itself.

Q. What entity approves EO filings?

A. EO is an award granted to a utility by the New York State Office of Real Property Tax Services, or ORPTS, if the utility can show that it has not been achieving its modified required rate of return. This award reduces a company’s assessed value on special franchise property, which results in lower special franchise property taxes.

Q. How can a company apply for an EO award?

A. Every year, utility companies are required to file financial and inventory reports with ORPTS. Along with their inventory report filing, a company can also submit a request for an EO award adjustment.

Q. Has Corning filed for EO?

A. Yes. The Company first filed for EO in 2014 and has also filed for EO awards in 2015 and 2016. The Company received an EO award of 14%, 11% and 13% for each year, respectively. The 2014 award impacted school taxes paid in July 2015 – June 2016 and town and county taxes paid in January 2016 – December 2016. The 2015 award will impact school taxes paid in July 2016 – June 2017 and town and county taxes paid in January

2017 – December 2017. The 2016 award will impact school taxes paid in July 2017 – June 2018 and town and county taxes paid in January 2018 – December 2018.

Q. Will the Company continue to get EO awards in future years?

A. Yes, at least for the next few years. The EO calculation is based on a five year average achieved rate of return as compared to a modified five year average required rate of return. This achieved rate of return includes various ORPTS adjustments and, as such, is different than the earned rate of return the Company includes in its earnings calculations. As this calculation is an average over a five year period, and the EO calculation shows that the Company's achieved rate of return has been below the allowed rate of return, the Company should continue to receive an award.

Q. Does Corning's Rate Year forecast of property taxes include an appropriate reduction for EO?

A. The Company's forecast only includes a small amount of the Rate Year reduction the Company will actually realize.

Q. Why does it only include a portion of EO?

A. The Company's Rate Year forecast of property taxes is based on the historic test year expense, which covers the period January 2015 through December 2015. The Company first filed for EO in 2014 and this award impacted school taxes paid in July 2015 – June 2016 and town and county taxes paid in January 2016 – December 2016. As such, the historic test year expense does not include any impact of EO on town and county taxes and only half of the annual impact on school taxes.

Q. Please explain your adjustment.

A. My adjustment imputes a full year of EO for both school property taxes and town and county property taxes and assumes an EO award of 12.5%. This adjustment results in a decrease to Rate Year property tax expense of $99,586. This adjustment is shown in detail in Exhibit __ (AAE-3).

Q. Why did you use an EO award of 12.5%?

A. Due to the timing of awards and property tax payments, the Rate Year school taxes will include an award of 13%. However the Rate Year town and property taxes will be split, with the first half of the Rate Year including the 2015 award of 11% and the second half of the Rate Year including the 2016 award of 13%. To simplify the analysis and calculation, I used a weighted average of 12.5% to estimate the actual impact on Rate Year property taxes. If the Company would like to provide a more detailed calculation, I will review it for reasonableness and include it in my analysis if appropriate.

Q. Please explain your second adjustment.

A. My second adjustment results from using a four year average increase to forecast Rate Year property tax expense, rather than the five year average the Company has proposed.

Q. Why did Corning use a five year average to forecast Rate Year property tax expense?

A. In the response to IR DPS-241, the Company states that, “A five year average was used in Case 11-G-0280 and is consistent with the Economic Obsolescence (“EO”) calculation allowance. Furthermore, variables such as changes in construction activity, EO and Functional Obsolescence (“FO”) allowances, and municipalities' budgetary needs may impact the Company's tax liability in different years. Therefore, the five year average is the most appropriate way to normalize these one-time events."

Q. Do you agree with this explanation?

A. No. The Company is correct that the EO calculation uses a five year average of achieved versus allowed ROE to calculate an award. However, the ORPTS calculation has nothing to do with a forecast of future expenses. Rather, ORPTS is trying to determine an appropriate reduction to the value of real property.

Q. Do you have any other concerns with this explanation?

A. Yes. While the Company is correct that the use of an average smooths out variations in expense components, the Company's response does not justify why the use of a five year average is appropriate, rather than an average over a different period.

Q. What is a more appropriate average to use to forecast Rate Year property tax expense?

A. A four year historical average is more

appropriate for three reasons.
Q. Please explain your first reason.
A. The Company's workpapers show that property taxes have increased 13.87%, 6.56%, 11.85%, 5.99% and -.76% over the period 2011-2015. Given this data, the large increase in 2011 appears to be an outlier.
Q. Did the Company provide an explanation for the significant increase in 2011?
A. No. IR DPS-180 asked the Company to explain this significant increase, however the Company simply pointed to the raw data that was supplied and did not provide any qualitative explanations or any further explanations or analysis.
Q. Were you able to determine the reason for the significant increase?
A. In part, yes. I reviewed the Company's workpapers, and found that the 2011 increase was driven by a 19.94% increase in the assessment values for state, county and town taxes. This large increase appears to be the result of an increase in assessed values for the Company's properties in four jurisdictions - the Towns of Caton, Erwin, Corning and Virgil. These four

increases represent an increase in assessed value of $4.847 million out of the total increase of $5.687 million, or 85% of the total increase.

Q. What is the reason for these large increases?

A. In the Company’s response to IR DPS-333, the Company states that the increase in the assessment for the Town of Caton was the result of an addition to the Caton Compressor Station; the increase in the assessment for the Town of Erwin was due to main replacement mandated by the Commission; and the increase in the Town of Corning was the result of main replacement and an investment associated with the connection to local production. Additionally, the increase for the town of Virgil was related to the addition of the Company's property in the town of Virgil to the tax rolls as 2011 was the first time that the Company’s expansion in Virgil was included in the Company’s property tax assessments. As these increases are mostly related to one-time investments, they are not representative of future changes and therefore should not be included in the average for the

Rate Year forecast.
Q. What is the second reason you believe supports the use of a four year, rather than a five year average?
A. In 2012, New York State implemented a property tax cap of 2%. This 2% cap is on the amount of property taxes a school, city, town or county can levy. The cap remained at 2% in 2013 and was reduced to 1.46%, 1.62% and .73% in the years 2014-2016. Although there are exceptions to this cap, for example increases related to pension costs, in general the cap has worked to control costs. As such, a historical average ideally would not include a period that was prior to the cap being implemented.
Q. Does the data support your statement that the cap has worked to control costs?
A. Yes. With the exception of 2013, the rate of increase in property taxes has decreased over the last four years. In fact, in 2015, the Company actually had a reduction in property tax expense of -.76%.
Q. Please explain the third reason that you believe supports the use of a four year, rather than a

five year average.

A. The most recent change in property taxes is -.76% and a two or three year average results in an increase of 2.61% or 5.69% respectively. As such, my use of a 5.91% property tax inflator is conservative in nature.

Q. Reflecting the use of a four year average of property tax increases, what do you forecast for Rate Year property tax expense?

A. I began with the historic test year property tax expense of $2,147,769. I then increased this amount by the four year average increase of 5.91% from the end of the historic test year through the Rate Year to arrive at a forecast of Rate Year expense of $2,468,482. This results in a reduction to Rate Year property taxes of $91,259.

Q. Do you recommend a true up for Rate Year property taxes?

A. No. As this is a one year rate case, I do not recommend a property tax true up.

Cash Working Capital

Q. Please explain the cash working capital component of rate base.

A. Cash working capital is an allowance given to the Company to bridge the gap between the time the utility pays its bills for ongoing operating expenses and the time collections are received from customers. Since the 1970s the Commission has used the Federal Energy Regulatory Commission, FERC, working capital formula to measure this lag. The FERC working capital formula begins with a utility’s total operating expenses and subtracts all purchased power expenses as well as all non-cash expenses. A factor of 1/8 is then applied to these net operating expenses to determine the cash working capital requirement that should be included in rate base.

Q. Why is a factor of 1/8 applied to the net operating expenses?

A. The 1/8 factor was calculated by FERC and is designed to be an estimate of the lag between when service is provided and when the Company actually receives payment for services.

Q. How did the Company calculate cash working capital?

A. As shown in Company Exhibit __ (CNG-4), Schedule 5, the Company began with total operating expenses and deducted purchased gas and uncollectible expense to arrive at the net operating expenses.

Q. Do you have any adjustments to this calculation?

A. Yes, I have four adjustments. My first adjustment removes pension and OPEB expenses of $629,801 from the calculation as these expenses are non-cash items. My second adjustment removes amortization expense of negative $3,997 from the calculation as this is also a non-cash item. This amortization expense is associated with the gas supply specialist deferral, explained in the testimony of Staff witness Wright. The third adjustment is a decrease to uncollectible expense of $28,881 based on the uncollectible adjustment explained in the testimony of Staff witness Malpezzi. The fourth adjustment is a decrease to total O&M expenses of $2,116,364 and is a flow through of all of Staff’s O&M adjustments. These four adjustments total $2,717,284. After applying the 1/8 formula, this results in a decrease to cash working capital of $339,661.

Q. Does this complete your testimony at this time?

A. Yes.