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May 18, 2015

VIA ELECTRONIC FILING

Hon. Kathleen H. Burgess
Secretary
New York State Public Service Commission
Three Empire State Plaza
Albany, New York 12223-1350

Re: Case 15-G-0151 – Proceeding on Motion of the Commission to Consider Implementation of a Recovery Mechanism to Support the Accelerated Replacement of Infrastructure on the Natural Gas System

Dear Secretary Burgess:

Pursuant to the Order Instituting Proceeding for a Recovery Mechanism to Accelerate the Replacement of Leak Prone Pipe, issued by the New York State Public Service Commission on April 17, 2015, Multiple Intervenors hereby submits its Comments in the above-referenced proceeding. Multiple Intervenors is an unincorporated association of approximately 60 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State.

Respectfully submitted,

COUCH WHITE, LLP

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STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Proceeding on Motion of the Commission to Consider Implementation of a Recovery Mechanism to Support the Accelerated Replacement of Infrastructure on the Natural Gas System.	**Case 15-G-0151**

COMMENTS OF MULTIPLE INTERVENORS

Dated: May 28, 2015

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PRELIMINARY STATEMENT

Multiple Intervenors, an unincorporated association of approximately 60 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State, hereby submits its Comments in response to the Order Instituting Proceeding for a Recovery Mechanism to Accelerate the Replacement of Leak Prone Pipe ("Order") issued by the New York State Public Service Commission ("Commission") on April 17, 2015 in Case 15-G-0151.[1] For the reasons set forth herein, Multiple Intervenors urges the Commission to adopt the positions advanced in these Comments.

The Commission has instituted this proceeding in an effort to consider acceleration of the current pace of removal and replacement of leak prone pipe ("LPP") inventory within New York's natural gas infrastructure. (Order at 1-2.) The Commission asserts that: "Such accelerated investment in gas infrastructure would increase gas safety and reliability, modernize gas transmission and distribution assets, and benefit the environment." (*Id.* at 2.) Based on the Order, it appears that the Commission already has determined to accelerate the removal and replacement of LPP, and now is considering "where appropriate, implementation of a recovery mechanism to provide funding for accelerated LPP removal and replacement outside the strictures of a traditional major rate proceeding." (*Id.*)

Multiple Intervenors supports reasonable efforts to improve gas safety and reliability. As large energy consumers, many Multiple Intervenors members rely on the reliability of the State's natural gas infrastructure in their operations. The safety of the gas system also is

[1] Case 15-G-0151, *Proceeding on Motion of the Commission to Consider Implementation of a Recovery Mechanism to Support the Accelerated Replacement of Infrastructure on the Natural Gas System*.

important for obvious reasons. That being noted, potential, incremental improvements in gas safety and reliability should be evaluated with due consideration of the incremental costs, and rate impacts on customers, associated with pursuit of such benefits. In this respect, the Order appears lacking in that it advances a proposed goal – reducing the statewide average replacement timeline for LPP to 20 years (*Id.* at 6-7) – but does not contain any analysis of the attendant costs and rate impacts. While Multiple Intervenors is not opposed *per se* to some acceleration of the pace of LPP removal and replacement where warranted, the means for pursuing and implementing such acceleration should not be considered in a vacuum – the potential costs and rate impacts on customers must be analyzed "front and center" in this proceeding.[2]

In addition to the potential overall cost of this initiative, Multiple Intervenors has several concerns with the proposed use of a new surcharge mechanism to pay for it. First, it is not clear that the potential acceleration of LPP removal and replacement needs to – or should – be considered outside of the LDCs' rate proceedings. Where practical, "single issue ratemaking" should be avoided. In a rate proceeding, the potential cost of this initiative could be examined in conjunction with all other "drivers" of rates – including certain declining costs and/or available credits that potentially could be used to offset the impacts of this initiative on customers.

[2] Furthermore, the Commission should not rely only on selective considerations to justify the outcome of this proceeding. For instance, in the Order, the Commission references the current low cost of capital and relatively low commodity prices for natural gas as justifications for accelerating LPP removal and replacement. (*Id.* at 5-6.) While those considerations are relevant to the instant inquiry, so, too, are the facts that (i) New York's economy still is weak, (ii) customers are burdened with some of the highest energy costs in the nation, and (iii) the State's local distribution companies ("LDCs") already have accelerated materially the removal and the replacement of LPP compared to a few short years ago. Additionally, gas commodity prices historically are extremely volatile and there are no guarantees that existing price levels will be maintained throughout this initiative. Thus, there are considerations both for and against implementation of a rapid, and potentially very costly, initiative to remove and replace LPP.

Second, even if, *arguendo*, the Commission wishes to implement this initiative now, without waiting for rate proceedings (a number of which are expected to be filed within the next year), it also is not clear that a new surcharge mechanism should be instituted as opposed to granting the LDCs deferred cost recovery. Multiple Intervenors is concerned that, similar to taxes, a new surcharge mechanism, once implemented, may prove difficult to eliminate. Additionally, a surcharge mechanism would result in immediate rate impacts on customers and potentially allow for the recovery of a material amount of costs prior to any audit of such costs.

Third, if, notwithstanding Multiple Intervenors' positions to the contrary, the Commission elects to institute a new surcharge mechanism for the costs of LPP removal and replacement, such mechanism must be designed in a manner that ensures the fair and equitable allocation and recovery of such costs, consistent with cost-of-service principles. For instance, LPP removal and replacement on the LDCs' gas transmission and/or large-diameter pipeline systems generally benefit all customers and should be allocated to all firm customers. Significantly, however, LPP removal and replacement on the LDCs' distribution and/or small-diameter pipeline systems do not benefit all types of customers directly and, therefore, a different approach should be utilized in allocating and recovering those costs. Perhaps most importantly, the costs of LPP removal and replacement bear no relationship to customer gas volumes delivered and, therefore, the possible use of a volumetric surcharge would be unjust and unreasonable, particularly to large, high-volume customers.[3] Rather, the incremental costs of LPP removal and replacement

[3] In this regard, Multiple Intervenors is not aware of a single rate proceeding wherein LDC capital expenditures on LPP removal and replacement were allocated to the classes on a purely volumetric basis. If the Commission is determined to utilize a new surcharge mechanism, at a minimum the mechanism should operate in a manner consistent with how LPP removal and replacement costs typically are allocated to and recovered from customers in rate proceedings. In other words, the fact that a surcharge mechanism may be utilized in lieu of addressing LPP removal

recoverable from customers should be allocated to all firm service classifications on a neutral basis (*e.g.*, delivery revenues exclusive of fuel) and then recovered from customers.

In the Order, the Commission solicited comments from interested parties on a number of specific questions. Multiple Intervenors' comments in response to selected questions are set forth below.

COMMENTS

Question 1. How should a cost recovery mechanism be designed? The Commission envisions two possibilities, namely a surcharge or a deferral mechanism, or even some combination of the two, however other methods of cost recovery may be relevant. A common approach in the water industry is to recover a return, depreciation expense and property tax expense (to the extent property taxes are not already reconciled) associated with prudent capital investments as shown in the Appendix. The Commission has recently concluded that a surcharge mechanism was the more appropriate mechanism to provide cash flow to fund the acceleration of leak prone pipe. This relative improvement in cash flow could also be beneficial to utility financial metrics reviewed by bond rating agencies.

Response: Initially, the Commission should evaluate the possible acceleration of LPP removal and replacement with full information as to the costs and the customer rate impacts involved. For instance, the Commission states in the Order that:

> New York currently has approximately 12,000 miles of LPP and the gas LDCs are replacing about 400 miles each year, resulting in a range of replacement timelines for gas LDCs between 11 and 45 years. Our goal will be to reduce the statewide average replacement timeline to 20 years and is based on reasonable assumptions that gas LDCs will ramp up their removal and replacement programs.

(*Id.* at 6-7.) Based on the foregoing, it appears that the average replacement timeline currently is approximately 30 years (*i.e.*, 12,000 miles/400 miles each year). What are the projected costs –

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and replacement costs in a rate proceeding should not result in a different allocation and/or recovery of those costs than what typically has been approved in rate proceedings.

and the projected customer rate impacts – of reducing that replacement timeline from 30 years to 20 years? Why is 20 years more appropriate than, for example, 25 years? Multiple Intervenors is not necessarily opposed to accelerating the removal and the replacement of LPP, where justified. Significantly, however, the Commission should not accelerate the existing replacement timeline by one-third (*i.e.*, from 30 years to 20 years) in a vacuum, without full knowledge and consideration of the associated costs and rate impacts – information that has yet to be produced in this proceeding.

To the extent the Commission determines to accelerate the pace of removal and replacement of LPP, Multiple Intervenors advocates that such acceleration and the attendant costs be addressed in rate proceedings. Importantly, many of the rate plans negotiated recently already reflect capital budgets providing for the accelerated removal and replacement of LPP by LDCs. For example, in the Final Joint Proposal filed in the pending Central Hudson Gas & Electric Corporation ("Central Hudson") electric and gas rate proceeding, the signatories negotiated increased capital funding to replace 13, 14 and 15 miles of LPP during the first, second and third rate years, respectively – almost doubling LDC's past replacement efforts.[4] Recently-implemented (or proposed) acceleration efforts should not be ignored or taken for granted.

Moreover, many LDC rate plans, including the aforementioned Central Hudson Joint Proposal, utilize rate moderators that were sized and determined based on the data that was presented in the underlying rate proceedings. In other words, had the parties been made aware that the Commission might approve increased spending levels above and beyond what was negotiated

[4] *See* Cases 14-E-0318, 14-G-0319, *Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Central Hudson Gas & Electric Corporation for Electric and Gas Service*, Final Joint Proposal (filed April 22, 2015) at 51-52.

and/or decided upon in the LDCs' current rate plans, the parties thereto may have pushed for the more aggressive use of customer credits as rate moderators.[5]

The Commission should strive to avoid engaging in single issue ratemaking. The pace and the cost of LPP removal and replacement should be determined in conjunction with an LDC's capital expenditure plans, rates and other considerations addressed typically in rate proceedings. For instance, are there other LDC costs that are declining that could be used to offset increased spending on LPP removal and replacement? Has a particular LDC already accelerated its LPP removal and replacement efforts recently, or is it already under the 20-year replacement timeline proposed in the Order? Have a particular LDC's rates been relatively stable, such that some upward pressure potentially could be tolerated, or has its customers been exposed recently to material rate increases? These are just a few of the highly-relevant considerations that can be examined far more easily in rate proceedings than on a generic, statewide basis.

If, *arguendo*, the Commission decides to order the acceleration of LPP removal and replacement outside of rate proceedings, Multiple Intervenors urges that the attendant costs be deferred until the LDC's next rate proceeding (during which, any acceleration ordered herein can be addressed prospectively). Multiple Intervenors does not favor the institution of new surcharges – customers already are exposed to an "alphabet soup" of surcharges that needs no expansion. Multiple Intervenors also is concerned that, once instituted, a surcharge mechanism may prove difficult to eliminate. The use of deferral accounting would allow all costs purportedly incurred in furtherance of accelerated LPP removal and replacement to be audited fully prior to collection

[5] Accordingly, if, *arguendo*, the Commission directs the State's LDCs to increase spending on LPP removal and replacement outside of rate proceedings, all available gas customer credits should be utilized to pay for such expenditures prior to reliance on deferral accounting and/or a new surcharge mechanism.

from customers – an important consideration given that the LDCs already have existing rate allowances that provide for a certain amount of LPP removal and replacement.[6] Finally, by using deferral accounting, the actual allocation and recovery of the costs authorized herein can be implemented within a rate proceeding, in full knowledge of other cost drivers, any available customer credits, and the resulting customer rate impacts.[7]

Multiple Intervenors has numerous concerns regarding the possible institution of a new surcharge mechanism. First and foremost, the Commission should refrain from implementing volumetric surcharges to recover costs that are not incurred – or result in benefits based upon – energy consumption or deliveries. Where utilized inappropriately, volumetric surcharges can produce inequitable, and exorbitant, rate impacts on large, high-load-factor customers. Such rate impacts contribute to the energy price disadvantage that many businesses experience in New York, and can lead to jobs, production and/or capital investments going elsewhere.

A possible volumetric surcharge for the costs associated with accelerated LPP removal and replacement would be contrary to cost-of-service principles. The cost of removing and replacing LPP has nothing to do with gas consumption. Additionally, the purported benefits of LPP removal and replacement – increased gas safety, reliability and certain environmental benefits – are not realized by customers on a volumetric basis based upon their gas consumption.

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[6] For example, an LDC's rate plan already may provide $X million intended to fund Y miles of LPP removal and replacement. It may prove difficult to distinguish that spending, and any cost overruns associated therewith, from any new spending authorized in this proceeding. A full audit of LDC expenditures would be needed, and cost recovery should await – not precede – the completion thereof.

[7] In this context, cost allocation and cost recovery are very different. Cost allocation refers to how the costs of accelerated LPP removal and replacement should be allocated to the various service classes, while cost recovery refers to the means of collecting a service class's responsibility for such costs. As detailed, *infra*, Multiple Intervenors strongly opposes use of a volumetric surcharge in this instance.

Accordingly, a volumetric surcharge would not be appropriate here, either from a cost causation or beneficiaries pay perspective.

The cost of LPP removal and replacement typically is not (and perhaps never) allocated to service classifications on a volumetric basis in rate proceedings. Accordingly, if, *arguendo*, the Commission determines that a surcharge mechanism should be utilized as opposed to addressing such costs in rate proceedings, it should, at a minimum, ensure that use of a surcharge mechanism does not result in a different (and, in this case, unjustifiable) allocation of LPP removal and replacement costs.

Ideally, the cost of removing and replacing LPP should be allocated to firm customer classes based on the types of pipe involved.[8] For instance, LPP removal and replacement on an LDC's transmission and/or large-diameter pipe system benefits all or virtually all service classifications and the attendant costs should be allocated as such. Conversely, LPP removal and replacement performed on an LDC's distribution and/or small-diameter pipe system only benefits certain service classifications directly, and the costs associated therewith should be allocated entirely to those classes.

To the extent certain LPP removal and replacement benefits all or most service classifications, the costs should be allocated on a neutral basis; for instance, based on each classes' share of delivery revenues net of fuel. Alternatively, these capital costs could be allocated based on each classes' share of the LDC's peak demand. Upon information and belief, such approaches

[8] Inasmuch as interruptible rates currently are based on price and other competitive considerations and not cost of service, there appears no reason why the costs authorized in this proceeding should be allocated to interruptible service classifications. Indeed, to the extent costs were to be so allocated, the application of price and other competitive considerations likely would result in the same total cost being charged to interruptible customers, thereby effectively negating such allocation.

to the allocation of capital expenditures (and deferred expenses) in general, and LPP removal and replacement costs in particular, are far more prevalent (and justified) than an allocation based solely on total volumes delivered. After the costs of any initiative adopted in this proceeding are allocated appropriately to an LDC's respective service classifications, then, if necessary, a surcharge recovery mechanism can be utilized (although, for the numerous reasons set forth above, Multiple Intervenors opposes this approach).

If, *arguendo*, a surcharge mechanism ultimately is utilized, the Commission should implement a "hard cap" on the amounts recovered thereunder, thereby ensuring that customers are not exposed to unacceptable rate impacts. To the extent an LDC's claimed incremental costs exceed such cap, such overage should be deferred and recovered after it has been audited fully. Ideally, any amounts recovered under a surcharge mechanism should be known to customers and relatively stable, thereby avoiding cost and rate impact volatility to the extent practicable.

<u>Question 2</u>. What conditions should the Commission consider imposing on the recovery mechanism? For example, should the recovery mechanism include only work incremental to removal targets when the gas LDC is in a stay-out? This may be obvious for gas LDCs in a rate plan, but LDCs in a stay-out period have mileage targets that continue unless modified by Commission action. Should additional removal miles be required for the cost recovery mechanism to be applicable?

<u>Response</u>: Any type of cost recovery mechanism approved in this proceeding should be limited in its application to the incremental removal and replacement of LPP above what is required or contemplated by an existing rate plan. Similarly, the Commission must ensure that only the costs associated with such incremental work are subject to recovery by a new mechanism.

For instance, if, for example, an LDC's rate plan requires it to remove and replace 10 miles of LPP annually and contains a $10 million annual rate allowance for such work, any new recovery mechanism approved herein should be limited to the costs incurred prudently by the LDC above the required 10 miles. Importantly, if the LDC is experiencing cost overruns, and the first 10 miles of LPP removal and replacement costs $12 million, the incremental $2 million should not be recoverable under the new mechanism but, rather, should be subject to the terms of the rate plan (which may or may not allow recovery of cost overruns for such work). In other words, the possible creation of a new cost recovery mechanism for incremental LPP removal and replacement should not be utilized to recover cost overruns associated with non-incremental work that the LDC already has committed to perform.[9]

Accordingly, to the extent a new cost recovery mechanism is established, it is imperative that the Commission ensure that its application is limited to costs incurred performing LPP removal and replacement that truly is incremental to what already is required under an existing rate plan. Moreover, for the reasons stated, *supra*, incremental cost recovery should (i) not be permitted unless and until an LDC first has utilized all available customer credits to mitigate these additional costs that were not contemplated when its existing rate plan was developed, and (ii) be subject to a hard cap to control spending and customer rate impacts.

Question 3. What is the most effective way to develop a recovery mechanism using a streamlined process that does not run afoul of PSL §66(12)(c) provisions on "major" rate proceedings? In a recent case considering a surcharge mechanism for KeySpan Gas East Corporation d/b/a National Grid, the Commission allowed a surcharge, but capped collections thereunder, in part, to conform with PSL §66(12)(c). The subject of minimizing costs and rate impacts should be a concern. Should there be any consideration of potential offsets to cost recovery, such as incremental revenue (if system constraints are alleviated which enables the LDC to connect additional customers) or operation and maintenance savings?

[9] This may necessitate separate accounting treatment for current and incremental LPP removal and replacement work.

<u>Response</u>: The Commission's recent order regarding KeySpan Gas East Corporation d/b/a National Grid ("KEDLI") does *not* provide an appropriate precedent for development of a recovery mechanism that should be implemented for an initiative to accelerate LPP removal and replacement. In the KEDLI proceeding, the LDC sought approval for incremental spending, via a combination of deferrals and surcharges, of over $700 million, which exceeded the statutory threshold for a major rate increase under Public Service Law ("PSL") section 66(12)(c). That decision departed from long-standing Commission precedent, and arguably the PSL, and should not be followed here.

PSL section 66(12)(c) provides, in pertinent part, that proposed rate increases exceeding the greater of $300,000 or 2.5 percent constitutes "major changes" in rates that require "hearings held upon notice to the public." N.Y. Pub. Serv. Law § 66(12)(c). The Commission should not be striving to create a cost recovery mechanism that somehow subverts the clear legislative intent underlying PSL section 66(12)(c). Instead, the Commission should recognize, and accept, that any new cost recovery mechanism established in this proceeding to recover incremental LPP removal and replacement costs would be subject to the operation of PSL section 66(12)(c). It should not be approving costs that exceed that statutory threshold outside the context of a rate proceeding.

<u>Question 4</u>. When the Commission considers a petition for the recovery mechanism, should it also consider, or even mandate, the modification of any existing safety metrics, such as updating the mileage targets if a gas LDC takes advantage of the cost recovery mechanism?

<u>Response</u>: Multiple Intervenors firmly believes that to the extent additional rate relief is provided to LDCs for LPP removal and replacement, customers should be entitled to receive all benefits commensurate with such accelerated replacement activity, including, but not limited to, any projected reductions in operation and maintenance costs and improved safety performance.

An LDC's safety performance incentive mechanism almost always is established in the context of a rate proceeding, wherein relevant factors can be considered. If, *arguendo*, an LDC now is going to be required – and compensated – to implement incremental LPP removal and replacement at customer expense, then it would be appropriate, and equitable, to credit customers with the benefits of such work, such as a reduced operation and maintenance expense (where warranted) and improved gas safety performance metrics.

CONCLUSION

For all the foregoing reasons, while Multiple Intervenors generally supports reasonable efforts to improve gas safety and reliability, it has several concerns regarding this initiative to possibly accelerate LPP removal and replacement throughout New York State. The projected costs of this initiative must be quantified and considered, along with recent efforts already undertaken by LDCs in furtherance of this goal. Ideally, incremental efforts and costs related to LPP removal and replacement should be considered in rate proceedings. If, *arguendo*, the Commission declines to continue this long-established approach, any incremental costs authorized herein should be deferred, as opposed to the creation of yet another customer surcharge.

If, *arguendo*, the Commission elects to establish a new surcharge, it should ensure that all incremental LPP removal and replacement costs are allocated and recovered from the LDCs' respective firm service classifications, and individual customers, in a fair and equitable manner. For instance, the Commission should *not* allocate these costs on a volumetric basis because such an approach would be highly inequitable to large, high-volume customers and run afoul of basic cost-of-service principles.

Dated: May 18, 2015
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