STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

OPINION NO. 98-8

CASE 94-E-0098 - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Niagara Mohawk Power Corporation for Electric Service.

CASE 94-E-0099 - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Niagara Mohawk Power Corporation for Electric Street Lighting Service.

OPINION AND ORDER ADOPTING TERMS OF SETTLEMENT AGREEMENT SUBJECT TO MODIFICATIONS AND CONDITIONS

Issued and Effective: March 20, 1998

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COMMISSIONERS:

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(Issued and Effective March 20, 1998)

BY THE COMMISSION:

INTRODUCTION

On October 10, 1997, Niagara Mohawk Power Corporation (Niagara Mohawk or the company) filed a Settlement Agreement (Settlement) addressing electric rate, corporate structure, and competitive market matters. In addition to the company, the Settlement was executed by Department of Public Service Staff (Staff); the Settling Independent Power Producers (SIPPs); the Independent Power Producers of New York, Inc. (IPPNY); Sithe/Independence Power Partners, L.P.; Multiple Intervenors (MI); the Steam Host Action Group (SHAG); Pace Energy Project; Natural Resources Defense Council; Adirondack Council; Association for Energy Affordability; New York Rivers United; New York State Community Action Association; Joint Supporters by The E Cubed Company; National Association of Energy Services Companies; IBEW Local 97; State Department of Economic Development, Empire State Development Corporation, and the Job

Development Authority (jointly DED); and, the New York Power Authority (NYPA).

The Settlement includes the Master Restructuring Agreement (MRA) that Niagara Mohawk entered into with 16 independent power producers to ameliorate the above-market prices the company pays for electricity. Both the Settlement and the MRA are considered in this opinion and order.

General Background

In 1990, Niagara Mohawk charged among the lowest electricity prices of the investor-owned utilities operating in New York, even taking into account its costs for two nuclear generation plants. However, between 1990 and 1995, the company’s average retail prices rose by 25% and some customers experienced 35% increases in their total bills. Several factors contributed to this dramatic change. For one thing, the company’s external costs grew rapidly during the early 1990’s. By 1995, they had become nearly half of Niagara Mohawk’s total costs. In addition, gross receipts and real property taxes increased the company’s costs.

By far, the single largest factor contributing to the company’s higher electric prices was increased payments to independent power producers (IPPs) pursuant to power purchase agreements (PPAs) containing prices exceeding the market value of electricity. In 1995, for example, Niagara Mohawk’s total payments to IPPs exceeded $1 billion. These payments were expected to increase over the next 20 years at a rate faster than the forecast rate of inflation.

Niagara Mohawk’s financial difficulties have been compounded by economic recession in its service territory. From 1990 to 1995, electric sales did not grow appreciably. Even today, growth lags in comparison with the downstate region. While economic growth, and other factors, have helped to moderate electricity prices elsewhere, Niagara Mohawk’s electric rates remain relatively high.

In 1993, the company began to reduce its internal costs by implementing a substantial work force reduction. Over five years, it managed to decrease its departmental expenses by almost ten percent and capital spending by a third. With respect to external costs, Niagara Mohawk sought to monitor the IPPs' qualifying facility status, to curtail purchases from IPPs, and it requested assurances from the IPPs that ratepayers will ultimately receive the anticipated benefits of front-loaded contracts that were supported in rates. It also sought to limit the amount paid for IPP generation in excess of contract quantities and to eliminate statutory requirements mandating IPP purchases. The company also challenged various property tax assessments and lobbied for legislative tax reforms. While some of its efforts were successful, Niagara Mohawk did not manage to reduce its external costs appreciably.

Finally, during the 1990's, Niagara Mohawk was under constant pressure to reduce electric prices from customers with access to competitive alternatives. It was also strongly encouraged to stop increasing electric rates.

Procedural History

These cases began in February 1994 when Niagara Mohawk filed a proposal for a traditionally-derived electric rate increase for 1995 and proposed electric price caps for the succeeding four years. The company's 1995 rate proposal was fully litigated; Staff and other parties responded to the company's multi-year rate proposal with alternatives of their own. Following the first round of hearings, new rates were set for 1995 and these proceedings were bifurcated.[1] We directed Niagara Mohawk to continue to devise an acceptable multi-year plan addressing its rate levels, the company's financial

[1] Cases 94-E-0098 et al., Order Setting Electric, Electric Street Lighting, and Gas Rates (issued April 21, 1995); Opinion No. 95-21 (issued December 21, 1995).

security, customer service quality, and certain regulatory changes needed to stimulate competition in the marketplace.

During the summer of 1995, the parties met regularly to address these matters. Administrative Law Judge Jeffrey E. Stockholm served as a Settlement Judge and he aided the parties in their efforts to achieve a negotiated resolution of the issues.[1] Initially, the company provided the parties pertinent information about its financial condition and stated its position on electric restructuring issues.

In October 1995, Niagara Mohawk submitted, only for settlement discussion purposes, a comprehensive, multi-year rate and restructuring proposal commonly referred to as "PowerChoice".[2] For the next nine months, the parties continued negotiations and we developed our approach to restructuring New York's electric utilities. In May 1996, the electric service competitive opportunities decision was issued.[3] Niagara Mohawk was explicitly excepted from the filing requirements of that decision as it had already submitted its PowerChoice proposal.[4]

In June 1996, progress in the PowerChoice settlement discussions stalled while Niagara Mohawk focused its efforts on separate negotiations with the IPPs. Completion of these efforts was necessary for Niagara Mohawk to be able to draft a revised PowerChoice proposal for the parties to consider. On July 9, 1997, the company executed the MRA with 16 SIPPs whose 29 PPAs represent more than 80% of Niagara Mohawk's above-market costs.

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[1] Later on, Administrative Law Judges Jaclyn A. Brilling and Judith A. Lee also provided the parties assistance in their settlement efforts.

[2] Niagara Mohawk decided to make the PowerChoice proposal public to promote a better understanding of the changes under consideration.

[3] Cases 94-E-0952 et al., Competitive Opportunities Proceeding, Opinion No. 96-12 (issued May 20, 1996).

[4] Ibid., pp. 74-75.

Thereafter, on July 23, 1997, the PowerChoice settlement discussions resumed and the company presented a new settlement offer taking into account the MRA. Negotiations facilitated by the Settlement Judge culminated on October 10, 1997 when the Settlement was filed.

In accordance with the October 17, 1997 ruling that set the schedule for these proceedings, the parties prefiled testimony supporting and opposing the Settlement.[1] Evidentiary hearings began on November 18, 1997 and ran for three days. Between November 25 and December 4, 1997 public statement hearings were held at ten locations throughout the company's service territory. Oral statements and written comments were received from residential, commercial, and industrial customers and their representatives. Statements and comments were also received from local government officials and participants in the emerging competitive electric market.

On December 29, 1997, Administrative Law Judge William Bouteiller's recommended decision was issued. The Judge recommended that the MRA be accepted and the financing needed to implement it be approved. He also recommended that the Settlement be adopted subject to three modifications that would shorten it from five to three years, eliminate those customer charge increases that would increase customers' bills, and permit some customers to use on-site generation and to form municipal systems without having to pay some or all of their share of the company's stranded costs.[2]

Briefs on exceptions to the recommended decision were filed on January 9, 1998 by Niagara Mohawk; Staff; the State Consumer Protection Board (CPB); the State Department of Law (DOL); the SIPPs; the National Power Lenders Forum (NPLF); MI; SHAG; Norcen Energy Resources Limited (Norcen); DED; IPPNY; the

[1] Cases 94-E-0098 and 94-E-0099, Ruling Setting Case Schedule, (issued October 17, 1997).

[2] The Judge presented various other recommendations that are discussed below in the context of the parties' exceptions.

Federal Executive Agencies and the Department of Defense (USEA);[1] Retail Council of New York and the Buffalo Commercial Building Association (Retail Council); the City of Oswego;[2] Public Utility Law Project of New York, Inc. (PULP); Enron Capital & Trade Resources Corp. and Wheeled Electric Power Company (Enron/Wepco); Finch, Pruyn & Company, Inc. (Finch); New York State Electric & Gas Corporation (NYSEG); Novus Engineering, P.C.; The Wing Group for the Retail Service Communities; and, the City of Buffalo.[3]

Briefs opposing exceptions were filed on January 16, 1997 by all but nine of the parties filing exceptions[4] and by Central Hudson Gas & Electric Corporation, Long Island Lighting Company, and Rochester Gas and Electric Corporation (jointly Central Hudson/LILCO/RG&E); New York Coalition for On-Site Power Generation (Coalition); ENtrust, LLC; and, ANR Pipeline and Empire State Pipeline.[5]

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[1] USEA generally supports the recommended decision and takes no specific exceptions to it.

[2] The Cities of Fulton and Cohoes, the New York State Conference of Mayors, and the New York State Assessors' Association join in the brief filed by the City of Oswego.

[3] The City of Buffalo's brief was filed by Council Member Alfred T. Coppola.

[4] DOL, NPLF, IPPNY, USEA, Retail Council, NYSEG, PULP, The Wing Group, and the City of Buffalo did not file briefs opposing exceptions.

[5] Written comments continued to be submitted after the recommended decision was issued, including those from the Niagara Chapter of the Sierra Club, State Senator James W. Wright, the New York State Wide Senior Action Council, Inc., and the Genesee Memorial Hospital.

SUMMARY OF THE MRA AND THE SETTLEMENT[1]

The MRA will terminate, restate, or amend 29 PPAs and provide the SIPPs about $3.6 billion in cash,[2] 46 million shares of Niagara Mohawk common stock, and a portfolio of financial and physical delivery contracts. Currently, the 29 PPAs affect 1800 MW of capacity and, on average, 11,500 gWh of energy per year for the next five years. They require Niagara Mohawk to pay substantially more than it would cost the company either to generate the same amount of electricity or to purchase it from others.

Initially, the MRA reduces by about 5,000 gWh Niagara Mohawk's annual purchases from the SIPPs and makes this electricity available for purchase in the competitive energy market. Most of the electricity remaining under contract to Niagara Mohawk will be subject to financial instruments that allow generators to participate fully in the competitive market. New contracts for 5,000-8,000 gWh annually will be executed and indexed to the cost of competitive natural gas supplies.

Various conditions and requirements must be satisfied before Niagara Mohawk and the SIPPs will close the MRA, including the negotiation of restated and amended contracts and their obtaining third-party consents to terminate the existing PPAs and other agreements. The SIPPs expect to enter into new arrangements to restructure their projects economically. Niagara Mohawk must complete its financing arrangements. Both sides must obtain approvals from their boards of directors, shareholders, and partners. While one or more of the SIPPs may, under certain circumstances, drop out of the MRA, Niagara Mohawk remains obliged to close it as long as the company's benefits are not adversely affected by the loss of a particular SIPP.

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[1] This section summarizing the MRA and the Settlement is provided for the convenience of the reader. It does not take precedence over the MRA's or the Settlement's terms.

[2] $50 million of this amount may either be paid in short term notes or cash at the company's option.

The Settlement itself runs for five years. It would reduce average residential and commercial prices by 3.2% during its first three years relative to 1995 levels, including anticipated reductions in the New York State gross receipts tax. Tariff rates for the industrial class would be reduced to below 6¢/kWh which is a reduction of 25% by 2000. Because some industrial customers are already receiving discounts, not all customers will experience the 25% reduction.

During the settlement term, Niagara Mohawk could defer certain unanticipated costs (above the forecasted amounts) for environmental remediation, nuclear decommissioning, and changes in governmental requirements. But it would eliminate the existing fuel adjustment clause (FAC) and various other bill surcharge mechanisms.

In the fourth and fifth years of the settlement period, Niagara Mohawk could file for rate increases, but they would be capped at one percent annually for increases in transmission, distribution, nuclear, customer service costs, and changes in the competitive transition charge (CTC). Beyond this amount, the company’s recovery of deferred costs, certain surcharges, and any auction incentive it earns is limited by the rate of inflation.

The Settlement allows Niagara Mohawk to recover its MRA-related costs. A MRA-related regulatory asset would be established and this liability would be paid off over the next ten years, if not sooner. The Settlement also provides the company a reasonable opportunity to recover its strandable costs; however, Niagara Mohawk has agreed to forgo most of the earnings it would otherwise receive, and the proposed rate plan is premised on the limited recovery of the company’s carrying charges for the MRA-related regulatory asset. Thus, the company would absorb over the next five years approximately $2 billion of its stranded costs due to electric industry restructuring by accepting a very low equity return during the Settlement’s term. Otherwise, stranded costs are recoverable from all customers through the CTC, other fees, and access charges.

The Settlement provides for the divestiture of Niagara Mohawk's fossil and hydro generation assets either at auction or by being spun off to a separate entity. If the auction produces viable results, winning bids would be selected within eleven months of Commission approval of an auction plan. The Settlement allows the company to retain for shareholders a percentage of the auction sale proceeds as an incentive to obtain the maximum amount. Niagara Mohawk may keep its generation assets that receive no positive bids at auction.

The Settlement allows Niagara Mohawk's nuclear facilities to remain with the regulated business while the Commission and the company explore statewide resolutions to nuclear power issues. If this matter is not resolved this way, the company would have to file, no later than 24 months, a plan that analyzes all available solutions for the nuclear facilities, including the feasibility of an auction, transfer, or divestiture. Niagara Mohawk would be allowed to pass through to customers its replacement power costs if a nuclear plant is prudently retired.

This year, large industrial and commercial customers would have full retail access and, by the end of 1999, all customers would be able to choose their own electricity suppliers. Niagara Mohawk would continue to deliver electricity over its transmission and distribution facilities, and it would continue to be the provider of last resort for customers who do not choose another supplier.

The Settlement proposes to decrease electric energy charges and to increase the customer charges that residential and small commercial customers pay. While the classes would, on the whole, experience an overall 3.2% revenue decrease, about 44% of residential and 55% of small commercial customers' bills would increase slightly if this Settlement provision were approved.

Under the Settlement, electric rates would be unbundled into separate charges for transmission, distribution, customer service, electric commodities, and the CTC. Customers will have bundled and unbundled service options, and the ability to choose a fixed or floating CTC. Niagara Mohawk would charge its customers the actual market price for the electricity it provides. Customers who purchase electricity from a competing supplier would see Niagara Mohawk's energy charge "backed out" of their utility bills. Certain customer service costs would also be backed out of customers' bills.

To ensure that customers obtain quality service from Niagara Mohawk, the Settlement includes an incentive mechanism that exposes the company to up to a $6.6 million loss annually if its performance does not measure up to specified standards. To assist low-income customers, the Settlement requires Niagara Mohawk to expand its Low Income Customer Assistance Program (LICAP) and make it available to all qualified customers.

The Settlement provides for a third-party administrator for the system benefits charge and $15 million during each of its first three years for demand-side management, research and development, and low-income energy efficiency programs. The Settlement also contains a number of other environmental and public policy provisions, including those concerning the development of an environmental disclosure mechanism, wind and photovoltaic generation, the donation and sale of land holdings of significance to the environment, and the retirement of sulfur dioxide allowances. It also allows the company to operate as a holding company and contains rules for affiliate transactions and standards for competitive conduct. No additional royalty payments for affiliated companies would be required other than those subsumed by the proposed rate plan. The Settlement also addresses tax refunds Niagara Mohawk may receive, and the disposal of certain real estate interests the company no longer needs pursuant to an Occupancy Cost Reduction Initiative.

EXCEPTIONS

Master Restructuring Agreement

Two parties, PULP and the City of Oswego, except to the Judge's recommendation to accept the MRA and approve the financing needed to execute it. Five other parties--the SIPPs, NPLF, Niagara Mohawk, SHAG, and DED--except to the recommendations about the need for an escrow account to control the payment of the MRA proceeds, and whether we should oversee negotiations between the steam hosts and power producers. Finally, Norcen seeks certain ratemaking presumptions for any costs Niagara Mohawk incurs to obtain third-party releases from the existing PPAs. The parties' arguments are summarized first, followed by a discussion and our conclusions on these matters.

1. Prudence

PULP claims the Settlement's proponents did not demonstrate that the MRA is prudent and that ratepayers should bear its costs. PULP says they failed to meet their burden of proof and that the Judge skirted the issue by limiting his finding. It insists that the MRA's prudence must be addressed directly but, it says, the record is deficient and precludes an affirmative finding.

PULP believes the proponents should have compared the MRA to other alternatives, including a continuation of the status quo. Because Niagara Mohawk did not provide a quantitative, present value analysis of competing alternatives, PULP claims there is no way of knowing whether it is prudent for the company to incur debt to finance the MRA.

PULP also objects to the SIPPs acquiring almost 25% of Niagara Mohawk's common stock. It claims such an ownership interest guarantees the SIPPs two seats on the company's board of directors that they could use to influence company decisions.[1] Rather than support corporate policies that benefit ratepayers, shareholders, and competition, PULP says these directors would favor the SIPPs' interests.

Instead of obtaining cash and common stock, PULP considers it preferable that the SIPPs receive utility debt, such

[1] The SIPPs deny that the MRA provides them any seats on the board of directors. They say it only requires Niagara Mohawk to select two directors from a list of ten candidates who are not affiliated with the SIPPs but who are acceptable to them.

as notes and bonds. Alternatively, it contends Niagara Mohawk should have followed through with its plan to acquire the SIPPs' facilities through eminent domain proceedings. PULP fears that the SIPPs will use their MRA proceeds to purchase Niagara Mohawk generating plants at auction and thereby control the price of electricity in the upstate region. If this were to occur, PULP says, it would defeat our efforts to establish a competitive electricity market.

Finally, PULP challenges any suggestion that Niagara Mohawk must take steps to avoid bankruptcy now. It insists that the company has cash resources to sustain it to the year 2000 and there is ample time for Niagara Mohawk to strike a better deal than the one presented here. If need be, PULP says, the company could obtain temporary rate relief were a true emergency to arise. Thus, PULP urges that other alternatives be explored, including a merger and consolidation of Niagara Mohawk with another electric distribution company, before the MRA is accepted.

The City of Oswego also criticizes the MRA, saying it is neither the only alternative nor the best one available. Rather than worry about bankruptcy, the City says an approach should be established to provide sufficient rate reductions for residential customers, to avoid adverse consequences for local municipalities, and to better serve the public interest.

In response to PULP and Oswego, Niagara Mohawk insists the MRA is prudent, that bankruptcy is the likely alternative, and that corporate insolvency would not serve the public interest.[1] As to PULP's call for a net present value analysis, the company says the MRA payments are less than those required by the existing contracts and it denies that the MRA's benefits can be determined by this measure alone. In addition to providing

[1] As to when the company would become bankrupt, Niagara Mohawk concedes that its insolvency is not imminent; however, it says, steps must be taken to arrest its financial demise. Since it sees no better approach emerging in the future, the company urges that the MRA be approved.

financial savings, Niagara Mohawk points out that the MRA permits it to restructure long-term IPP payments and its debt obligations. It also notes that the MRA provides a basis for rate reductions and a quick transition to competition in the generation market. Also, by forgoing a return on the MRA-related regulatory asset, the company says, it will bear a large portion of the costs of the financing without obtaining recovery from ratepayers.

Niagara Mohawk urges us to reject PULP’s alternatives, noting that the MRA was produced through years of litigation and arms length bargaining. The company denies that the SIPPs could gain corporate control with their equity interest since they cannot act in concert in a competitive market, and because any SIPP with more than a two percent equity interest must execute a written agreement to remain independent of the other power producers.

The SIPPs add that they have neither the intent nor the ability to control Niagara Mohawk’s transmission and distribution system, nor can they influence unduly its board of directors. They point to the large number of producers, their diverse ownership and geographical locations, and to the competition among them. Rather than keep their Niagara Mohawk common stock, the SIPPs say it is more likely they will use it to settle creditors’ claims.

2. Escrow Account

The SIPPs, NPLF, and PULP except to the Judge’s recommendation that the SIPPs provide steam hosts, and others, reasonable assurances of their ability to pay claims and judgments with the MRA-related proceeds and other assets. Absent such assurances, the Judge recommended that we carefully consider the need for an escrow account to serve this purpose.

The SIPPs agree with the Judge’s recommendations concerning other SHAG proposals; however, with respect to the need for any "reasonable assurances," they insist that nothing in the record suggests that they would breach contracts, deplete assets, or attempt to avoid their responsibilities.

The SIPPs note that detailed contracts control their relationships with the steam hosts and that the contracts were executed by knowledgeable executives. The SIPPs also claim there are ample assets available to meet their obligations,[1] and that they are required by state and federal law to deal fairly with suppliers, contractors, and creditors.[2] Given the prevailing contracts and applicable law, the SIPPs insist that no further assurances are needed. They urge us not to provide the steam hosts any new or better rights than those bargained for in the respective contracts.

NPLF also considers it unwise to require the SIPPs to provide any assurances to steam hosts beyond those in their contracts. It objects to the use of regulatory authority either to obtain additional assurances or to review the adequacy of any assurances due the steam hosts. NPLF says it is better to refrain from overseeing power producer/steam host transactions. According to NPLF, an escrow mechanism, or any similar process, could adversely affect the SIPPs’ secured creditors and prevent the MRA’s consummation.[3]

As to any potential Niagara Mohawk liability to the SIPPs’ contractors and suppliers related to the PPAs, the SIPPs say that the MRA provides the company adequate protection because

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[1] In addition to MRA-related proceeds, the SIPPs claim they have physical assets and contractual rights with substantial value.

[2] The SIPPs observe that the New York Debtor and Creditor Law and the Federal Bankruptcy Code protect creditors against fraudulent conveyances and the improper depletion of assets. They also note that the Delaware, New York, and Illinois Revised Uniform Limited Partnership Acts protect creditors by prohibiting limited partnerships from making distributions that result in liabilities exceeding assets.

[3] PULP and the Retail Council are also opposed to the establishment of an escrow account to benefit the steam hosts. They believe the steam hosts’ contracts should determine their rights.

it can insist on adequate releases (or indemnification) or Niagara Mohawk can refuse to close the deal. Niagara Mohawk insists that it is not a party to the SIPPs' dealings with the steam hosts and it has no liability to them. It prefers to remain out of these matters.

In response to the parties who oppose an escrow account, SHAG insists one is needed to address concerns about the power producers' contract performances, and to protect thousands of jobs in the upstate region it asserts are otherwise at risk. SHAG fears the power producers will pursue a strategy of protracted litigation and force them to incur significant costs that they may not be able to recover without an escrow account. In SHAG's opinion, the assurances the SIPPs have provided to date are inadequate.

SHAG adds that the applicable state and federal statutes do not preclude limited partnerships from making wrongful distributions--they merely provide an injured party a cause of action against a partner who receives a fraudulent conveyance. SHAG insists that an escrow account is needed to preserve the MRA proceeds before they can be conveyed to others.

As to the possibility of protracted litigation between IPPs and steam hosts, SHAG says its members cannot afford to incur the operational problems and service interruptions that lawsuits may engender. It also suggests Niagara Mohawk may have to be involved if the disputes go to court. If litigation ensues, SHAG also says there could be job losses and damage to the upstate economy.

Given that the MRA is, in part, attributable to governmental urgings that the SIPPs modify the existing PPAs, SHAG considers it proper for us to require an escrow account for the benefit of contractors, suppliers, and creditors which would serve the public interest by forestalling economic harm to them. SHAG also doubts that the MRA would unravel if an escrow account were established. It insists that the steam hosts are not seeking to improve their positions or take unfair advantage of the power producers. SHAG concludes, saying the steam hosts have provided reasonable estimates of their costs and damages if the SIPPs cease to perform their contractual duties.

3. Steam Host and Power Producer Dealings

Contrary to the Judge's recommendation, SHAG urges us to oversee the negotiations between SIPPs and steam hosts. It claims only we are in a position to assist the parties and address their concerns. According to SHAG, performance delays, interruptions, and uncertain thermal supplies would adversely affect the steam hosts' competitive positions and their capital investments. It asks us to promote good faith negotiations and determine when SIPPs may terminate service to steam hosts. It also proposes that we address regulatory issues that may arise between the parties and ameliorate the steam hosts' economic losses by exempting them from the CTC, other fees, and access charges, when necessary.

DED agrees with SHAG that steam hosts should be relieved of the CTC and other charges and fees. It urges that such relief not be limited to SHAG members but also be made available to other similarly situated firms. DED believes Niagara Mohawk should be kept whole by ratepayers for any revenues it loses. DED also argues that steam host relief is important to the State's economy.

The SIPPs respond that there is little need for us to oversee negotiations with steam hosts. They say there is no strategy to protract negotiations or to assume a litigation stance. The SIPPs point to instances where steam hosts and power producers have reached agreements, and cases where power producers have offered to continue to provide thermal energy under existing contracts. Thus, the SIPPs surmise that only a few steam hosts are threatening the MRA by seeking our involvement in their negotiations.

In its reply, Niagara Mohawk opposes SHAG's and DED's request that steam hosts be relieved of the CTC and other transition charges. The company highlights its poor financial condition, emphasizes its substantial contribution to the Settlement, and complains that relieving steam hosts of the CTC would unfairly burden the company further. In response to DED's proposal that lost revenues be collected from other customers, Niagara Mohawk points out that residential, commercial, and other industrial customers' rates are already too high and should not be increased further to pick up stranded costs that should properly be allocated to the steam hosts.

4. Third-Party Releases and Ratemaking Presumptions

Norcen, a natural gas supplier to three SIPPs which has "backstop agreements" with Niagara Mohawk,[1] considers the MRA imprudent to the extent it does not avoid potential negative effects on third parties such as it. To mitigate the MRA's adverse consequences, Norcen proposed that any costs Niagara Mohawk incurs to obtain third-party consents and releases be presumed to be recoverable in rates. It also proposed that any costs the company incurs to unsuccessfully block third-party rights be presumed to be unrecoverable. The Judge recommended against these presumptions, and Norcen excepts.

Norcen says its approach does not require any final determinations now and it only provides the company the benefit of rebuttable presumptions. It claims such presumptions are the regulatory norm for circumstances like these and they should be made explicit.

Next, Norcen says Niagara Mohawk can afford to make payments to third parties even taking its MRA financing costs into account. It suggests that any additional costs be recovered from ratepayers through the CTC.

Finally, Norcen criticizes the Judge for observing that third parties should look primarily to the SIPPs, and not Niagara Mohawk, for their compensation. In response, it points to the

[1] According to Norcen, these agreements are separate contracts in which Niagara Mohawk has undertaken independent obligations otherwise undertaken by the IPPs.

backstop agreements Niagara Mohawk executed and says the company has a direct contractual relationship with Norcen for which it is responsible. If the SIPPs do not cover the full enterprise value created by the PPAs, then Norcen believes Niagara Mohawk should remain liable to third parties that have valid claims against it.[1]

In response, Niagara Mohawk urges us not to establish any ratemaking presumptions at this time. The company says they are unnecessary and premature until a court determines that Niagara Mohawk is liable to Norcen. The SIPPs also ask us not to prejudge Norcen's claims against the company. They say the way the MRA works, ratepayers do not have any financial risks or liabilities running to Norcen. Finally, ANR Pipeline and Empire State Pipeline urge that no third-party entities affected by the MRA or the Settlement be given preferential treatment. It says none of the third-party interests should receive any precedence over the others.

5. Discussion and Conclusion

Several parties correctly suggest that the MRA's prudence is the first matter that must be decided in these proceedings because much depends upon this determination. To the MRA's credit, few parties have challenged it even though all recognize this issue as one of the most important in these cases. Only PULP and Oswego present alternatives to the MRA and urge us either to postpone a decision or to explore a different avenue. The other parties who raise issues about the MRA do not challenge it; rather, they either assume it will be implemented and seek to assure that their own interests are protected, or they simply seek our assistance to avoid commercial disputes.

Beginning with the procedural issues, we find that the record in these cases is sufficiently developed to evaluate the

[1] In its reply brief, Norcen addresses the reasonable assurances the SIPPs provided in response to the Judge's request and says they are inadequate. Like the steam hosts, Norcen urges that an escrow account be established to protect its interests.

MRA’s prudence. The Settlement’s proponents executed their responsibilities and fulfilled their burden of going forward by providing direct testimony supporting the reasonableness of the MRA and the Settlement. Such testimony was provided by the Settlement’s primary sponsors, including the company, the SIPPs, Staff, and DED.[1] We also find that the Settlement’s opponents were afforded ample opportunity to challenge the MRA’s merits and to provide us all the information they consider relevant to the MRA’s prudence, including alternatives.

Turning to the substantive issues, we find that the MRA is a reasonable method to restructure the company’s finances and provide Niagara Mohawk the means to provide safe and adequate service, at just and reasonable rates, in New York’s emerging competitive electric market. Among other things, the MRA is projected to result in new contracts with IPPs that will afford Niagara Mohawk greater operating flexibility, allowing it to make fewer purchases on a "must take" basis. The new contracts will also give Niagara Mohawk greater flexibility to make purchases from IPPs when needed, at lower per kWh rates. The anticipated cumulative effect of these changes is that Niagara Mohawk, and ultimately ratepayers, will avoid future rate increases previously forecast to total 20% or more over the next few years.[2] Indeed, our analysis suggests these new arrangements will yield ratepayer benefits on a net present value basis of approximately $0.5 billion if the future payment streams are discounted at 10%, and more if a lower discount rate were assumed.[3] Additionally, the MRA permanently resolves many of

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[1] See, for example, Tr. 12,565-12,568; 12,779-12,795; 13,039-13,042; 13,066-13,073; 13,288-13,292.

[2] See, Tr. 13,040.

[3] The analysis values the transfer of Niagara Mohawk’s stock to the SIPPs based on the company’s valuation of the regulatory asset as presented in Appendix C to the Settlement. Our prudence determination is premised on that value.

the most difficult issues recently faced by Niagara Mohawk, short of a utility bankruptcy, which no party advocates.

Nor are we troubled by Niagara Mohawk using a portion of its common stock to pay the SIPPs. The proponents have convincingly demonstrated that the SIPPs cannot use their combined interests in the company to improperly influence its operations. Were they to attempt to do so, we would investigate any such circumstances and take proper steps to preclude improper manipulations of the competitive market.

The opponents of the MRA have also failed to establish that there is any serious alternative that would produce the same or greater benefits than the MRA. PULP, for example, suggests a continuation of the <u>status</u> <u>quo</u>, including the prospects for rate increases, is preferable to the MRA because the company might be able to avoid making payments to the SIPPs by moving closer towards bankruptcy. However, we consider PULP’s proposal inferior because of its greater risk of rate increases and for courting the uncertain and adverse effects of a Niagara Mohawk bankruptcy on the rates and service of this and other New York utilities. If efforts were made to put off the restructuring of the company’s finances, such action would create pressure for higher rates as more uneconomic purchase power obligations came due. It would also leave the steam hosts and other third parties far more vulnerable than they are under the MRA. In any event, we would continue to face the same issues that are before us now as they would not disappear. We could not put off these matters for long and there is no reason to believe any better solution than the MRA would be presented.

PULP suggests that the SIPPs would accept lower payments if the company were closer to insolvency. However, there is no evidence that the proximity of bankruptcy proceedings would lead to the results PULP envisions. The reorganization of the company in a bankruptcy proceeding would entail great uncertainty, and we are not convinced that the public interest is best served by pursuing any such course.

However, we are concerned about the effect of the MRA on steam hosts. We agree that it is an important public interest consideration bearing on whether we should approve and find prudent the MRA, because the potential effects on steam hosts could have a substantial impact on the economy in Niagara Mohawk's service territory. If satisfactory arrangements between the SIPPs and steam hosts had not been reached, the public interest would not have been served. Consequently, to the extent such arrangements had not been reached we would not have approved the MRA.

When we first considered these proceedings in early February 1998, we expressed a strong interest in obtaining prompt resolutions of the issues remaining between the SIPPs and the SHAG members in order to serve the public interest, protect the State's economy, and minimize the risk that the MRA might not close. Such results benefit ratepayers by making clear and certain the company's obligations during the rate plan. Consequently, our Staff assisted these parties and they managed to resolve their private disputes in all cases except one pertaining to Encogen Four Partners, Ltd. (Encogen) and Outokumpu American Brass, Inc. (American Brass). Thus, we are satisfied that acceptable steam host/SIPP arrangements have been reached in all cases except one.

We hereby find the MRA to be in the public interest and Niagara Mohawk's conduct to be prudent to the extent that satisfactory SIPP/steam host arrangements are reached. Consequently, if the one outstanding dispute cannot be resolved to the mutual satisfaction of the parties or the Commission, Niagara Mohawk should not proceed to consummate the MRA as concerns Encogen.[1]

With respect to the parties' exceptions urging us to place the MRA-related proceeds in an escrow account to ensure

[1] As Niagara Mohawk has agreed in the Settlement Agreement, this finding of prudence carries with it no entitlement to recovery by Niagara Mohawk of any return on the regulatory asset associated with the MRA, either during the term of the Settlement or thereafter.

their availability for steam hosts, the treatment described above adequately addresses these interests. And as to third party claims, we are satisfied that no liabilities will flow to Niagara Mohawk from the SIPPs' dealings.

Finally, there is no need for us to adopt any of the ratemaking presumptions that Norcen proposes. We accept Niagara Mohawk's and the SIPP's representations that their resolution of the matters pertaining to Norcen are not expected to result in any additional costs for ratepayers.[1]

PowerChoice Settlement Provisions

1. The General Public Interest Standard

Our Settlement Guidelines establish the following standards for assessing a proposed settlement and determining whether it should be approved:

> A desirable settlement should strive for a balance among (1) protection of the ratepayers, (2) fairness to investors, and (3) the long term viability of the utility; should be consistent with sound environmental, social, and economic policies of the Agency and the State; and should produce results that were within the range of reasonable results that would likely have arisen from a Commission decision in a litigated proceeding.
>
> In judging a settlement, the Commission shall give weight to the fact that a settlement reflects the agreement by normally adversarial parties.[2]

The PowerChoice Settlement proponents maintain, and the Judge generally found, that these criteria are satisfied. However, the opponents, principally PULP and the City of Oswego,

[1] The parties' exceptions concerning the CTC are discussed elsewhere in this opinion and order.

[2] Cases 90-M-0225 et al., Settlement Procedures, Opinion No. 92-2 (issued March 24, 1992) Appendix B, p.8.

claim that the Settlement is generally not in the public interest.

PULP argues that the changes to the rate plan recommended by the Judge demonstrate that the Settlement is not in the public interest. Moreover, PULP contends the Settlement is contrary to law and inconsistent with desirable public policy objectives even if all of the Judge's recommended changes were adopted. Only to the extent PULP's position is accepted in its entirety would this party conclude that the Settlement is in the public interest.

In general, PULP prefers that restructuring of the electric industry proceed pursuant to legislation. Also, rather than rely on the company's historical operating data and information provided in other proceedings, PULP would prefer that Niagara Mohawk provide more recent financial data and forecasts to set electric rates for 1998 and subsequent years.

The City of Oswego meanwhile contends a better analysis of the Settlement's impacts on local municipal units is needed before its reasonableness can be determined. Until the Settlement's effects on local business, employment, and municipal revenues are fully known and detailed, the City maintains, the requirements of the State Environmental Quality Review Act (SEQRA) cannot be completed and action on the Settlement should wait.

Niagara Mohawk responds to PULP's general arguments.[1] Comparing the Settlement with the vision and goals provided by our Competitive Opportunities decision,[2] the company observes that the Settlement reduces electric prices, aids the State's economy, creates a competitive market, and provides customers retail access. It also points out that the Settlement was negotiated in full compliance with our rules and guidelines and

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[1] The company, Staff, and MI also respond to the specific points supporting PULP's and Oswego's general opposition to the Settlement. Such points are addressed below.

[2] Cases 94-E-0952 et al., supra, Opinion No. 96-12.

describes it as properly balanced, protecting ratepayers and investors and helping ensure the company's long-term viability. All of this is demonstrated, according to the company, in the Settlement's specific provisions. And, as a wide range of interests--20 parties in all--have endorsed the Settlement, Niagara Mohawk says, this is strong proof that the public interest and the State's environmental, social, and economic policies are well served by the Settlement.

Niagara Mohawk also points to the Settlement's specific benefits to refute PULP. The company points, for example, to the rate reductions for all customer classes, lower energy charges approaching marginal costs, and cost-based customer charges. It highlights as well the Settlement's few cost deferrals and surcharges, and the elimination of the fuel adjustment clause.

Niagara Mohawk also contends the Settlement will achieve electric generation competition because the divestiture of its non-nuclear facilities will end its vertical integration and control over the generation market. In the next two years, the company goes on, energy suppliers will move into the industrial, commercial, and residential sectors and, by the end of 1999, all customers will be able to choose their own unbundled energy services.

Niagara Mohawk contends, as well, that the public interest is served by its corporate and financial structure changes ending the current arrangements with the SIPPs, allowing competitive markets to form, and segregating monopoly services from competitive ventures. The company says it expects to halt its financial deterioration, avoid bankruptcy, and recover uneconomic stranded costs without disturbing the operation of the competitive marketplace. And it will abide by the rules governing affiliate relationships and protecting competitive conduct.

In sum, according to the company, no other alternative provides as much benefit and serves the public interest as well as the Settlement. No other party, it says, has laid out an alternative approach that accomplishes as much as the Settlement.

Any continuation of the status quo, the company warns, will require rate increases to cover its rising costs. Finally, Niagara Mohawk points to the low earnings it will experience for the next three to five years as convincing proof that it is making every effort to serve the public interest through this Settlement.

Responding to the City of Oswego, Niagara Mohawk contends its electric rates in a competitive market should not be made to cover the cost of government services for localities that may lose tax revenues due to electric industry restructuring. The company also maintains that, on the whole, the Settlement will provide substantial economic and social benefits for the entire service territory by creating new business opportunities, generating jobs, and promoting economic development. In this context, Niagara Mohawk believes the local impacts of concern to Oswego do not provide good reason to forgo the sale of the company's generation facilities, which is essential to electric generation competition.

Many of PULP's and Oswego's public interest criticisms and concerns are discussed below in the context of our issue-specific findings and in the overall discussion and conclusion at the end of this opinion and order. These include, for example, those about the Settlement's proposed rate design, the adequacy and fairness of the proposed rate reductions, and compliance with SEQRA. At this point, however, we observe that legislative action, while possible, is not necessary for us to evaluate the Settlement's reasonableness or to implement its terms. Furthermore, legislation proposed to date does not provide the level of benefits created by the Settlement. Also, it is not necessary for us to have more recent financial results and forecasts in order to evaluate the Settlement's reasonableness. Staff conducted an examination of the company's financial condition over the Settlement term which provides us an ample basis for evaluating the Settlement's rate plan. In sum, we conclude that the Settlement, as modified and conditioned by this opinion and order, is in the public interest.

2. <u>The Settlement's Revenue Decreases</u>

a. <u>Exceptions</u>

CPB, PULP, and Retail Council consider the 3.2% revenue decreases proposed for the residential and small commercial customer classes to be too small and urge that the classes receive greater decreases.

CPB excepts to the Judge's recommendation against the ratemaking adjustments it proposed. At a minimum, CPB believes a 5.2% revenue decrease should apply to these classes and it can be achieved by reducing the company's bad debt expense, increasing the forecast of electric sales, and increasing the amortization period for the MRA-related regulatory asset. Several other parties also propose changes in the amortization of the MRA-related regulatory asset or in the term of the MRA debt financing.[1]

CPB says residential and commercial customers expect to see lower rates from the changes in the electric industry. CPB notes that these customers experienced substantial rate increases in recent years and it remains unpersuaded that a valid cost basis exists to raise customer charges now.[2] Lower prices for residential and small commercial customers, CPB says, would help to improve the economic condition of the service territory. It also believes that Niagara Mohawk's long-term financial viability would improve were lower electric prices implemented for all customers.

Retail Council and PULP complain about the disparity in the revenue decreases the Settlement would provide to large industrial and commercial customers, on the one hand, and to small commercial and residential customers, on the other. PULP believes there are sufficient programs currently available to

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[1] CPB specifically proposes that the amortization period for the MRA-related asset be extended by a year. Enron/Wepco consider a one to three year extension of the MRA debt financing proper while PULP does not quantify the extension it recommends.

[2] Customer charges are addressed below.

provide electric rate relief to large industrial customers and the Settlement's provisions are not needed.

Retail Council argues that the Settlement's industrial rate provisions are flawed and the record does not support disparate rate reductions for the various classes. According to it, economic development and business growth are more apt to come from the commercial and service sectors than from industry. Assuming there are insufficient funds to provide large decreases for the commercial and service sectors, Retail Council contends that all classes should receive comparable revenue reductions.

If any customers are to receive disparate rate reductions, PULP urges that low-income customers' rates be reduced by 25%. It says these customers are the neediest and least able to afford even modest bill increases.

b. Replies

In response to CPB's proposal for larger revenue decreases, Staff and the company say there are no funds available to finance such reductions. They also say any extension of the payment period for the MRA-related debt or the amortization period of the regulatory asset is undesirable. According to Staff, an extension would only shift these costs to future ratepayers and increase the total amount (and the interest payments) ratepayers would have to pay. Staff urges that the company's cash flow not be adversely affected, and the company agrees that its cash flow is needed to sustain its operations.

Niagara Mohawk says an extension of the MRA financing is contrary to strandable cost minimization and would unnecessarily extend the transition to competition. The company also contends an extension of the financing period would be unfair to it to the extent it agreed to give up some earnings for the next few years on the condition it can repay the MRA-related debt promptly and thus improve its financial condition. The company concludes by saying an extension of the MRA financing could endanger its ability to obtain this financing and thereby upset the Settlement.

Niagara Mohawk and Staff fail to see any merit in CPB’s proposed adjustments to bad debt expense and electric sales. They are unaware of any support for CPB’s position on bad debt, and they are concerned about increasing the company’s financial risk exposure. As to the projected sales, Staff observes that CPB did not provide its own sales forecast but compared the company’s projections with actual sales.

Niagara Mohawk also challenges CPB’s policy arguments for an additional two percent rate decrease for residential customers. It insists that the proposed industrial rate reductions are needed to produce competitive, electric rates, particularly if NYPA sales are ignored. The company also disputes the extent to which small businesses can reasonably be expected to drive the upstate economy and provide economic growth. Given that the upstate area remains vulnerable to loss of load and usage reductions from industrial and large commercial accounts, the company insists that the Settlement’s industrial rate reductions are of paramount importance.

MI also disputes CPB’s claim about the economic advantages of expanding large industry versus smaller businesses. Like Niagara Mohawk, MI contends that existing industrial rates remain unattractive, even taking into account low-cost hydropower that is available in limited quantities to specified customers. MI insists that small businesses, by themselves, cannot rehabilitate the upstate region or provide sufficient amounts of sustained economic growth. It says industrial growth is needed to cure the lag in the State’s economy dating back to 1989.

Staff questions the wisdom of PULP’s proposal to use the limited amount of rate reductions available to reduce only low-income customers’ rates. Staff contends it would be better to use the amount available to improve the local economy and thereby provide assistance to more customers. Staff also notes that the Settlement’s LICAP program, its provider of last resort provisions, the service quality standards, and the revenue reduction for the residential class, all enure to the benefit of low-income customers.

c. Discussion

We agree that the largest possible rate decrease overall, and the decreases for the residential and commercial classes, are important objectives. In recent cases involving other electric companies, we did not approve the parties' proposed settlements until we were satisfied that all reasonable means for obtaining the greatest amount of rate decreases were exhausted. In this case, we are satisfied that a full examination of the company's ability to provide rate decreases was made and it suggests decreases larger than anticipated in the Settlement cannot reasonably be granted at this time. However, to implement the Settlement in a manner that ensures that S.C. 1 (residential) and S.C. 2 (commercial) customers experience the tariff rate reductions projected from the Settlement relative to current rate levels, we shall require the company to reduce its energy charges using as the base year the most current twelve-month period or the 1995 base year levels as set forth in the agreement, whichever base year results in the lowest first year rate level.

With respect to CPB's proposals to further reduce the company's total revenue requirements based on a forecast of the company's bad debt expense and an increase in the company's projection of future electric sales, we find these projections are too speculative to support any further rate decreases at this time.

As to various parties' proposals to adjust the term of the MRA financing or extend the amortization of the MRA-related asset on the company's books, we find the Settlement reasonable and adopt it without any change. In reaching this decision, we have balanced the need for reductions in Niagara Mohawk's bundled electric rates with the company's need to be able to finance the MRA and we conclude that the Settlement, as proposed, is fairly balanced.

Concerning various parties' suggestions that more economic development can be obtained by shifting more of the overall revenue reduction from the industrial customers to the commercial and residential customer classes, we are not persuaded that any such substantial changes should be made. To begin, industrial load is more contestable to the extent industrial customers have a greater ability to shift production. Lower industrial rates help maintain total load and ensure contribution to total costs, benefiting all ratepayers. While it may be true that some economic growth could be stimulated by reducing electric rates for commercial and retail customers more than the amount the Settlement provides, and by reducing the cost of electricity for residential customers, we are not willing to sacrifice the improvements that the Settlement provides in the electric rates for large industrial customers, which provide substantial net employment opportunities in the upstate region. Moreover, if the amount available to reduce rates were used to provide all classes of customers the same percentage reductions, residential and small commercial customers would only see slightly greater reductions--4.3% instead of the Settlement's 3.2% reductions.[1] In sum, the larger reductions for the industrial class provide a significant opportunity for economic development as well as a contribution to total fixed costs to the benefit of all customers.

Finally, as to PULP's proposal for a 25% rate decrease for low-income customers, the Settlement's LICAP provisions provide substantial benefits designed to assist needy customers. Before we would entertain a proposal like PULP's, the expanded LICAP program should be fully implemented and its results evaluated. Finally, we conclude implementation of PULP's proposal, with the limited resources available, would provide less benefit to the economy overall in comparison with the Settlement.

3. <u>The Settlement's Duration</u>

Rather than commit to a five-year settlement term, the Judge recommended that we adopt the Settlement only for three

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[1] Tr. 13,048.

years. He expressed concern about the possibility of electric rate increases in 2001 and 2002, and recommended that the company file in the normal course for any rate increases in either of these years. Niagara Mohawk, Staff, NPLF, MI, and DED except.

Niagara Mohawk says the period need not be shortened because the Settlement does not assure it any rate relief for 2001 and 2002. The company points out that the Settlement requires it to fully justify any request it makes for these years and it caps the request at one percent for each year. If this limit is not adopted, Niagara Mohawk says ratepayers may otherwise be exposed to greater rate increases.

Niagara Mohawk also says it negotiated for a reasonably assured revenue stream in the Settlement’s fourth and fifth years. Without an assurance of adequate revenues in these years, the company says it would be exposed to higher financial risks than it can stand. It also expresses concern that other important Settlement provisions, including the collection of any generation sale auction incentive and recovery of certain deferred and nuclear generation costs, would be undermined if the Settlement’s term were shortened.

NPLF is also concerned about Niagara Mohawk’s financial risks absent the five-year Settlement. It says a shorter period would threaten the viability of the financing needed for the MRA.

Staff explains that the Settlement does not provide the company automatic rate increases in 2001 or 2002, and it emphasizes the amount Niagara Mohawk may seek in these years is limited. Staff also contends it is desirable to preserve advantageous Settlement features that apply in the fourth and fifth year, including the service quality incentives, the LICAP enrollment targets, and the affiliate transaction rules and competitive conduct standards.

MI points out that the Settlement places a "hard cap" on the amount by which rates can increase. While it would have preferred an absolute prohibition on rate increases, MI considers this aspect of the Settlement to be a reasonable compromise. MI also sees benefits in various Settlement provisions for 2001 and

2002, including those concerning optional five-year contracts for large industrial and commercial customers and those allowing certain customers to extend their current contracts for the full Settlement term.[1]

DED also supports a five-year Settlement for reasons similar to those already discussed. The provisions for 2001 and 2002 of primary interest to DED are those governing S.C. 11 contracts and the transition plan for the Economic Development Zone Rider.

In response to these exceptions, various parties continue to state concerns about customers being exposed to higher rates in 2001 and 2002. CPB, Oswego, and PULP, for example, generally favor a three-year rate plan.

CPB says that even if the rate increases for 2001 and 2002 are not automatic, they remain a real possibility due to the Settlement’s provisions. Similarly, PULP says electricity prices for residential customers could escalate significantly under the Settlement due to market changes in energy rates, higher customer charges, company cost increases, deferrals, and surcharges.

The parties’ exceptions are granted and the Settlement will be approved for five years. As many proponents point out, the Settlement offers substantial benefits in the fourth and fifth years. While the Judge is properly concerned about rate stability in the fourth and fifth years, we are satisfied such stability will be afforded by the Settlement. This is because, as some parties point out, any rate increase requests in those years is not automatic and they will be subject to full review. The company’s possible rate increases for non-commodity costs are capped at one percent and those increases, together with surcharges and deferral recoveries, are subject to an overall

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[1] While MI seeks to preserve a five-year rate option for industrial customers that would lock in their Niagara Mohawk electric commodity and CTC charges, Enron/Wepco is concerned that the company will use this option to provide large customers below market rates and preclude marketers from competing for their business.

inflation cap. Moreover, our current forecasts suggest the need for increases in these years will not be great and they can be ameliorated by anticipated savings related to recent interest rate reductions.[1] Finally, we are concerned that shortening the Settlement's term to three years could adversely affect the terms and maturity of the MRA-related debt issues, if not their feasibility overall. In sum, the risks of significant rate increases are sufficiently minimized that the Settlement should be approved for its full term.

4. Customer Charges

The Settlement proposes to increase the customer charges for residential and small commercial customers over the next three years as energy rates decline. For low-use customers, the higher customer charges would increase their electric bills by modest dollar amounts.

The Judge recommended against any customers experiencing bill increases due to of the Settlement, seeing such results as contrary to the objective of decreasing customers' electricity costs. The company and Staff except, while CPB, DOL, PULP and Oswego oppose the Settlement's proposed customer charge increases and the exceptions.

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[1] The financial forecasts supporting the Settlement (Appendix C to the agreement) are premised in part on an assumed average interest rate of 8.5% for the senior subordinated notes needed to finance the MRA. Since the time those forecasts were made, interest rates have declined. While the actual interest rates on the senior subordinated notes will not be known until the company issues the notes in the near future, we are requiring the company to defer the interest rate savings between the forecasted 8.5% and the actual rate for each of the five years of the settlement period. To the extent the Commission reduces rates beyond the levels in PowerChoice or the company applies for a rate increase in the fourth or fifth year, as allowed by the Settlement's terms, the deferred interest rate savings may be used to fund such reductions or offset any such increase that may be authorized. To the extent a deferred interest rate savings balance remains at the end of the fifth year, we will decide at that time how best to use the deferred savings.

The excepting parties insist there are good reasons for the Settlement's rate design provisions. The company, for example, contends it is proper to align energy rates with marginal energy costs. Staff agrees, noting the benefits of economically efficient pricing that customers should see in a competitive energy market.

The company and Staff points out the customer charge proposal also will help to eliminate the inherent unfairness of large-use customers paying for costs that small-use customers should bear. Niagara Mohawk also emphasizes that it prefers to recover its fixed costs through customer charges so any decline in sales will not affect the recovery of these costs. Given its generally poor financial condition, the resulting revenue stability will help minimize the company's risks.

Anticipating arguments that customer charges should not be increased for low-income, low-use residential customers who may not be able to afford modestly higher bills, Niagara Mohawk and Staff say LICAP provides them sufficient assistance. Staff also notes that many low-income customers who use large amounts of electricity stand to benefit substantially from the proposed changes.

Finally, highlighting the Settlement's substantial advantages for average and high-use residential customers, Staff points out that under the Settlement energy charges would decrease by about 17%. It notes that small commercial customers would also see significant energy rate savings. Staff believes that such reductions would improve economic development in the service territory, making it more attractive for small businesses to expand their operations.[1]

In response, CPB denies that low-use customer rates and costs are out of line. According to CPB, there is conflicting cost of service evidence on this point and, in a competitive

[1] Staff observes that the Retail Council supports the Settlement's rate design approach for small commercial customers.

environment, a new study may be needed to adequately address its differences with Staff. On the basis of the cost data CPB would credit, it says that non-heat (low-use) customers are not being subsidized by high-use, electric heating customers. CPB also believes that many low-income, low-use residential customers would experience unacceptable bill increases were the Settlement approved. And it remains concerned that higher minimum bills will lead to lower sales, greater uncollectibles, and customer disconnections.

Retail Council characterizes the Judge's rate design recommendations as regressive and counterproductive. It urges that the electric bill components be realigned, as the Settlement provides, to more accurately reflect marginal customer and energy costs. In this regard, it says the Settlement's rate design provisions are better than the Judge's status quo recommendations.

If we adopt any customer charge increases, PULP says we should also adopt its low-income rate proposal. DOL urges us not to allow any bill increases pursuant to the Settlement. Oswego responds to Staff by claiming that many residential customers may be worse off by the Settlement's effects on local employment, disposable income, and municipalities with utility generation facilities.

The Settlement's proponents have offered valid reasons why it would be beneficial to increase the customer charges applicable to the residential and small commercial customer classes. In previous rate proceedings, we have permitted these charges to increase for many of the reasons that the proponents have advanced here. But this portion of the Settlement has generated substantial public reaction. At a time when we are fostering a transition to competition and economic development, the Settlement's proposed customer charges would have the undesirable effect of increasing the bills for many of the company's residential and small commercial customers. This holds the potential for customer confusion and skepticism about the benefits of competition. In these circumstances, we shall exercise our discretion on this rate design matter and defer a final decision on this aspect of the Settlement until unbundled rates are filed for residential and small commercial customers. No changes from base period levels will be made in these charges for now.

5. Stranded Cost Recovery

a. Exceptions

The Judge generally recommends the use of a competitive transition charge (CTC) and a system of access charges and other fees to provide Niagara Mohawk the revenues it needs to pay the stranded costs associated with restructuring its above-market purchase power agreements and divestiture of its fossil generation facilities. However, he also recommends that some amount of stranded cost bypass be allowed for on-site generation and municipalities. Numerous exceptions to these recommendations have been filed by Niagara Mohawk, Staff, MI, PULP, CPB, Enron, Novus, and The Wing Group.

Niagara Mohawk contends that stranded cost bypass for self-generators and municipalities would be unfair to the remaining ratepayers and would constitute poor public policy. It maintains as well that uneconomic on-site generation should be discouraged and that all customers should pay stranded costs, other than the $2 billion the company will absorb during the term of the Settlement.

The company observes that the debt needed to finance the MRA can only be obtained if it has sufficient revenues. If any customers are allowed to bypass the CTC, access charges, and other fees, the company contends, the debt market may not be sufficiently assured of Niagara Mohawk's ability to repay the MRA-related debt. This could prevent the financing or result in higher debt costs. The company also doubts that any amount of stranded cost bypass can reasonably be controlled and limited.

Staff agrees that stranded cost bypass must be prevented in order to finance the MRA. Given the company's already poor financial condition, Staff is concerned about any loopholes for customers to bypass the CTC. Staff also supports access charges and other fees to recover embedded investments and discharge commitments before customers can be allowed to bypass the system. Staff distinguishes between economic and uneconomic on-site generation and notes that only uneconomic alternatives to the company's services are discouraged under the Settlement.

While MI supports the Settlement, it also believes that customers who have determined that on-site generation is a viable alternative should be allowed to obtain backup service from Niagara Mohawk without paying a CTC, access charges, or other fees. If the Judge's recommendations on this matter were to be adopted, it proposes that the parties devise suitable criteria for an on-site generation program. PULP opposes stranded cost bypass by any customers other than perhaps large industrial and commercial customers who have competitive alternatives.[1]

CPB opposes the CTC mechanism altogether, claiming it is anti-competitive. According to CPB, Niagara Mohawk should simply reduce its rates, achieve greater efficiencies, and absorb any stranded costs it cannot recover within these constraints. It fears the company will use the CTC to engage in predatory pricing and thereby harm the competitive market. It is also concerned about the CTC being used to reverse the modest rate decreases that residential and small commercial customers obtain from the Settlement.

Enron/Wepco oppose the CTC to the extent the level of this charge can vary over time, or "float" pursuant to the Settlement's terms. Like CPB, they say the charge is incompatible with the operation of a competitive market. They contend the floating CTC will be a significant barrier to entry

[1] With respect to these customers, PULP believes we should reconsider whether they should be able to avoid making CTC payments. In general, PULP considers it inequitable for stranded cost recovery to shift from some customers to others. It suggests that the existing exemption for customers with flexible negotiated rates cease when their contracts end. Only in those cases where the CTC would force a customer off the system would PULP support a waiver.

by competitors, precluding them from offering consumers a fixed-price product in competition with Niagara Mohawk's. These parties urge that a fixed CTC be established from the start. They claim customers can be assured of rate decreases without Niagara Mohawk's floating CTC and they point to other settlements that contain fixed CTCs and provide specified rate decreases for bundled service.

Novus, meanwhile, urges establishment of an on-site generation program that does not have the Settlement's "suppressing" effects. Specifically, it proposes that up to 8 MW of load currently served by Niagara Mohawk be allowed to convert to on-site generation without having to pay access charges. It says this amount of self-generation would have virtually no impact on the company but would allow some beneficial self-generation to develop in the service territory.

Finally, The Wing Group on behalf of various local communities interested in municipalization, points to substantial amounts of customer dissatisfaction with the rates Niagara Mohawk charges. It urges that all types of on-site generation be exempt from stranded cost recovery.

b. Replies

Niagara Mohawk insists that no substantial amount of CTC bypass can be tolerated. Responding to MI, the company says it is inappropriate for this party, as a signatory to the agreement, to support any Settlement modifications, even those proposed by the Judge.

In response to CPB, Niagara Mohawk reiterates that it will absorb $2 billion of stranded costs and that it should not be asked to absorb any more. Staff says CPB has misconceptions about the proposed CTC and explains that the CTC is included in the company's bundled rates, which will be unbundled and reduced during the Settlement term. According to Staff, the overall Settlement approach enhances competition and does not allow the company to use the CTC to abuse the marketplace.

The company opposes PULP's proposal for ratepayers and shareholders to share stranded costs as this too would increase the amount of stranded costs for it to absorb. Staff responds to PULP's criticism of the rates applicable to large industrial and commercial customers by stating that the CTC applies to these customers despite any energy discounts they may receive to remain on the electric system.

Responding to Enron/Wepco, Niagara Mohawk and Staff say a floating CTC guarantees that customers experience fixed and stable prices, which are important to several parties who executed the Settlement and to ratepayers generally during the transition period. The company also says it cannot afford to undercollect stranded costs, and a fixed CTC applicable to all customers would expose it to this risk. Finally, Niagara Mohawk says Enron/Wepco can only speculate that a floating CTC will hinder competition since no one knows how retail marketers will offer their services and products. If it interferes with competition, the company says we can modify the transition process accordingly.

Staff says that Enron/Wepco only present theoretical arguments against a floating CTC that do not pertain here. Staff insists it is not possible to implement a fixed CTC for all customers immediately without exposing the company to an unacceptable amount of financial risk. Further, Staff argues that Enron ignores the relationship between the wholesale market and retail rates. According to it, the mixture of fixed and floating CTCs provided in the Settlement carefully balances the hedged and unhedged power facing Niagara Mohawk in the wholesale market. Staff concludes that the Settlement's mix of fixed and floating CTC options represents the best retail package that could be fashioned given the existing and restructured IPP contracts.

Responding to The Wing Group, Niagara Mohawk says this party cannot credibly oppose the company's recovery of stranded costs given that it is affiliated to a firm that wants full recovery of its strandable costs.[1]

Various other parties oppose the company's and Staff's positions and urge that a limited amount of stranded cost bypass be allowed for on-site generation and municipal interests. These parties include Oswego, ENtrust, Coalition, Finch, and Novus. They doubt that a limited amount of CTC bypass for these interests would expose the company to any large risks, and they urge that competition from on-site generation not be precluded. They note that this alternative has been historically available to customers and they claim it should not be forestalled now.

c. Discussion

We previously determined that it is prudent for Niagara Mohawk to execute the MRA in order to reduce the financial burdens due to its uneconomic purchase power contracts with the IPPs. This significant transaction benefits all the company's customers by mitigating a long-standing problem and by making the transition to a competitive generation market possible. A non-avoidable CTC is both an important element to Niagara Mohawk's ability to issue over $3 billion of debt to fund the IPP buyout and a reasonable means to recover the costs of the MRA from all who benefit from it. Were any customers who currently use the company's generation resources able to bypass the CTC, aside from grandfathering self-generation investments already made, this would unfairly require the remaining customers on the system to pay costs which are fairly and properly attributable to departing or bypassing customers. To ensure that the CTC remains manageable, and does not become too large a burden for any group of customers, we will approve the Settlement's terms imposing certain fees in limited circumstances and structuring backup rates to recover stranded costs from on-site generators. We note that the Settlement states that the access fees related to on-

[1] This point refers to The Wing Group's affiliation to Western Resources, Inc.

site generators taking back-up service are designed to discourage uneconomic bypass. Consistent with this goal, we will require that the company's implementing tariff be designed to avoid any harsh results for customers who can demonstrate that, as of October 10, 1997, they had made a decision to proceed with and had made a substantial investment in on-site generation, effectively grandfathering them from the effects of the new rates.[1]

Any municipality that forms its own electric system will be required to pay for the generation facility costs that are attributable to the customers who transfer to municipal service. Consequently, we are granting the Settlement proponents' exceptions concerning stranded cost recovery.[2]

With respect to CPB's and Enron/Wepco's concerns about the CTC being anti-competitive, their arguments are unpersuasive. The application of this charge to all customers helps to ensure that all generation will compete on an equal footing, thus furthering development of a competitive market. Through our continuing oversight of the company, and by enforcing applicable Settlement provisions, we shall ensure that Niagara Mohawk does not engage in predatory pricing, or any other anti-competitive behavior during the transition to a competitive market or after a fully competitive market is established. Also, the CTC cannot be rigidly fixed for all customers initially without sacrificing the rate decreases that customers are expecting to see in the company's bundled rates pursuant to the Settlement.

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[1] Such customers shall be considered the same as existing S.C. 7 customers under Settlement §4.11.4.1. To implement this requirement, we are directing Niagara Mohawk to file a proposal within two weeks and interested parties will have ten days to comment on it.

[2] MI proposed that the parties meet to consider ways to implement the Judge's recommendations but no such meetings are necessary.

6. Enron/Wepco Rate Proposals

a. Energy Backout Rate

The Judge recommends that we reject Enron/Wepco's proposal to increase the amount to be backed out of Niagara Mohawk's bundled rates when customers obtain commodity services from other marketers. He considered the Settlement's provisions covering this matter adequate for the limited period before the independent system operator (ISO) begins to operate. He saw no need to expend any substantial resources to devise a better administrative method for setting this credit before a fully competitive market emerges. Enron/Wepco except.

These parties say the Settlement's backout rate is too low and anti-competitive because it does not reflect all the costs that they claim an equally efficient rival would bear. At a minimum, Enron/Wepco urge that the backout rate be adjusted for property taxes, and that the New York Power Pool's (NYPP's) 18% reserve requirement be substituted for the 14% figure the company estimates assumed. They say there is no reason not to use the NYPP's reserve requirements for 1998.

With respect to property taxes that were excluded from Niagara Mohawk's original estimates, Enron/Wepco attempt to demonstrate how this item could affect the calculation of generation costs. Enron/Wepco say that Niagara Mohawk forecasted $15/kW for capacity without accounting for property taxes. In 1997, the average real estate taxes the company paid on its steam stations was $22.50/kW. Thus, they maintain that an equally efficient competitor should receive a $37.50/kW capacity credit. In addition to this, Enron/Wepco point to other costs (administrative and general costs, depreciation, and allowances for funds used during construction) excluded from the Settlement's backout rate. In sum, they say the Settlement's backout rate provisions are so low as to preclude rivals from entering the market.

Enron/Wepco insist that a properly designed backout rate should cover up to three to five years worth of generation costs. But, they say, the Settlement's provisions neither cover the costs for this period nor do they otherwise reflect long-run incremental costs that are more properly used to set backout rates.

Finally, as a check on Niagara Mohawk's backout rate, Enron/Wepco compared it to the then available backout rate proposal in the NYSEG case. They say that the Judge's recommendations here are inconsistent with those made by a different Judge in the NYSEG case, which they prefer.

In response, Niagara Mohawk insists that the parties negotiated a proper backout rate, and the forecasts of market prices they relied upon are reliable. It says the long-run incremental cost (LRIC) method Enron/Wepco favor should not be used to administratively set the backout rate because past attempts to do this resulted in much too high prices for independent power production. According to Niagara Mohawk, competition currently exists in the generation market and it requires no stimulation before the ISO operates and the company divests its generation facilities.

Niagara Mohawk admits that the Settlement's backout rate is low but says it is not because the rate omits costs. It insists that the low backout rate reflects low market prices and a surplus of electricity that is driving energy prices down.

Addressing property taxes specifically, Niagara Mohawk says the Settlement's backout rate need not be adjusted for this cost because an equally efficient ESCO can purchase electric commodities in the open market and need not build or operate any generation facilities. Thus, an ESCO may never incur any property taxes and, the company says, it would be incorrect to adjust the backout rate for this.

With respect to NYPP reserve requirements, Niagara Mohawk insists a 14% requirement is reasonable for 1998. It says the current 18% standard is not pertinent because the New York State Reliability Council is expected to only require a 14% reserve when the ISO begins to operate later this year. In any event, Niagara Mohawk says this item has only a small effect on the backout rate.

Finally, the company says whatever the settlement in the NYSEG case is, it is not good precedent here and its circumstances are distinguishable in any event due to different financial circumstances between the two utility companies.

Staff criticizes Enron/Wepco's backout rate proposal for not reflecting the current market price of power and as posing a serious risk to the proper development of a competitive market. Like Niagara Mohawk, it observes that marketers purchase power in the open market from competing suppliers at market prices. Because rivals need only incur these market prices, Staff suggests no specific allowance is needed to cover Niagara Mohawk's property taxes or any of its other costs. Staff concludes that it is market prices, not Enron/Wepco's LRIC approach, that provide the proper backout rate.

The company and Staff are correct that the backout rate proposed here requires no change and this Settlement provision is approved. As the company notes, competition has begun and market-based transactions are occurring. The backout rate is properly pegged to a market price and the forecast of such prices negotiated by the proponents is both reasonable and the only such forecast presented here. Finally, we concur that the financial risks faced by Niagara Mohawk and NYSEG are different--among them being Niagara Mohawk's agreement to accept poor earnings--and, in any event, the NYSEG settlement is not precedental.

b. Niagara Mohawk Energy Sales to ESCOs

Enron/Wepco proposed that Niagara Mohawk be required to sell energy to them and other marketers at the same price backed out of the company's bundled rates. The company responded, saying it would sell to them but only if it had hedged power left from meeting its retail customers' needs. The Judge accepted Niagara Mohawk's response; however, Enron/Wepco continue to urge that the company be unconditionally required to provide them energy at the Settlement back-out rate. They point to the Dairylea pilot program and other utility companies' retail access programs where this approach was used. They say a similar stopgap measure is needed here so competition can begin without ESCOs incurring losses.

Niagara Mohawk responds that it may not have sufficient amounts of hedged power to provide electric commodities to ESCOs. And, it says, the company should not be required to bear the financial risk of providing unhedged commodities to marketers.

Requiring Niagara Mohawk to sell at its backout rate is reasonable only to the extent the company has a sufficiently hedged wholesale supply. And the company is willing to sell to ESCOs up to that point. Beyond it, however, the effect of any such requirement would be to expose the company to an unknown, potentially significant risk, at a time when it is already in a weak position. For this reason, Enron/Wepco's approach is not reasonable here and its exception on this point is denied.

c. Alternative Residential Rate Design

The Judge found that the record did not demonstrate sufficiently the merits of Enron/Wepco's alternative rate design for the residential class. He recommended that the proposal be examined further and addressed when the company presents its unbundled tariffs for this class. This approach is similar to the one we adopted in the Orange & Rockland rate restructuring case. Enron/Wepco and Niagara Mohawk except.

Enron/Wepco urge that their alternative rate design be adopted now since, they believe, they have shown its clear advantages, including additional revenues for Niagara Mohawk. They also say there would be no adverse customer impacts under their proposal as residential customers' total bills would remain the same as those produced by the current rate design. But, they say, customers would benefit from the new design's lower usage-sensitive energy prices.

On the other hand, Niagara Mohawk excepts to further consideration for the Enron/Wepco proposal when it files unbundled rates. It says the proposal has never been tried or fully analyzed. It also contends that the proposal presents unacceptable financial risks and it fears that no additional revenues would materialize. According to Niagara Mohawk, Enron/Wepco overestimate the price elasticity for the proposed price change. And, the company is not sure that customers would like the alternative design which it considers to be impractical and too costly to administer.

Enron/Wepco respond by denying their proposal creates any financial risk for the company and they stand by their price elasticity estimates. According to them, there is no good reason to delay a move to lower energy rates, given that customer charges can be adjusted to maintain overall bill levels. They say that a similar approach has worked well in the telecommunications industry and suggest this could also work in the electric industry.

Staff responds to Enron/Wepco, saying the Judge properly put off their alternative to when the unbundled tariffs are filed. It says this is the best way to deal with the controversy and uncertainty surrounding the proposal.

We shall adopt the Judge's recommendation to handle this matter just as we did in the Orange & Rockland case.[1] This rate design proposal is basically the same as the one we previously considered in the Orange and Rockland case, and it has not been adequately developed for us to consider adopting it. The proposal may therefore be raised again by Enron/Wepco and be explored further when unbundled rates for the residential and small commercial customers are filed.

7. Generation Auction Incentives

The Judge recommends we adopt CPB's proposal to limit the financial incentive payments to Niagara Mohawk when it divests its fossil and hydro-generation facilities to 10% of any gain. However, contrary to the CPB proposal that the ratepayer share of the sale proceeds be used to fund rate reductions, the

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[1] Case 96-E-0900, Orange and Rockland Utilities, Inc. - Electric Rates/Restructuring, Opinion No. 97-20 (issued December 31, 1997), mimeo pp. 16-18.

Judge recommends instead that it be used to pay off stranded costs. Niagara Mohawk, Staff, IPPNY, CPB, PULP, and Oswego except.

The company and Staff support the Settlement's auction incentive provisions. Concerning the proposed incentive payments for any sales made below book cost, they insist that the plants' remaining original costs are irrelevant because the auction seeks bids based on future expectations of electric generation costs and revenues, not the plants' historic value. The company also contends that ratepayers are fully responsible for its stranded costs; therefore, they benefit from any proceeds obtained at auction even if the plants are sold at a loss.

In further support of the Settlement's incentive provisions, the company and Staff claim they properly align ratepayer and shareholder interests and the graduated payment feature reflects the fact that higher bids and sales prices are harder to obtain. Nonetheless, if higher than expected prices are achieved, they say, the Settlement precludes the company from enjoying a windfall. These proponents claim the Judge's proposal lacks these attributes.

Niagara Mohawk, Staff, and IPPNY also maintain that incentives greater than the Judge proposes are needed to maximize the sale price of the generation facilities. IPPNY notes that the Settlement's auction incentive provisions are designed to discourage the company from rejecting bids and to promote an auction over a spin-off of the generation facilities to another entity.

These three parties assert that the auction incentive provisions are integral to the Settlement and shareholders expect higher equity earnings, if the auction proves to be successful, in exchange for otherwise accepting lower earnings. Niagara Mohawk also argues it is entitled to the full incentive contained in the Settlement, given its willingness to divest its non-nuclear generation facilities. Similarly, Staff points to the benefits of the company's withdrawal from the State's electric generation market and argues such action warrants a strong incentive.

CPB excepts to the recommendation that the auction proceeds be used to pay stranded costs. It urges that they be used instead to provide residential and small commercial customers greater rate decreases. Only after larger rate reductions are achieved for these customers would CPB use any auction proceeds to reduce stranded costs. CPB argues that public acceptance of the Settlement can only be gained with larger rate decreases and the auction proceeds provide a painless way to obtain them. It suggests that a similar issue in the Orange & Rockland rate restructuring case was resolved as it proposes.

PULP is opposed to divestiture by Niagara Mohawk until comprehensive legislation is passed. Alternatively, it urges that additional hearings or proceedings be held concerning the company's generation divestiture plan filed on December 1, 1997.

Oswego urges that comments on the company's December 1997 divestiture plan not be considered until after we act on the Settlement (a decision already made). However, until the economic and other effects of divestiture of generation facilities are fully evaluated and the impacts on local communities are known, Oswego says we should not find the Settlement to be in the public interest. According to Oswego, Niagara Mohawk has not provided sufficient concessions to warrant as large a financial incentive as the Settlement provides.

In response to PULP and Oswego, Niagara Mohawk sees no need for further hearings or legislative action. The company also suggests we fully addressed the merits of utility generation divestiture in our Competitive Opportunities decision and argues our prior conclusions are not undermined by the record here.

In response to Staff and the company, CPB insists that Niagara Mohawk should not receive an incentive for sales made below book value because ratepayers will have to pay for more stranded costs as a result. It argues the company should only be rewarded for obtaining a gain. As to the amount of an incentive the company should be allowed to earn, CPB says a 10% incentive is ample and anything more, in its view, would be excessive.

We find with respect to Niagara Mohawk's non-nuclear generation units, except for the Oswego facilities,[1] 15% of any gain the company achieves above net book value is a sufficient and proper incentive for it to obtain the best possible prices for these facilities at auction. As to Oswego's and PULP's procedural proposals, having decided to approve the Settlement with the modifications presented herein, we will next consider Niagara Mohawk's divestiture plan and the parties' comments concerning it. Given the ample record in these proceedings, there is no need for any additional hearings concerning the divestiture of the company's non-nuclear generation facilities.

8. Nuclear Generation Facilities

The Settlement provides that:

> [t]he nuclear assets held by Niagara Mohawk will remain part of [the transmission and distribution company] as a separate business unit until they are either transferred or divested.
>
> Niagara Mohawk will continue to pursue statewide solutions for its nuclear assets through discussions in formation of NYNOC and in any generic proceedings established by the Commission. Statewide solutions for nuclear plants will be explored before other potential solutions.
>
> . . .
>
> Absent a statewide solution, Niagara Mohawk commits to file a detailed plan, analyzing the proposed solutions for its nuclear assets, within 24 months of this Settlement Agreement. The plan will consider the feasibility of auction, transfer, and/or divestiture of Niagara Mohawk's nuclear assets. The detailed plan will undergo an

[1] We are approving the Settlement's incentive provisions for the auction of the Oswego Steam Station.

appropriate level of Commission review and approval to be concluded on an expedited basis.[1]

The Judge recommends approval of this Settlement provision, and NYSEG excepts. Rather than pursue a statewide solution or consider a Niagara Mohawk plan thereafter, NYSEG urges that the company be required to auction its nuclear assets now to resolve this issue expeditiously. It considers the Settlement too open ended and insists that a continuation of the status quo is intolerable and contrary to our goal of obtaining complete divestiture of all utility generation facilities. NYSEG takes no solace in the fact that nuclear generation matters are currently being considered in Case 94-E-0952.

Niagara Mohawk, Central Hudson/LILCO/RG&E, and Staff respond to NYSEG. The company says the Settlement approach is best because it neither delays the resolution of nuclear matters nor forestalls their proper consideration. It considers Case 94-E-0952 a better place to determine whether a nuclear auction should be pursued.

The other utility companies agree with Niagara Mohawk on the latter point and dispute NYSEG's assertion that an auction would provide certainty. They say there are regulatory approval problems inherent with an auction that may not be easily resolved.

Staff responds that the Settlement is neither adverse to nor inconsistent with NYSEG's preference for a nuclear auction because that result is not precluded. Staff insists that all worthy alternatives should be examined in Case 94-E-0952 before a decision is reached.

It is clear that the disposition of Nine Mile 2 directly involves the other utilities and any resolution would affect each of them. Rather than seek to resolve such matters here, the Settlement properly acknowledges the currently ongoing

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[1] Settlement §3.3.1.

statewide efforts and provides a reasonable period for Niagara Mohawk to submit its own proposal if the ongoing efforts fail. Moreover, we are considering divestiture of nuclear generation in Case 94-E-0952 and we have no plans to delay that proceeding. NYSEG's exception is therefore denied.

9. Niagara Mohawk's Identity and Royalty Payments

a. Use of the Corporate Name

Enron/Wepco proposed that Niagara Mohawk's affiliates be precluded from using the corporate name and logo in their marketing, particularly in the company's service territory. The Judge did not recommend their proposal and these parties except.

Enron/Wepco say the Niagara Mohawk affiliates will obtain a competitive advantage from using the company name but it does not provide them with any greater efficiency, which should be the primary determinant of whether a competitor succeeds. In contrast, they say, new market entrants will have to expend substantial sums to establish their own brand names. Alternatively, if the affiliates are allowed to use the utility name, Enron/Wepco urge that a royalty be imposed to capture the name's value. These parties say one or the other approach is needed to ensure that affiliates do not dominate the energy services market simply by virtue of their association with the incumbent utility.

Niagara Mohawk replies that its affiliates should be allowed to use its name. It says the name's value is uncertain but, in any event, its use should not be restricted nor should its affiliates be handicapped from the start. Other potential competitors, according to Niagara Mohawk, are large, well-funded, and fast becoming known to the consuming public. In this context, the company says there is no reason to place it at a competitive disadvantage.

We are not persuaded that a utility must be denied the use of its name and identity in its own service territory for competitors to be able to enter the market and compete successfully. Whether or not a utility affiliate is known to operate in the same market, competitors will, in any event, have to establish themselves and advertise. The exception is denied.

b. Royalty Payments

The Settlement provides that the rate plan:

> . . .shall be in lieu of any and all "royalty" payments that could or might be asserted to be payable by any affiliate or imputed to [Niagara Mohawk] or credited to [Niagara Mohawk] customers at any time, including after the expiration of this Settlement.[1]

The Judge recommends that royalty payments not be required during the term of the Settlement because the company's low earnings during this period could reasonably be considered to subsume a royalty. However, he recommends that we not accept this provision to the extent it would exempt the company and its affiliates from making royalty payments indefinitely, even beyond the term of the agreement. The company, Staff, and PULP except.

Niagara Mohawk says its low earnings under the Settlement and the $2 billion of stranded costs it is absorbing warrants permanent elimination of any royalty. As elsewhere, it insists that this provision is integral to the deal it struck. And it insists that the company's affiliates should not be hindered in their future competitive efforts by having to make any such payments.

The company believes that changes in the electric industry since the Commission first adopted its royalty policy support the Settlement's approach. It also points to our approval of a recent settlement involving Consolidated Edison Company of New York, Inc. as precedent supporting approval of this Settlement provision.

[1] Settlement §9.3.1.

For its part, Staff points to the Settlement’s affiliate transaction rules and its code of competitive conduct as reasons for eliminating royalty payments. It observes that, once the royalty requirement is dropped and affiliates begin to use the corporate name, it will become more difficult to apply the royalty concept fairly thereafter. Staff therefore argues against any reexamination of this matter at the Settlement’s end.

If Niagara Mohawk forms a holding company, PULP contends unregulated affiliates that use the corporate name and advertise their affiliation should be required to pay royalties to compensate the regulated utility company for the competitive value of this use. The company’s current financial condition, according to PULP, is no excuse for not requiring a royalty, especially given that a royalty would be a beneficial source of new revenues. Further, PULP contends Niagara Mohawk should receive substantial royalty payments given that the Settlement allows the company to pay up to $625 million of dividends to a new parent company.

In response to PULP, Niagara Mohawk argues that the Settlement’s corporate structure and dividend payment provisions are reasonable and supported by the record. The company maintains that the rate plan subsumes an unquantified but certain sum to compensate for the use of the corporate name and argues that royalty requirements are fast becoming obsolete in any event. Staff replies that PULP is also incorrect to suggest there will be any additional money available to pay a royalty.

For its part, CPB urges us not to rule out the possibility of an explicit royalty payment at a later date. It says it is best to reserve the right to examine this issue after the company’s current circumstances are resolved and when it can be considered as a matter of long-term policy.

It is permissible for the proponents of rate settlements to address the issue of royalty charges in any rate plan they submit, as the parties have done here. And, if a rate plan is otherwise acceptable, we would not necessarily reject it if it contained no explicit amount earmarked as such. Instead, we examine a proposed settlement as a whole to determine whether it is reasonable. In this instance, we are satisfied with the rate plan being proposed for the next five years and we see no need to impute or ascribe any additional royalty amounts to the company, either as a matter of general policy or on the basis of arguments presented here. We therefore reject PULP's and Enron/Wepco's exceptions.

As to whether the company should be subject to any royalty payments subsequent to the rate plan's five-year term, we are adopting the Settlement subject to the condition we will not preclude parties from raising and having the issue considered again, with any royalty to be effective, if ever, after this Settlement ends.

10. Generic and Case-Specific Determinations

The Judge accepted the Settlement's dividing line between those issues which would be fully resolved here on a company-specific basis and those which would be resolved in generic cases. Enron/Wepco except to this recommendation to the extent the Settlement's affiliate transaction rules and competitive code of conduct would remain in place for the Settlement's term even if intervening generic decisions are different. Similarly, they except to the extent the Settlement would establish specific creditworthiness requirements for ESCOs that operate in Niagara Mohawk's service territory.

Enron/Wepco contend the negotiations that produced the Settlement should not dictate our policies to foster competition. They complain the Settlement's provisions restrict our flexibility to address competitive market developments, and claim the Settlement's rules are too inflexible, impairing competition and barring us from taking remedial action when necessary. These parties ask that we reserve the right to apply different rules and codes produced on a generic basis.

As to the Settlement's creditworthiness requirements for ESCOs, Enron/Wepco again claim the provisions will impede competition.[1] They say the company does not require as much security as it seeks to obtain from ESCOs. Accordingly, they contend these requirements amount to an unfair barrier to entry that should be rejected. The details of implementing retail access, they say, should be the subject of further proceedings rather than be codified by the Settlement.

Niagara Mohawk responds that the Settlement is intended to protect the company, during its term, from adverse financial impacts that could occur were changes made to our regulatory approach to affiliate relations. Staff observes that the Settlement's standards for competitive conduct do not provide the company any license to act improperly. Staff adds that the Settlement contains procedures for resolving competitor complaints and violations of its standards. Thus, Staff sees no reason why such matters should be referred to a generic proceeding.

As to the Settlement's ESCO creditworthiness requirements, the company says they are needed to protect against the risk of an ESCO's default, in which case Niagara Mohawk would be obligated to pay for power needed to serve affected customers until they switch to another provider. Staff responds that the Settlement's creditworthiness requirement is commensurate with the company's financial exposure inasmuch as defaulting ESCOs may owe the company for three months or more of service.

We find no need or reason to disturb the Judge's recommendations on these matters. We find that the Settlement's affiliate relationship rules and its code of competitive conduct are reasonable in the context of the overall agreement. Also, the Settlement's ESCO creditworthiness provisions are justified given the extent of the company's financial exposure. Accordingly, Enron/Wepco's exceptions are denied.

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[1] Enron/Wepco specifically object to the requirement that ESCOs provide security equal to their customers' two highest monthly usage levels multiplied by the company's highest monthly on-peak energy buyback rate.

As a final matter in this category, we note that the Settlement requires all customers in S.C. 3 and above to have an hourly interval meter whether or not they select an alternative energy supplier.[1] Under the Settlement, such customers would bear the incremental cost of a new meter unless we decided otherwise as a matter of general policy. S.C. 3A and 4 customers already have such meters but S.C. 3 customers may have to obtain them by May 1999.

We plan to consider, as a generic matter, whether customers should be required to bear the cost of new meters and we may adopt new metering standards for use in 1999. Therefore, Niagara Mohawk customers will not be required to purchase any replacement meters until the standards for 1999 are known.

11. State Environmental Quality Review Act Findings

On May 3, 1996, in conformance with the State Environmental Quality Review Act (SEQRA), we issued a Final Generic Environmental Impact Statement (FGEIS) which evaluated the action adopted in Case 94-E-0952, the generic Competitive Opportunities Proceeding. The individual electric utility companies were subsequently required to provide individual environmental assessments of their restructuring proposals. Niagara Mohawk provided its Environmental Assessment Form (EAF) and SEQRA recommendation on August 26, 1997. The company supplemented its EAF on November 4, 1997 and addressed the environmental implications of Settlement provisions that differed from the company's original proposal. Parties to these proceedings were requested to provide their comments on the supplemented EAF either by December 3, 1997 or with their trial

[1] Settlement §8.3.2.

briefs. Comments on this matter were received from various parties, including SHAG, MI, and Oswego.[1]

The information provided by Niagara Mohawk in its EAF, the parties' comments and responses, and other information were evaluated in order to determine whether the potential impacts resulting from adopting the Settlement's terms would be within the bounds and thresholds of the FGEIS adopted in 1996. Arguably, all of the potential impacts need not be considered given that some result from Type II exempt rate actions. Nonetheless, the analysis examined all areas in which impacts would reasonably be expected.

No impacts were found to be associated with the Settlement's treatment of the competitive transition charge (CTC).

Localized community economic impacts may occur (e.g., due to reduced tax receipts or employment at existing generating stations), but these would be balanced by positive effects in other localities.

Another potential concern is the possible increase in air pollution that could accompany increased demand for electric energy. It is possible that increases in energy demand will result from the Settlement's decrease in rates and in DSM expenditures: 0.50% average annual increased demand over the 1997-2012 period from the former and 0.13% increased demand from the latter. Each of these incremental growth rates is an upper bound. For example, it is not clear that all of the rate reductions from the Settlement should be attributed to restructuring; and the lower DSM expenditures do not consider ESCO DSM spending. Staff's view is that the actual growth rates

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[1] The final Environmental Assessment Form is Appendix C. The substantive comments received are considered here and in the EAF. As a procedural matter, Oswego excepts, contending we have failed to comply with the requirements of SEQRA to date. However, as detailed above, the process we have used complies fully with the applicable requirements. Moreover, the attached EAF addresses the substantive and environmental concerns that were raised by Oswego and other parties.

will be substantially less than the corresponding rates in the FGEIS (1% annual incremental growth from the "high sales" scenario, and 0.29% from the "no incremental utility DSM" scenario).

Because of the inherent uncertainty in forecasting future impacts, as a matter of discretion, monitoring of the restructuring and environmental impacts is being implemented and a system benefits charge is being established.

Based on these analyses, the potential environmental impacts of the Settlement are found to be within the range of thresholds and conditions set forth in the FGEIS. Therefore, no further SEQRA action is necessary. We note, however, that we will act in the future on the company's plan for auctioning its generation assets. Additional SEQRA analysis may be required at that time.

12. Other Matters

a. Cost Allocation Manual Review Procedures

The Settlement requires Niagara Mohawk to file a cost allocation manual with the Director of the Office of Accounting and Finance that will become effective 30 days after it is submitted if the Director accepts the company's filing.[1] The Judge recommended that the National Electrical Contractors Association (NECA) and other interested parties be allowed to examine the company's proposed manual and submit comments to the Director for his consideration.

On exceptions, Niagara Mohawk says acceptance of the Judge's recommendation would change the Settlement which did not contemplate an opportunity for anyone to submit comments concerning the manual. The company also says it did not expect the Director to approve the manual but merely to accept it for filing purposes. While Niagara Mohawk does not object to NECA

[1] Settlement §9.2.1.3.

inspecting its proposed manual, it is opposed to NECA, or any other party, slowing the process the Settlement envisions.

We adopt the Judge's recommendation allowing anyone interested in the company's cost allocation manual to submit timely comments to the Director of the Office of Accounting and Finance before he accepts the proposed manual. If need be, the Director can postpone the effective date of the manual, or any subsequently proposed amendments and supplements, beyond the 30-day period stated in the Settlement if additional time is required to consider any comments he receives. If the company submits a proposed manual which the Director considers to be unacceptable, our understanding of the Settlement is that he has the authority to refuse to accept the company's filing. In any event, by allowing parties to file comments we do not intend that there be any delay in this process.

b. Disclosure of Social Security Numbers

DOL proposed that Niagara Mohawk be required to inform customers in all instances that provision of social security numbers to an ESCO is not necessary to obtain electric service. The Judge recommended against the proposal.

On exceptions, DOL urges that customers be notified of their right to decline to provide their social security information and that such action will not adversely affect service. DOL says customers should know that they can keep this information private to avoid its misuse.

Niagara Mohawk responds that it complies with laws that apply to social security numbers and it knows of no customer who has been injured by having been asked to provide the company this form of identification. It urges us to refrain from imposing new disclosure requirements that neither Congress nor the Legislature has seen fit to impose.

DOL also presented its concerns about the use of social security numbers in a recent rulemaking proceeding, Case 96-M-0706, in which we changed some of our consumer protection rules to streamline their operation, remove burdens on utility companies, and maintain adequate customer protections. In that case, we said:

> In its comments on the Revised Rulemaking, [DOL] again argues for a prohibition on social security numbers, or that potential customers should at least be informed that disclosure is voluntary and no harmful consequences will come to those who refuse to supply it. [DOL] does not offer any new reasons why the use of social security numbers should be prohibited; we will not revise the proposal on this matter. However, we do agree that potential customers should not be coerced into revealing social security numbers or left with the impression that refusal to reveal a social security number will result in harmful consequences. If customers are asked for a social security number, they should also be made aware that they are not required to give it, and that other identification will be accepted.[1]

The rule we adopted applies to this situation and all ESCOs; this statement addresses adequately the concerns DOL raised in these cases.

c. <u>Future Tax Refunds</u>

The Settlement seeks to streamline the handling of future tax refunds and deficiency assessments. The company would keep any refunds of up to $500,000 each and it would not be able to recover any liabilities up to this amount. Refunds and liabilities exceeding this amount would be deferred for disposition after the Settlement term.[2] According to the Settlement, the company would not file a formal notice of the tax refunds it receives nor would additional hearings be convened.[3]

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[1] Case 96-M-0706, <u>Consumer Protection Rule Amendments</u>, Memorandum and Resolution Adopting Amendments To 16 NYCRR Part 11 (issued February 17, 1998), p. 6.

[2] Settlement §11.1.2.

[3] <u>Id.</u>

In response to DOL's objection to this proposed procedure, the Judge recommended that the company continue to provide formal notice of its refunds and that a decision on whether to hold a hearing be made after such notice is provided. The Judge supported the Settlement's substantive treatment of future refunds and recommended that the company have the benefit of a rebuttable presumption that the Settlement results should apply.

On exceptions, Niagara Mohawk urges that the Settlement's approach to future refunds be adopted in its entirety. It insists that notice and hearings should not be needed for any refunds under $500,000.

In response, CPB urges us to preserve the option to hold a hearing in any instance that may warrant one. It agrees with Niagara Mohawk that hearings are not needed for trivial matters but, it says, that should be decided after notice is provided.

The notice requirements implementing PSL §113(2), set forth at 16 NYCRR §89.3, will be followed since they are not burdensome and we reserve the right to schedule a hearing upon the filing of such notice. However, we will establish a rebuttable presumption that all refunds received during the Settlement's term should be accounted for and applied as the Settlement provides. The Settlement provision is adopted subject to this change or condition.

d. Residential Hydroelectric Allotments

PULP objects to the Settlement's method for providing residential customers the benefit of certain low-cost hydroelectric power to which they are entitled. Rather than include this cost in the company's base rates, it would prefer to see hydropower separately stated on customers' bills without any markups. PULP says its approach is consistent with the move to unbundled charges, and it asserts its proposal should be adopted to ensure residential customers receive their full allocation of this low-cost electricity. Essentially, PULP is concerned customers may end up paying more for NYPA hydropower based on its market value.

The Judge recommended against this proposal because PULP did not show the Settlement would deprive residential customers of any of the benefits of their allocation of this power. PULP excepts, requesting that further proceedings be established at which Niagara Mohawk would prove the Settlement approach is the best means to provide hydropower benefits to residential customers.

Niagara Mohawk responds, pointing to testimony and other information establishing that residential customers will continue to receive all their hydropower benefits of approximately $45 million per year. Similarly, Staff affirms that unbundling electricity charges will have no impact on the customers' hydropower benefits and they will receive them no matter who is their chosen supplier. Staff notes also that NYPA, the authority charged with the responsibility of administering this power, supports the Settlement, among other reasons, because it ensures residential customers will continue to receive their full hydropower benefits.

Having considered PULP's points, we find that the Judge's recommendation properly resolves this matter. For the reasons offered by the Judge and the parties, PULP's exception is denied.

e. <u>PULP's Legal Arguments</u>

PULP excepts to the Settlement's approach for implementing competition in the electric industry and claims we lack authority to implement its provisions. First, it objects to an expansion of LICAP through 2002 because it generally does not include customers who receive public assistance. It claims that these customers should have the same opportunity to obtain favorable credit terms as non-recipients of public assistance and that LICAP violates the Equal Credit Opportunity Act (ECOA).[1]

[1] Specifically, 15 U.S.C. §1691(a)(2).

PULP insists that LICAP coverage of public assistance customers in the Child Assistance Program and the company’s willingness to test a pilot program for public assistance customers is not enough to satisfy the ECOA’s requirements.

Next, PULP claims the Settlement’s utility generation divestiture provisions would adversely affect the company’s ability to provide adequate service, as the company would no longer own and operate facilities needed to supply customers. At most, it believes that the Settlement’s proponents should have developed a proposal for comprehensive restructuring legislation rather than pursue generation divestiture through the Settlement.

Similarly, PULP objects to the Settlement provisions contemplating that ESCOs will sell electricity to the public. PULP insists that they cannot do so without satisfying statutory requirements applicable to electric utility companies. It says all market entrants should be required to provide the customer service and rate protections that public utilities are currently required to provide.

PULP also says the Settlement’s retail access plan is impermissible. Rather than allow the market to set electricity prices, PULP says administrative action must set just and reasonable prices for adequate service. PULP doubts that adequate competition will emerge to protect customers’ interests and it would prefer to see legislation establish competition in the electric industry. At a minimum, PULP urges us to condition the Settlement’s approval on the formation of an adequate competitive electric market in which no sellers can exercise market power. It objects to any relaxation of the service rules applicable to electric utilities for the benefit of the ESCOs.

Finally, PULP claims that, before we can establish any competitive opportunities policies, legislation should address the impacts of such changes on municipalities. As tax bases and local employment may suffer, PULP urges legislation be passed to address these matters.

In response, Niagara Mohawk and Staff insist that PULP is viewing the applicable legal requirements too restrictively and it is ignoring recent case law that supports the approach being used here. Staff also says PULP's legal arguments have already been presented, considered, and rejected.

With the exception of PULP's challenge to Niagara Mohawk's LICAP, this party has not presented any new legal arguments or theories that we have not already considered and rejected. They deserve no further consideration here and PULP's exceptions on them are denied for reasons explained elsewhere.[1]

As to LICAP, we are satisfied it does not violate the Equal Credit Opportunity Act. To begin, LICAP is not primarily intended to be a mechanism for providing credit to customers. Instead, it is a means for the company to control its uncollectibles and the amount of bad debt it incurs, benefiting all customers. Moreover, even if the ECOA applies, a creditor does not violate the law if a refusal to extend credit to a public assistance recipient is made pursuant to a program otherwise expressly authorized for a class of disadvantaged persons.[2] The LICAP proposal targets such a group, while taking into account the limited resources available for such a program in the circumstances presented. Finally, to the company's credit, it has agreed to substantially enlarge the scope of this program and make it applicable to more public assistance recipients. The company has also not ruled out the possibility that a suitable program to decrease arrears and uncollectibles might be developed for other public assistance customers. For all of these reasons, PULP's exceptions to the LICAP recommendations are denied.

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[1] See, for example, Case 94-E-0952, Competitive Opportunities, Opinion and Order Deciding Petitions for Clarification and Rehearing, Opinion No. 97-17 (issued November 18, 1997), mimeo pp. 29-35.

[2] 15 U.S.C. §1691(c)(1).

f. Standard Performance Contracts

With respect to system benefits charges (SBC), the Settlement says:

> [n]othing in this agreement will prohibit the Statewide administrator from allocating a significant portion of the total SBC revenues derived from Niagara Mohawk's customers to be disbursed within Niagara Mohawk's service territory through competitive standard performance contracts which provide for stipulated pricing for energy efficiency, consistent with any generic guidelines for SBC expenditures separately developed from this proceeding by the PSC.[1]

In its initial trial brief in these cases, NAESCO supported the Settlement's SBC provisions. Pointing to this provision, NAESCO said it supported the competitive distribution of energy efficiency funds through a standard performance contract mechanism with stipulated pricing. The Judge recited NAESCO's position in the recommended decision and MI, another Settlement supporter, excepts.

MI disputes NAESCO's characterization of the provision and says its clear language does not provide support for standard performance contracts. According to MI, this provision merely preserves the matter for a future generic proceeding and the Settlement would permit such contracts to be used in the Niagara Mohawk service territory if they are allowed as a matter of general policy. NAESCO does not respond to MI's description of this section.

MI is correct that the Settlement only establishes that the use of standard performance contracts is not barred by the agreement. Whether such contracts should be employed remains open for further consideration.

[1] Settlement §7.1.2.

g. Local Taxes and the CTC

The City of Oswego claimed that the Settlement would adversely affect its tax structure and eliminate a significant source of its tax revenues. It proposed that lost tax revenues, due to reductions in the value of utility generation assets, be included in the CTC as part of the transition to a competitive, electric generation market. The Judge recommended that this proposal be rejected and Oswego excepts.

Oswego says the Commission has the authority, and the public interest would be well served, to require that local taxing jurisdictions recover lost tax revenue through the CTC. However, Niagara Mohawk urges that local municipalities not be allowed to recover the cost of governmental and local services in utility charges applicable to all customers. The company says it is unfair to burden customers elsewhere with the costs for local services, which do not benefit and cannot be controlled by them.

Staff responds that Oswego's tax problems are not due to the Settlement. It observes that the Settlement neither changes the City's tax base nor alters Oswego's assessment of the company's property. If anything, Staff says, the Settlement serves Oswego's interests by providing for three-year energy purchase contracts for the generation units that are sold. The allowance made for such contracts presumes that property taxes will continue to apply.

The City of Oswego's proposal to include "stranded taxes" in the CTC is denied. We agree with the company that there are inequities in including any such amounts in the CTC that applies to all customers. Staff is also correct that the Settlement provides the City, and other municipalities that host utility generation facilities, a transition period with the energy purchase contracts Niagara Mohawk expects to execute with the firms that buy its plants.[1]

h. Additional Public Comments

The recommended decision considered the comments made by customers and their representatives at the public statement hearings and in correspondence. Written comments from persons interested in the Settlement continued to be submitted after the recommended decision was issued. For example, substantial comments about numerous Settlement provisions have been received from The Wing Group, a City of Buffalo Council Member, and a Washington, D.C. public utility consultant. Comments have also been received from the Sierra Club in the Niagara region, and the Statewide Senior Action Council, which reinforce the statements made by their respective members at the public statement hearings. Various firms interested in self-generation and customers interested in municipal power have also continued to submit comments on the Settlement's provisions, all of which have been considered.

i. Recently Settled and Corrected Matters

By letter dated January 22, 1998, Niagara Mohawk notified us that, as contemplated by the Settlement, various parties had considered the details of an implementation mechanism for the expanded LICAP program and had reached an agreement. These parties arrived at a performance incentive mechanism that contains annual enrollment, service, and workshop goals for the company to meet. Niagara Mohawk's failure to achieve these goals would subject the company to financial penalties of up to

[1] We are aware that Niagara Mohawk is participating in ongoing negotiations with the City of Oswego, County, and School District representatives on the future tax status of the company's facilities in Oswego. We consider such negotiations between municipalities and utility companies to be a beneficial means for resolving such issues, absent legislation.

$1.1 million per year. The company will also provide quarterly and annual reports concerning its progress and performance.

By letter dated January 23, 1998, the company also notified us that various parties have agreed on provisions for the customer service backout credit, as provided by the Settlement. Niagara Mohawk's revenue exposure for these credits is limited to $30 million during the first three years covered by the Settlement. This amount is allocated among the company's service classes and, if the class allocations are reached, access to the credits will be restricted. Staff will review the company's subscription levels, historical data, and its calculations when the available amounts may be exhausted. ESCOs will also be informed of the amounts that remain available to them.

While we received these agreements after briefs opposing exceptions were filed, the parties to these proceedings were on notice that these matters would be considered and that the details of the LICAP performance incentive mechanism and a customer service backout credit would be submitted to us for consideration with the Settlement. This approach drew no objections when it was presented nor has any party criticized the specific provisions that have been reached. Accordingly, we will adopt the agreed-upon terms for these two additional issues.

Finally, by letter dated February 13, 1998, Niagara Mohawk notified us that a provision the parties had intended to include in the Settlement was inadvertently omitted. The Settlement eliminates Niagara Mohawk's fuel adjustment clause (FAC). However, when the FAC ends, the company will have either a positive or negative deferred fuel balance that must either be paid back to customers or collected from them. The settling parties intended to include in the Settlement a provision to flow through the deferred fuel balance to customers over two monthly billing cycles. To accomplish this, the company has provided a revision for Settlement §4.3.1. We accept this revision to the Settlement to the extent it allocates to customers deferred costs or benefits properly allocable to them.

j. Finch's Exceptions

Finch urges us to adopt and apply four general principles to on-site generation:

> (1) Supplemental service rates for on-site generators should be the same as the rates that apply to full service customers in the same service category;
>
> (2) Backup and maintenance service rates for on-site generators should be set using the same cost method that is used to develop rates for similar full requirements customers;
>
> (3) On-site generators should be given the option to obtain firm service at the same rates that apply to similar customers without on-site generation; and,
>
> (4) Customers with existing on-site generation facilities should not be transferred to a new service class that would substantially increase the rates applicable to them.

Finch complains that the Settlement proponents have not provided a proposed tariff for the on-site generation parties to examine and see how the Settlement would actually apply to them. It insists that only a smattering of general concepts has been offered for consideration. Finch is concerned about such things as the amount of the proposed access charges, the applicable energy rates, surcharges, and reconciliations. It also claims that the proponents do not share a common understanding of the Settlement's on-site generation rate, tariff, and stranded cost provisions. Given such uncertainties as these, Finch says, it is impossible for on-site generation customers to determine how the Settlement specifically affects them. It believes this portion of the Settlement should be rejected and Niagara Mohawk should be required to provide a specific proposal for consideration now.

Also with respect to the Settlement's on-site generation provisions, Finch claims they are unduly discriminatory, unjust and unreasonable, and not in the public interest. It says they are contrary to the Public Service Law, the Public Utility Regulatory Policies Act (PURPA), and the Federal Energy Regulatory Commission (FERC) regulations implementing PURPA. Further, it maintains they are anti-competitive and preclude on-site generators from using economically competitive alternatives.

In response to Finch, the company points out that this party entered the proceedings after the close of the record, did not contribute to the record, and did not participate in the settlement process. Nonetheless, the company responds to Finch's policy and legal arguments.

As to Finch's concerns about rate discrimination, Niagara Mohawk says the existing and proposed service classes for on-site generators are based on their common characteristics and cost of service. It points out that such customers require continuous connections to the company's system for backup power and, as a group, they have distinguishable load and cost characteristics. The company contends that the Settlement's provisions for these customers are designed to recover the fixed costs associated with each customer's historic level of usage and to recover a proper share of stranded costs. Thus, the company says Finch errs in claiming that the Settlement's S.C. 7 provisions are not cost based.

With respect to whether the intended revisions for S.C. 7 should have been submitted with the Settlement, Niagara Mohawk says the Settlement contains the complete proposal for revising the service classification and nothing more is needed for it to be approved. Given the complexity of these proceedings and large amount of activity they require, the company claims it is reasonable for action on the S.C. 7 tariff revisions to follow the Settlement's approval.

Concerning the claim that the on-site generation rate proposal violates state and federal statutes and regulations, Niagara Mohawk denies Finch's assertion. The company insists that the Settlement's provisions are consistent with PURPA and FERC regulations requiring that accurate data and consistent systemwide costing principles be used to set all customers' rates. Finch objects to the rate reductions for customers other than on-site generators; but, the company says this aspect of the Settlement is not discriminatory. Niagara Mohawk points out that the parties vigorously negotiated allocation of the rate decreases and applying the rate decreases to full service customers is fully justified.

Next, Niagara Mohawk says on-site generators must pay stranded costs because the company stands ready to serve their load requirements at any time. According to the company, the valid reasons for not treating on-site generators the same as full requirement customers include the need to discourage uneconomic bypass and to avoid shifting costs to other ratepayers.

Finally, the company says the Settlement's on-site generation provisions are clear and it will not have any difficulties submitting a revised S.C. 7 that complies with the Settlement. To the extent any party's view of the Settlement's requirements differs from the company's, it says any such matters can be resolved when the revised tariffs are filed.

MI says Finch's claims of disparate treatment should not be credited because the Settlement does not produce or require any such results. MI suggests that Finch wait and see the new, on-site generation tariffs the company proposes, and the results of Niagara Mohawk's generation auction, before it launches any such charges.

MI is correct that Finch's concerns about the actual rates and charges Niagara Mohawk will file to implement the Settlement's provisions applicable to on-site generation are premature and should await the company's tariff filing. When the tariff is submitted, Finch and other parties will have an opportunity to examine it and provide their comments.

In any event, Finch's broad criticisms and legal challenge of the Settlement's on-site generation provisions are rejected. Like all other classes of customers, the on-site generators that subscribe to Niagara Mohawk's backup and supplemental services must bear a portion of the company’s stranded costs in fairness to all other customers who must also pay these costs. Moreover, it is reasonable to revise the S.C. 7 tariff due to the company’s restructuring and the transition being made to a competitive market. During the transition period, uneconomic alternatives should not be encouraged as the company must be assured of a reasonable opportunity to pay its MRA-related costs.

We have examined Finch’s claims of discrimination and anti-competitive rates and find that the Settlement’s on-site generation provisions do not violate any state or federal requirements that preclude undue discrimination and anti-competitive behavior. The Settlement proponents have detailed and supported the Settlement’s acceptable approach to this class of customers. Clear differences exist between these customers and the company’s full requirements customers supporting the separate classifications and the differing treatment they receive under the Settlement. There is, therefore, no need to adopt Finch’s four general principles for on-site generators. The principles we normally adhere to design rates and to allocate revenue requirements will continue to apply except to the extent the Settlement requires any departures for its proper implementation.

Finally, as discussed above, in making the transition from the existing S.C. 7 tariff to the revised tariff required by the Settlement, we are concerned that there not be any harsh impact for customers who, as of October 10, 1997, decided to implement on-site generation and have made a substantial investment. Niagara Mohawk will be required to present a proposal addressing this concern, and the parties may comment on it, before we consider the company’s revised tariffs for S.C. 7. To the extent any other matters require our attention, there will be ample opportunity for the parties to state specific concerns in their comments on the company’s on-site generation tariff revisions.

k. Recovery of Costs Associated With Termination of Gas Transportation and Peak Shaving Agreements

Appendix B of the Settlement provides that the company would continue to recover, solely from gas customers, lost revenues or additional costs incurred in connection with new peak shaving and gas transportation contracts, in effect extending the terms and duration of the Stipulation and Agreement among the parties in Cases 95-G-1095 and 95-G-0091. We approve the gas-customer-only recovery mechanism to the extent it is limited to lost revenues and replacement costs incurred between now and October 31, 1999, as provided in the Gas Stipulation and Agreement. However, without fuller explanation of the relative benefits of restructuring the peak shaving and transportation contracts, we are unwilling at this time to extend this gas-customers-only recovery mechanism beyond October 31, 1999. We shall review the appropriate allocation between the gas and electric departments at the time the company files its proposed recovery mechanism of such lost revenues and replacement costs beyond October 31, 1999.

l. Service Quality Incentive

Section 6 of the Settlement describes a service quality incentive whose total value is $6.6 million (30 basis points) per year. The total would be allocated one half to a customer service performance inventive and the balance would be for a service reliability incentive. The company is not now providing high levels of service and it will continue to face serious financial pressures. In these circumstances, a strong incentive is appropriate. To ensure that the company remains focused on its service obligations during the Settlement term, this provision is adopted subject to the modification that the $6.6 million is doubled and all the maximum dollar penalties associated with various scored intervals are doubled accordingly.

CONCLUSION

The terms of the Settlement and the Master Restructuring Agreement, summarized and discussed above, will offer a generally sound regulatory framework for Niagara Mohawk, its competitors, and its customers in the transition to fully competitive generation and energy services markets. Among other things, the Settlement and MRA reverse the upward spiral of rate increases experienced by ratepayers in the past and replace it with significant rate decreases. These rate reductions, brought about primarily by the company's absorption of up to $2 billion in revenue losses, savings from the MRA, and reduced taxes, avoid the need to consider the company's alternative pending request for a $3.25 million (10.5%) rate increase and the prospect of further rate increases driven by uneconomic power purchase contracts.[1] The majority of the nominal revenue reductions will be enjoyed by the residential and commercial classes. At the same time, significant rate reductions will be implemented for large industrial and commercial customers, reductions which are essential to attract and retain jobs and boost the economy of upstate New York. Other important benefits include the company's prompt divestiture of its fossil and hydro generation and the restructuring of a substantial amount of IPP generation capacity to market pricing. In 1999, all customers will have the ability to choose their energy supplier. These benefits, in our view, would not be achieved by any of the alternatives that have been presented or that we are otherwise aware of, including the bankruptcy alternative and the various legislative proposals now pending.

Having reviewed the Settlement's terms, the recommended decision, the parties' exceptions, the public's comments, and the Environmental Assessment Form prepared for us by our Staff, we find that there are several terms that are not satisfactory under the circumstances presented. They are discussed in detail above.

[1] Niagara Mohawk's contractual commitments to the IPPs alone have been rising by $50 million per year. Tr. 13,040.

Such items include the terms for the proposed cost recovery shift from energy to customer charges for the residential and small commercial classes, the base period for implementing the S.C. 1 and S.C. 2 rate reductions, the prejudgment of a royalty treatment beyond the Settlement's term, the incentive for divestiture of non-Oswego fossil and hydro generation, service quality penalties, recovery of certain lost gas revenues and new gas costs, and the disposition of certain tax refunds.

These and other terms of concern to us are adopted subject to the conditions or modifications described above or, in the case of the proposed customer charge increases, are not adopted at this time. With the modifications and conditions, the Settlement and Master Restructuring Agreement satisfy the objectives enumerated in Opinion No. 96-12 and meet the criteria states in our Settlement Guidelines.

Accordingly, the terms of the Settlement and the Master Restructuring Agreement are adopted with all the modifications and changes discussed in this opinion and order. Inasmuch as those terms and our modifications and conditions are interrelated, if any term, modification, or condition is modified, vacated, or otherwise materially affected on judicial review, we may re-examine our entire decision.

<u>The Commission Orders</u>:

1. The terms of the Niagara Mohawk Power Corporation PowerChoice Settlement Agreement, Exhibit 97-1 in these proceedings, including the revisions submitted by letters dated December 9, 1997 and February 13, 1998, and the supplements submitted by letters dated January 22 and 23, 1998, subject to the modifications and conditions described in this opinion and order, are adopted and incorporated as part of this opinion and order.

2. Niagara Mohawk Power Corporation is directed to cancel the suspended tariff amendments and supplements listed in Appendix B concurrent with the effective date of tariffs filed in

conjunction with the implementation of the PowerChoice Settlement Agreement, the PowerChoice Implementation Date.

3. The company is directed to file as soon as is reasonably possible, but not later than May 19, 1998, tariff amendments implementing the Settlement. The amendments shall become effective on not less than sixty (60) day's notice. The company shall serve copies of its compliance filing upon all parties to this proceeding. Any comments on the filing must be received at the Commission's offices within 45 days of service of the company's proposed amendments. The amendments shall not become effective on a permanent basis until approved by the Commission. The requirement of the Public Service Law that newspaper publication be completed prior to the effective date of the amendments is waived, but the company is directed to file with the Commission, not later than six weeks following the effective date of the amendments, proof that a notice of the changes set forth in the amendments and their effective date has been published for four consecutive weeks in a newspaper having general circulation in the service territory of the company.

4. Sections 4.5.1.2, 4.6.1.2 and 4.6.2.1 of the agreement addressing the rebalancing of customer and energy charges shall be modified as follows:

> Monthly customer charges for residential, small commercial non-demand and demand metered customers shall be fixed at $9.67, $14.65, and $27.22, respectively, at this time.

The parties may address the customer charge/energy charge rebalancing issues presented in these proceedings commensurate with the review period preceding Commission approval of unbundled tariffs for these customers.

5. The primary tariff filings directed in Clause 3 above required to effectuate initial implementation of the PowerChoice Settlement Agreement shall include unbundled retail access tariffs for Customer Groups I and II, as defined in §8.2 of the agreement, bundled (standard) tariffs for all remaining

customers not included in the above, and shall reflect the price reductions specified in §4.0 of the agreement and otherwise described herein. Subsequent unbundled tariff filings for customers in Groups III, IV and V should be made at least ninety (90) days prior to each group's scheduled date for obtaining retail access.

6. Niagara Mohawk Power Corporation is directed to file by no later than April 3, 1998 a tariff amendment, to become effective on one day's notice on a temporary basis, to grandfather the electric rates applicable to on-site generators who can demonstrate that as of October 10, 1997 they had made a decision to proceed with and had a substantial investment in self-generation. The company shall serve copies of its proposal upon all parties to this proceeding. Any comments on the proposal must be received at the Commission's offices within 10 days of service of the company's proposal. The amendments shall not become effective on a permanent basis until approved by the Commission. The requirement of the Public Service Law that newspaper publication be completed prior to the effective date of the amendments is waived, but the company is directed to file with the Commission, not later than six weeks following the effective date of the amendments, proof that a notice of the changes set forth in the amendments and their effective date has been published for four consecutive weeks in a newspaper having general circulation in the service territory of the company.

7. Niagara Mohawk is authorized to file tariff amendments, to become effective on not less than one day's notice on a temporary basis, to implement the open access charges for municipalizations. Any comments on the proposal must be received at the Commission's office within 10 days of service of the company's proposal. The amendments shall not become effective on a permanent basis until approved by the Commission. The requirement of the Public Service Law that newspaper publication be completed prior to the effective date of the amendments is waived, but the company is directed to file with the Commission, not later than six weeks following the effective date of the

amendments, proof that a notice of the changes set forth in the amendments and their effective date has been published for four consecutive weeks in a newspaper having general circulation in the service territory of the company.

8. To the extent exceptions to the recommended decision issued in these proceedings on December 29, 1997 are not moot, or are otherwise granted, they are denied.

9. The potential environmental impacts of these terms are within the bounds and thresholds evaluated in the 1996 FGEIS, and, therefore, no further SEQRA action is necessary in these cases at this time.

10. Niagara Mohawk, in cooperation with Staff, shall monitor the environmental impacts of electric restructuring resulting from this order.

11. Niagara Mohawk is authorized to include the following decommissioning related activities in its cost of service for Nine Mile 1: rampdown, wet fuel storage, dry fuel storage, and radioactive dismantlement costs in the amount of $23,227,000 in each year commencing on April 1, 1998 through 2009, unless and until the Commission orders otherwise. The company is authorized to deposit $18,494,000 of its Nine Mile 1 decommissioning authorization in a tax qualified nuclear decommissioning fund and $4,733,000 in a non-qualified nuclear decommissioning fund. The company is also authorized to include in its cost of service, the following decommissioning related activities for its 41% share of Nine Mile 2: rampdown, wet fuel storage, dry fuel storage, and radioactive dismantlement costs in the amount of $4,776,000 which it is authorized to deposit in each year commencing on April 1, 1998 through 2026 in a tax qualified nuclear decommissioning fund, unless and until the Commission orders otherwise. These plant decommissioning authorizations are based on plant specific studies escalated using the estimated escalation factors described below. The estimated decommission related activities of Nine Mile 1 and the company’s 41% share of Nine Mile 2, in 1998 dollars, are $518 million and $262 million, respectively. Using an escalation

factor of 3.5%, the Nine Mile Unit 1 radioactive decommissioning costs are estimated to be approximately $901 million in 2009, and the company's share of the Nine Mile 2 radioactive decommissioning cost is estimated to be about $802 million in 2026. The funding assumptions are based upon the DECON method of decommissioning and are assumed to be incurred between 2009 and 2041 for Nine Mile 1 and between 2026 and 2045 for Nine Mile 2. These time periods presently represent the respective years over which each plant is assumed to be decommissioned. An after-tax trust fund earning rate of 6.3% was used for the Nine Mile 1 trust fund and a 6.9% rate for the Nine Mile 2 trust fund. All applicable costs collected from ratepayers shall be deposited by the company in external trust funds on a quarterly basis.

12. For each of the five years of the Settlement period, Niagara Mohawk Power Corporation is directed to defer any interest rate savings related to the senior subordinated notes or other debt instruments used to finance the MRA buyout. The savings will be calculated by comparing the actual interest rate(s) to the 8.5% interest rate forecasted for such debt as included in Appendix C of the Settlement. The savings will be included in Account 253, Other Deferred Credits, until such time the Commission utilizes the deferred savings.

13. Niagara Mohawk Power Corporation shall submit a written statement of unconditional acceptance of the modifications and conditions contained in this opinion and order, signed and acknowledged by a duly authorized officer of the company by April 3, 1998. The company's statement should be filed with the Secretary of the Commission and served on the parties to these proceedings.

14. Cases 94-E-0098 and 94-E-0099 are continued.

By the Commission,

(SIGNED) JOHN C. CRARY
Secretary

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Amendments to Schedule P.S.C. No. 207 - Electricity

Original Leaves Nos. 71-U, 101-B, 101-C, 101-D, 101-E, 101-F, 101-G, 101-H
First Revised Leaves Nos. 79-N, 83-A7, 87-A4, 87-A5
Second Revised Leaves Nos. 70-C2, 70-H, 71-C, 79-0, 87-F2, 106-B, 165
Third Revised Leaves Nos. 97-A, 100, 151
Fourth Revised Leaves Nos. 57-A, 70-E, 106-A
Fifth Revised Leaves Nos. 57-B1, 70-I
Sixth Revised Leaves Nos. 57-B, 105
Seventh Revised Leaves Nos. 57-C, 106
Eighth Revised Leaf No. 79-I
Ninth Revised Leaf No. 79-F
Eleventh Revised Leaf No. 83-A3
Twelfth Revised Leaf No. 83-A4
Thirteenth Revised Leaves Nos. 67, 79
Fifteenth Revised Leaf No. 55-B
Seventeenth Revised Leaf No. 70-D
Eighteenth Revised Leaf No. 2
Nineteenth Revised Leaf No. 55-A
Twentieth Revised Leaf No. 101-A
Twenty-First Revised Leaf No. 56
Twenty-Second Revised Leaves Nos. 58, 99, 102
Twenty-Third Revised Leaves Nos. 57, 98
Twenty-Sixth Revised Leaf No. 95
Twenty-Ninth Revised Leaf No. 85
Thirtieth Revised Leaf No. 103
Thirty-First Revised Leaves Nos. 87-C, 97, 101
Thirty-Fifth Revised Leaves Nos. 55, 104
Forty-First Revised Leaves Nos. 3, 89
Forty-Third Revised Leaf No. 81
Forty-Ninth Revised Leaf No. 83
Fifty-Fourth Revised Leaf No. 94
Fifty-Fifth Revised Leaf No. 80
Fifty-Sixth Revised Leaf No. 88
Fifty-Seventh Revised Leaf No. 84
Fifty-Eighth Revised Leaf No. 78

Supplements Nos. 207, 215, 217 and 223 to Schedule P.S.C. No. 207 - Electricity

Amendments to Schedule P.S.C. 213 - Electricity (Street Lighting)

First Revised Leaf No. 80
Second Revised Leaf No. 78
Third Revised Leaves Nos. 44, 79, 81, 84
Twelfth Revised Leaves Nos. 9, 47
Sixteenth Revised Leaf No. 55
Seventeenth Revised Leaf No. 20
Eighteenth Revised Leaf No. 49
Twenty-Fifth Revised Leaf No. 43
Twenty-Seventh Revised Leaf No. 46
Thirtieth Revised Leaf No. 45
Thirty-Fourth Revised Leaves Nos. 30, 33, 34, 36, 40, 41
Thirty-Fifth Revised Leaves Nos. 28-A, 31, 37
Thirty-Sixth Revised Leaves Nos. 5, 6, 26, 28
Thirty-Seventh Revised Leaves Nos. 27, 38, 39
Thirty-Eighth Revised Leaves Nos. 16, 32, 35
Thirty-Ninth Revised Leaves Nos. 15, 29
Fortieth Revised Leaf No. 13
Forty-Second Revised Leaf 14
Forty-Third Revised Leaf 25

Supplements Nos. 67, 68 69 and 70 to Schedule P.S.C. No. 207 - Electricity

APPENDIX C

State Environmental Quality Review

ENVIRONMENTAL ASSESSMENT FORM

PROJECT INFORMATION

1. APPLICANT/SPONSOR: Niagara Mohawk Power Corporation (NMPC)	2. PROJECT NAME: **Elect.Rate/Restructuring - Case 94-E-0098, 94-E-0099**

3. PROJECT LOCATION: **NMPC Service Territory**
Municipality **NA** County **NA**

4. PRECIS**E LOCATION: (Street address and road intersections, prominent landmarks, etc., or provide map)**
NA

5. PROPOSED ACTION IS:
☐New ☐Expansion ☒ Modification/alteration

6. DESCRIBE PROJECT BRIEFLY: **Cases 94-E-0952, 94-E-0098 and 94-E-0099 - In the matter of competitive opportunities regarding electric service, filed in Case 93-M-0229; Plans for electric rate/restructuring pursuant to Opinion No. 96-12; and the formation of a holding company pursuant to PSL, §§ 70, 108 and 110, and certain related transactions -- Environmental Assessment Form.**

7. AMOUNT OF LAND AFFECTED: **NA**
Initially________acres Ultimately_________acres

8. WILL PROPOSED ACTION COMPLY WITH EXISTING ZONING OR OTHER EXISTING LAND USE RESTRICTIONS?
NA
☐Yes ☐No If No, describe briefly

9. WHAT IS PRESENT LAND USE IN VICINITY OF PROJECT?
NA
☐Residential ☐Industrial ☐Commercial ☐Agricultural ☐Park/Forest/Open space ☐Other

Describe:

10. DOES ACTION INVOLVE A PERMIT APPROVAL, OR FUNDING, NOW OR ULTIMATELY FROM ANY OTHER GOVERNMENTAL AGENCY (FEDERAL, STATE OR LOCAL)?

☒ Yes ☐No If yes, list agency(s) name and permit/approvals: NYS Public Service Commission

11. DOES ANY ASPECT OF THE ACTION HAVE A CURRENTLY VALID PERMIT OR APPROVAL?

☐Yes ☐No If yes, list agency(s) name and permit/approval **Stationary sources owned and operated by NMPC have valid, approved certificates to operate.**

12. AS A RESULT OF PROPOSED ACTION WILL EXISTING PERMIT/APPROVAL REQUIRE MODIFICATION? **NA**
☐Yes ☐No

I CERTIFY THAT THE INFORMATION PROVIDED ABOVE IS TRUE TO THE BEST OF MY KNOWLEDGE

Agency: **NYS Department of Public Service** Date: February 13, 1998

Signature:______________________________

PART II-ENVIRONMENTAL ASSESSMENT

A. DOES ACTION EXCEED ANY TYPE 1 THRESHOLD IN 6 NYCRR, PART 617.4? If yes, coordinate the review process and use the FULL EAF. ☐Yes ☒ No

B. WILL ACTION RECEIVE COORDINATED REVIEW AS PROVIDED FOR UNLISTED ACTIONS IN 6 NYCRR, PART 617.6? If No, a negative declaration may be superseded by another involved agency. **NA** ☐Yes ☐No

C. COULD ACTION RESULT IN ANY ADVERSE EFFECTS ASSOCIATED WITH THE FOLLOWING: (Answers may be handwritten, if legible.)

C1. Existing air quality, surface or groundwater quality or quantity, noise levels, existing traffic patterns, solid waste production or disposal, potential for erosion, drainage or flooding problems? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

C2. Aesthetic, agricultural, archaeological, historic, or other natural or cultural resources; or community or neighborhood character? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

C3. Vegetation or fauna, fish, shellfish or wildlife species, significant habitats, or threatened or endangered species? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

C4. A community's existing plans or goals as officially adopted, or a change in use or intensity of use of land or other natural resources? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

C5. Growth, subsequent development, or related activities likely to be induced by the proposed action? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

C6. Long term, short term, cumulative, or other effects not identified in C1-C5? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

C7. Other impacts (including changes in use of either quantity or type of energy)? Explain briefly:

Expected impacts are within the range of thresholds and conditions set forth in the FGEIS.

D. WILL THE PROJECT HAVE AN IMPACT ON THE ENVIRONMENTAL CHARACTERISTICS THAT CAUSED THE ESTABLISHMENT OF A CRITICAL ENVIRONMENTAL AREA (CEA)? ☐Yes ☒ No If Yes, explain briefly:

E. IS THERE, OR IS THERE LIKELY TO BE, CONTROVERSY RELATED TO POTENTIAL ADVERSE ENVIRONMENTAL IMPACTS? ☐Yes ☒ No If Yes, explain briefly:

Part III - DETERMINATION OF SIGNIFICANCE (To be completed by Agency)

See the attached Environmental Assessment Form Narrative.

Staff recommends that the Final Generic Environmental Impact Statement (FGEIS) issued on May 3, 1996 (Case 94-E-0952), with respect to the proposed action of adopting a policy supporting increased competition in electric markets be extended in applicability, without modification or supplementation, to the approval of New Niagara Mohawk Power Corporation (The Corporation) Agreement and Settlement on the grounds that the significance of the proposal's anticipated environmental impacts will not exceed the threshold values examined in the FGEIS. Consequently, no further State Environmental Quality Review Act (SEQRA) action is necessary in approving the Proposal.

Staff further recommends that a monitoring program be instituted to provide a record of changes resulting from the restructuring plan's implementation to enable confirmation and/or exposition of unexpected outcomes and their significance, and to assure that specific mitigation measures are implemented as needed.

NYS Department of Public Service	February 13, 1998
Name of Lead Agency	Date
John H. Smolinsky	**Chief, Environmental Compliance and Operations**
Print or Type Name of Responsible Officer in Lead Agency	Title of Responsible Officer
Signature of Responsible Officer in Lead Agency	Signature of Preparer(If different from responsible officer)

ENVIRONMENTAL ASSESSMENT FORM

I. BACKGROUND

On May 3, 1996, the Commission issued a Final Generic Environmental Impact Statement (FGEIS) in the Competitive Opportunities proceeding which addressed the environmental impacts of a policy supporting increased competition in electric markets. Alternative approaches to achieving electric competition, including a no-action alternative, were studied.

In Opinion No. 96-12[1] issued May 20, 1996, the Commission set forth its findings with respect to the FGEIS (p.76-81). The Commission determined that the likely environmental effects of a shift to a more competitive market for electricity are not fully predictable but that:

> In general, the proposed action will have environmental impacts that are modest or not distinguishable from those of alternative actions, including the no-action alternative... Apart from the areas of substantial concern noted below, the FGEIS did not identify reasonably likely significant adverse impacts.
>
> With respect to air quality impacts related to oxides of nitrogen and sulfur, it appears likely that the retail or wholesale electric market structures would have greater impacts than the no action alternative. It appears likely that, in the absence of mitigation measures, research and development in environmental and renewables areas would lose funding if competitive restructuring moves forward. In addition, there would likely be a decrease in the amount of cost-effective energy efficiency during any transition to wholesale or retail competition...
>
> In order to address the adverse environmental effects identified above on air quality, energy efficiency, and research and development, several mitigation measures will be employed as necessary. First, a system benefits charge will be used as appropriate to fund DSM and research and development in environmental and renewable resource areas during the transition to competition. Second, the competitive restructuring will be monitored closely to ensure that specific mitigation measures are implemented if needed. Finally, the Commission will support and assist efforts

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[1] Cases 94-E-0952, et al., In the Matter of Competitive Opportunities Proceeding Regarding Electric Service, Opinion No. 96-12 (issued May 20, 1996).

> by New York State and federal agencies to ensure that adverse environmental impacts to the state's air quality from upwind sources of air contamination do not occur as a result of the movement toward competition.
>
> Notwithstanding the mitigation measures identified, the proposed action to restructure the electric industry may result in an unavoidable adverse environmental impact on air quality related to oxides of nitrogen and sulfur, loss of some DSM activity, loss of some research and development funding in the environmental and renewables areas, and displacement of workers and local economic loss where plants are closed. Nevertheless, weighing and balancing these likely environmental effects of the shift to competition in the electric industry in New York with social, economic, and other essential considerations, leads to the conclusion that implementing the proposed action toward greater competition is desirable.

The Commission also recognized that individual utility proposals might bring to light new concerns. In Opinion No. 96-12,[1] and as further clarified in Opinion No. 96-17,[2] it required each utility to file with its restructuring plans an Environmental Assessment Form and a recommendation on further environmental review. The information to be provided was expected to assist the Commission in determining the need for additional mitigation measures with respect to company restructuring.

On August 26, 1997, Niagara Mohawk submitted its Environmental Assessment Form (EAF) and SEQRA recommendation in connection with its initially proposed PowerChoice restructuring plan in Case 94-E-0098 and Case 94-E-0099. This proposal served as the basis for negotiations between the company, Staff and interested parties. On October 10, 1997, the company, Staff and many of the interested parties signed a restructuring settlement.

On November 4, 1997, the company filed a supplement to its EAF which addressed the environmental implications of areas

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[1] Ibid, p. 78, n. 1.

[2] Cases 94-E-0952, et al., Competitive Opportunities Proceeding Rehearing Petitions, Opinion No. 96-17 (issued October 24, 1996).

where the negotiated settlement differed from the original proposal. On November 12, 1997, Administrative Law Judge Bouteiller issued a procedural ruling which requested parties in Case 94-E-0098 to file initial comments on the supplemented EAF by December 3, 1997. Comments were received from the Steam Host Action Group (SHAG) and Multiple Intervenors (MI) on that date. No other parties submitted formal comments at that time. However, a number of parties, including the City of Oswego, commented on the EAF or on environmental issues in their briefs.

SEQRA and Commission Approval of the Niagara Mohawk Restructuring Plan - Options Before the Commission

The FGEIS issued by the Commission in conformance with SEQRA in Case 94-E-0952, et. al., addressed the following proposed action:

> "adoption of a policy supporting increased competition in electric markets, including a preferred method to achieve electric competition; and regulatory and ratemaking practices that will assist in the transition to a more competitive and efficient electric industry, while maintaining safety, environmental, affordability, and service quality goals."[1]

Commission approval of Niagara Mohawk's proposed restructuring plan constitutes a "subsequent proposed action." SEQRA requirements with respect to this "subsequent proposed action" allow the Commission to pursue one of the four following options:

1. No further State Environmental Quality Review (SEQRA) compliance is required if a subsequent proposed action will be carried out in conformance with the conditions and thresholds established for such actions in the generic Environmental Impact Statement (EIS) or its findings statement.

2. An amended findings statement must be prepared if the subsequent proposed action was adequately addressed in the generic EIS but was not addressed or was not adequately addressed in the findings statement for the generic EIS.

[1] Cases 94-E-0952, et al., Competitive Opportunities Proceeding, Opinion No. 96-12 (issued May 20, 1996), p. 76.

3. A negative declaration must be prepared if a subsequent proposed action was not addressed or was not adequately addressed in the generic EIS and the subsequent action will not result in any significant environmental impacts.

4. A supplement to the final generic EIS must be prepared if the subsequent proposed action was not addressed or was not adequately addressed in the generic EIS and the subsequent action may have one or more significant adverse environmental impacts.[1]

The following environmental assessment will assist in choosing the appropriate option. The assessment is based on Niagara Mohawk's EAF, party comments submitted in response to the company's EAF, and on additional analysis by Department Staff. In addition, the EAF will consider certain generic comments raised by Public Interest Intervenors in its May 13, 1997 petition requesting that the Commission order the filing of supplemental environmental impact statements in all restructuring cases. The Assessment consists of:

Section II - summarizes the proposed settlement agreement.

Section III - summarizes the Environmental Assessment Form submitted by the company.

Section IV - summarizes party comments on the company's EAF.

Section V - Staff's analysis of the environmental impacts of the proposed settlement.

Section VI - recommends mitigation and monitoring plan.

Section VII - Staff's overall conclusions and recommendations.

II. NMPC Proposed Restructuring Settlement

Under the proposal, residential and smaller commercial customers would receive rate reductions phased in over the first three years of the settlement which would amount to an average reduction of 3.2% by the year 2000. Large industrial customers

[1] 6 NYCRR Part 617.10(d).

would receive reductions in their NMPC rates which would average 13% by the year 2000.

The agreement requires the company to auction virtually all of its non-nuclear generation and prohibits the company and its subsidiaries from owning generation in New York in the future. The company’s nuclear generation will be placed in a separate business unit but retained pending a statewide solution to the nuclear issue.

The plan also provides for phase-in of retail access for all customers by December of 1999. A competitive transition charge (CTC) will be charged all customers in order to collect stranded costs.

The plan establishes a $10 million fund which will be used for programs such a retraining, outplacement and early retirement of its employees to mitigate any employment impacts caused by the auction or retirement of its generating plants.

Under the plan, the company would continue its current program to remediate pollution at coal gas production sites. The plan also provides for the continuation of low income programs and for the institution of a $15 million per year System Benefits Charge to be used for RD&D energy conservation and other public benefit programs. The company has also agreed to retire 5000 SO_2 allowances and to transfer ownership or conservation easements for a number of land parcels in the Adirondacks to New York State.

In a separate but related action, the company negotiated an agreement (the Master Restructuring Agreement or MRA) with certain Independent Power Producers (IPPs) which are currently selling power to NMPC under "must run" contracts which are unfavorable to the company. This agreement will modify or terminate the contracts of the settling IPPs. A number of these IPPs also provide steam under contract to industrial customers (Steam Hosts).

III. The NMPC Environmental Assessment Form (EAF)

On August 26, 1997, Niagara Mohawk filed an EAF covering the environmental impacts of NMPC’s July 23 PowerChoice

Proposal. Subsequently, the company's proposal was modified as a result of settlement negotiations, culminating in an Agreement filed October 10, 1997. On November 4, 1997, the company filed a supplement to the EAF which addressed additional areas of environmental concern raised by details of the final settlement. In comprehensiveness and analytic depth, the NMPC EAF exceeds those submitted by other utilities in their restructuring cases.

As the basis for much of its EAF, NMPC ran a series of PROMOD computer analyses which simulated plant dispatching under various scenarios associated with the PowerChoice Proposal. The scenarios differed from one another in terms of assumed demand levels, IPP operations, Demand Side Management levels, and the early retirement of nuclear and certain fossil units, but encompassed the likely range of outcomes from PowerChoice. The company compared these scenarios to an NMPC-generated "no-action" base case and to the PROMOD runs contained in the FGEIS. The company reports that the potential air quality impacts associated with the scenarios fell well within the limits projected in the FGEIS scenarios.

The company argues that since existing generating facilities in New York have received permits which allow operation up to design capacity, and since operation at full design capacity was considered in the permitting process, changes in plant operation due to PowerChoice will not have significant aquatic or water quality effects beyond those already considered and found acceptable.

The company notes that while PowerChoice will have overall beneficial effects on the State's economy, a more competitive environment could result in localized socio-economic impacts, including loss of employment and tax revenues, if some existing NMPC or IPP plants are retired earlier than they otherwise would have been. Other communities might benefit from the construction of new competitive plants. Statewide employment levels should rise as an indirect effect of lower electricity prices.

The company's supplemented EAF also addressed the question of the indirect effect of the MRA on IPP steam hosts.

The company estimates that, at most, only 14 million mmBtu per year of steam production, or about 15% of the total IPP steam production, will be retired or mothballed as a result of the MRA. Only about 5% of that 14 million mmBtu is currently being used by steam hosts. Since this is only 0.07% of the over 1 billion mmBtu annual steam production in the NMPC system, the incremental air quality impacts of any changes in emissions resulting from steam hosts running less efficient boilers to replace IPP steam are immaterial and fall within the limits considered in the FGEIS.

The company notes in its supplemented EAF that the donation of SO_2 allowances, the $15 million per year SBC fund and the negotiated transfer of environmentally significant land parcels will result in environmental benefits not considered in the July 23 PowerChoice proposal.

The company also states that the PowerChoice proposal will not affect the company's existing Site Investigation and Remediation (SIR) program--which is designed to identify and mitigate polluted sites owned by the company.[1]

IV. Comments on the Niagara Mohawk EAF

On November 4, 1997, NMPC submitted a supplemented EAF which addresses issues arising from the negotiated agreement. Comments on the EAF were received from the Steam Host Action Group (SHAG) and Multiple Intervenors (MI) on December 3, 1997. Other parties, including the City of Oswego, addressed environmental issues in their briefs.

Comments Submitted on the Supplemented EAF

SHAG's comments addressed only one issue--the potential socio-economic effects of changes in contracts between NMPC and certain IPPs on some industrial customers who purchase cogenerated steam from the IPPs. For a number of years, NMPC has

[1] These are primarily sites where coal gas was produced for illumination during the 19th century which were acquired by NMPC during the period of consolidation of smaller utilities which resulted in the creation of NMPC.

had "must run" contracts to purchase power at above market prices from a number of IPPs. Many of those IPPs have had "steam host" customers who purchased steam or hot water which was produced as a byproduct of electric generation. Part of the negotiated settlement is a Master Restructuring Agreement (MRA) which sets the ground rules whereby NMPC and certain of these IPPs will modify or terminate their contracts.

SHAG states in its comments on the EAF that the termination of contracts between IPPs and NMPC may lead some IPPs to breach their contracts with the steam hosts. This might increase the costs of the steam hosts or disrupt their operations. In either event, layoffs and economic harm to communities containing the steam hosts might follow. SHAG states that these issues are not adequately addressed in the company’s supplemented EAF and urges the Commission to take steps to mitigate the impacts of the MRA on its members.

In its comments, MI states that the EAF adequately addresses all potential environmental impacts and that no further action under SEQRA is required. MI does support, however, SHAG’s request that the Commission adopt measures to mitigate the potential effects of the MRA on steam hosts.

Related Comments in Initial Briefs

Several parties also addressed the EAF, or environmental issues arising from the proposed settlement, in their initial briefs on the proposed settlement.

PULP’s position was that environmental matters had not been adequately considered in the proceeding to comply with the provisions of the State Environmental Quality Review Act (SEQRA), but did not specify in what ways the proceeding had failed.

The initial briefs of SHAG referred to its comments (summarized above) on the EAF.

The City of Oswego challenged both the SBC and renewable energy projects proposed in the settlement as wasteful and the company’s proposed conservation land donations as illegal, and faulted the EAF for not dealing adequately with potential socio-economic impacts of power plant closures which might result from the sale of NMPC generating units.

The Cities of Fulton and Cohoes and the NYS Assessors Association adopted Oswego’s comments on the EAF by reference in its initial brief.

Empire State Development, while supporting the settlement, suggested that the Commission monitor the compliance of parties with provisions of the settlement which require good faith efforts to mitigate the effects of the MRA on steam hosts.

The National Association of Energy Services Companies (NAESCO) endorsed the settlement in general and specifically singled out and supported the proposed level of system benefit spending and provisions in the settlement by which NMPC commits to investigating the use of DSM and distributed generation to mitigate T&D related problems.

The Consumer Protection Board, while taking no position on the effects of divestiture on local community taxes and employment, did note that recent sale prices of generation assets in California indicated communities might see tax increases resulting from divestiture. In addition, it endorsed the establishment of an SBC at the level specified in the settlement and declined to take a position on the adequacy of the EAF.

Multiple Intervenors recapitulated in the brief the environmental positions it took in its comments on the supplemented EAF.

The Settling Independent Power Producers endorsed the settlement agreement and the MRA and opposed the positions of the City of Oswego and SHAG with regards to impacts of the settlement and the MRA. SIPP stated that they believed that the potential costs and disruption to industrial operations claimed by SHAG were exaggerated and could be mitigated by negotiations between SIPP and SHAG members without Commission involvement.

Niagara Mohawk stated in its brief that the supplemented EAF it had submitted had fully satisfied the requirements of SEQRA.

<u>Generic Comments on Utility EAFs</u>

On May 13, 1997, the Public Interest Intervenors (PII) moved for the Department of Public Service Staff to prepare supplemental environmental impact statements (SEISs) in several restructuring cases. At the time the petition was filed, Niagara Mohawk had not yet submitted an Environmental Assessment Form. In its petition, PII identified a number of claimed deficiencies in the EAFs which had been filed at that date. Some of PII's comments were generic in nature and, in our understanding, were intended to apply to all utilities; some were specific to particular utilities. Even though NMPC had not submitted an EAF at the time of the PII petition and even though PII did not comment on the NMPC EAF subsequently, Staff summarizes below generic points raised by PII in May which are generally relevant to the NMPC EAF.

- PII noted that the FGEIS considered using a system benefits charge (SBC)--which would pay for certain energy efficiency, low income and R&D activities not likely to be undertaken by a deregulated utility--as a means of mitigating some environmental impacts. It asserted that the Commission made a decision in Opinion No. 96-12 that the SBC should be funded at approximately the current levels of activity and that the SBC charge proposed in several of the plans it reviewed were below this threshold.

- While the system benefits charge is intended to provide for energy efficiency services (beyond those arising from market forces), it is anticipated that utilities will continue to offer some DSM services. PII asserts that some utilities' proposed DSM budgets will be lower than in previous years as a result of the restructuring plan and that will have negative environmental impacts.

- PII noted that although the proposed agreements provided for transition to market pricing of generation, T&D services would remain under a traditional form of regulation. PII argued that traditional regulation contains inherent incentives for a utility to increase sales and inflate rate base and that the Commission is therefore required to order an SEIS.

- Several settlements reviewed by PII include provision for a Competitive Transition Charge (CTC) which would allow the company to recover certain non-marginal costs of utility electric plants. PII argued that, by providing a mechanism for the recovery of these costs, the agreement would subsidize the operation of utility plants, giving the companies an unfair price advantage when bidding energy sales to an ISO and result in those plants operating more than is economically efficient. Environmental impacts would ensue if the utility plants were run in lieu of other plants which are both more economically efficient and more environmentally benign.

- PII noted that load pockets have been identified in several utilities' service territories and that construction of new transmission facilities may be required to mitigate these load pockets. PII asserted that these facilities will have environmental impacts which should be evaluated in an SEIS.

Chief Administrative Law Judge Lynch considered the PII petition and reply comments by Staff and several other parties and recommended that "the final EAFs prepared for Commission use in the Con Edison and O&R cases consider the potential environmental effects of T&D price cap regulation for Con Edison and the recovery of non-variable generation costs in T&D rates for Con Edison and O&R" but that "in all other respects, there is no reason to commence preparation of SEISs."[1] Nonetheless staff's analysis in Section V will address the issues raised by PII which are broadly relevant to NMPC.

We note that several of the environmental groups represented by PII are signatories to the NMPC settlement

[1] Cases 94-E-0952, et al., Ruling on the Motion for Supplemental Environmental Impact Statements, (issued June 19, 1997), p. 17.

agreement[1] and that neither PII nor any of its member environmental groups have commented on the NMPC EAF or raised environmental impact issues.

V. Staff Analysis

The FGEIS covered the significant generic issues connected with restructuring at considerable length. The following analysis will not recapitulate the material in the FGEIS. Instead, this analysis will deal with issues identified by Staff, by comments on the Niagara Mohawk EAF and with general comments offered by parties on other utility restructuring EAFs. The issues to be examined are primarily those for which it is reasonable to believe that unique features of the company's service territory or restructuring plan might result in environmental impacts not considered in the FGEIS or in excess of thresholds identified in the FGEIS.

A. Effects of Restructuring on Overall Level of Electric Sales in Niagara Mohawk's Service Territory

A key determinant of the incremental environmental impacts of restructuring the electric industry in New York is the effect of restructuring on the overall level of electric sales. This section of the EAF will address the question of whether any likely effect of the Niagara Mohawk restructuring plan would cause sales growth in excess of the levels contemplated in the Final Generic Environmental Impact Statement (FGEIS).

There appear to be three realistic ways in which restructuring could have significant impacts on electric sales: reduced rates and price elasticity; effects

[1] The following PII members are signatories to the settlement: NRDC, PACE, the Adirondack Council, New York Rivers United and the Association for Energy Affordability.

of rate of return regulation; and reduced use of energy efficiency. The following paragraphs examine each of these effects.

1. Price Elasticity Effects

If electric prices drop as a result of utility rate reductions incorporated in restructuring agreements and/or as a result of competition among the utility and alternative suppliers, customers may make the economic decision to consume more electricity. This is a price elasticity effect. The FGEIS analysis included the preparation of a statewide "high sales" scenario based on estimated sales increases that could result from decreases in electric prices, given the best information then available to staff economists. The high sales scenario assumed that the compounding statewide electric sales growth would be about 2.2% per year.

This scenario was compared to a FGEIS base case "evolving regulatory model" scenario. The base case assumed incremental sales growth of 1.2%. Thus, the additional incremental statewide sales growth likely to result from the high sales scenario compared to the no action base case was estimated as about 1.0% per year.[1]

PROMOD simulation of comparative plant dispatching under these scenarios showed that, compared to the evolving regulatory model, the high sales model would result in a 2.9% increase in SO_2 emissions, a 5.5% increase in NO_x and a 12% increase in CO_2 by 2012. The Commission determined that, although the FGEIS showed the possibility of detrimental incremental air quality impacts "consistent

[1] To provide a sense of scale, estimated NYPP sales for 1996 were about 144,500 GWH and NMPC sales were 37,355 GWH. Under the FGEIS comparative scenarios, a 1.0% per year incremental growth rate would result in additional statewide sales of about 1,445 GWH in 1997 due to price elasticity and additional NMPC sales of about 374 GWH.

with the social, economic and other considerations, from among the reasonable alternatives available," the Commission’s restructuring policy "avoids or minimizes adverse environmental impacts to the maximum extent possible."[1]

Niagara Mohawk accounted for roughly 26% of NYPP sales in 1996. In analyzing the significance of any potential incremental sales growth attributable to the Niagara Mohawk restructuring plan, it is reasonable to focus on Niagara Mohawk’s pro rata share of the sales growth and impacts considered in the FGEIS and ask whether Niagara Mohawk’s incremental sales growth due to price elasticity effects resulting from restructuring would be likely to be significantly greater than the average statewide incremental sales growth due to restructuring.

Recently, Staff of the Office of Energy Efficiency and Environment (OEEE), with the assistance of the Office of Regulatory Economics (ORE) of the DPS, performed an elasticity analysis using the rate reductions in the Niagara Mohawk settlement. The results (see Attachment A, Table B) show that the settlement rate reductions are likely to produce a 0.50% incremental annual increase in demand compared to the FGEIS base case over the same 15 year modeling period used in the FGEIS. This is only half the incremental sales increase modeled in the FGEIS high sales scenario.

It is important to note that this elasticity analysis estimates only the additional sales growth which would result from the rate reductions in the settlement agreement. It does not consider other important factors, such as population growth, general economic growth and the prices of competitive energy sources, which also help to

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[1] Cases 94-E-0952, et al., In the Matter of Competitive Opportunities Regarding Electric Service, Opinion and Order 96-12 (issued May 20, 1996), pg. 81.

determine overall sales growth, and so should not be interpreted as a sales forecast.

2. Regulation of the T&D Utility

While the proposed settlement provides for a transition to a more competitive market for generation, the T&D portion of Niagara Mohawk would remain a regulated utility with rate of return regulation. In its May 13, 1997 petition, PII argued that rate of return regulation gives the T&D utility incentives to promote sales and to build uneconomic rate base. According to PII, these incentives could result in environmental impacts which should be considered in a separate SEIS.

For several years, a revenue decoupling mechanism (NERAM) was in effect for NMPC which was intended to remove the linkage between increased sales and increased company profits. However, in 1995 the Commission approved the discontinuation of the general NERAM revenue reconciliation mechanism, but allowed continuation of a limited mechanism for recovery of lost revenues due to DSM. As discussed below, the company's expenditures on DSM declined sharply after 1995. It did not request recovery of DSM lost revenues after that date.

The Agreement proposes discontinuation of this DSM lost revenue recovery mechanism. Its discontinuation is unlikely to have a material effect on the company's already much reduced DSM programs or to act as an incentive to promote sales and to build an uneconomic rate base.

3. Lower Energy Efficiency Effect

For a number of years, the New York Commission has encouraged utilities to promote end use energy efficiency (DSM). This encouragement has included review and approval of utility DSM plans and budgets and various incentive and cost recovery mechanisms. For all New York utilities, including Niagara Mohawk, the levels of DSM expenditures and energy savings have declined drastically in recent years. Niagara Mohawk's DSM expenditures peaked at

$65.9 million in 1992 and its incremental annual DSM energy savings peaked at 324.6 GWH, also in 1992. By 1996, its DSM expenditures had declined to only $0.8 million and its DSM incremental energy savings goal had declined to only 29.9 GWH. While the company had budgeted $2.7 million for DSM in 1997, by mid-year it had only spent about $0.1 million. We estimate 1997 incremental DSM savings at about 6 GWH based on mid-year achievements. The company plans to continue to offer limited DSM programs to customers, but no specific sum is included in the settlement for these activities. As discussed below, money is allocated for a System Benefits Charge (SBC) which will include energy efficiency programs.

Staff examined the possibility that DSM budget reductions could reduce the energy conservation measures taken by NMPC customers and result in incremental increases in electric sales beyond the base case.

In the FGEIS, the base case "evolving regulatory model" scenario and the "high sales" scenario included annual incremental Niagara Mohawk DSM energy savings of 112 GWH[1] for the years 1997 and beyond. Another scenario in the FGEIS estimated the sales and environmental impacts of halting all DSM activities; the sales and environmental impacts of this "No incremental utility DSM" scenario were shown to be much smaller than those of the "high sales scenario."

The FGEIS did not consider a scenario that assumed both high sales and no incremental DSM, so Staff evaluated the plausibility that a realistic combination of low Niagara Mohawk DSM and high Niagara Mohawk sales growth could result in sales greater than those postulated in the FGEIS "high sales scenario." Staff has re-analyzed the impact of energy efficiency programs on NMPC sales growth using a value of 29.9 GWH for 1996, 6.0 GWH for 1997 and 0

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[1] The assumed level of DSM was equivalent to the company’s 1996 DSM goal. No provision was made in the base case for energy efficiency sales reductions resulting from programs funded by a system benefits charge.

GWH for the years 1998 through 2012 and compared that to the DSM impact analysis underlying the FGEIS high sales scenario. We calculate that, averaged over the FGEIS modeling period (1997 through 2012), the elimination of all energy efficiency sales reductions after 1997 would increase sales by only 0.13% a year.

This analysis probably overstates the effects of reductions in utility DSM programs on the availability of energy efficiency services for two reasons. First, as discussed below, the Agreement provides substantial funding for an SBC, much of which will be used to provide energy efficiency programs or information. Secondly, (as observed in the FGEIS) retail competition will result in the development of a competitive ESCO market in which some ESCO's will probably offer energy efficiency services as a way of distinguishing themselves from competitors.

As discussed above, the price elasticity effects of the settlement rate reductions would increase sales by an average rate of 0.50% a year over the 15 year period compared to the FGEIS base case. If the effects of no DSM are added, the likely incremental sales increases due to the settlement are about 0.63%. This is well below the 1.0% incremental growth considered in the FGEIS high sales scenario.

B. <u>System Benefits Charge</u>

The settlement provides for an SBC funded at a level of $15 million a year. The City of Oswego has objected to the establishment of an SBC as wasteful. However, in adopting the FGEIS, the Commission found that an SBC is necessary to mitigate the environmental effects of the reduction in utility DSM programs and provide for the continuation of other important public benefit programs.

In its May 13, 1997 comments, PII argued that restructuring agreements should provide for SBCs funded at the levels of utility DSM expenditures current when the Commission adopted the FGEIS. Staff believes that the proposed level of funding is compatible with the FGEIS and that no further analysis is required.

C. Effect of Restructuring on Retirement or Construction of New Generation, Plant Dispatch or Fuel Purchase

Another potential factor that could, in concept, affect New York's environment is the direct or indirect effect of the Niagara Mohawk restructuring plan on the mix of fuels burned or plants run to meet electric sales in Niagara Mohawk's territory. The following section will analyze whether there is any reason to believe that the Niagara Mohawk plan would result in impacts that are greater than or different in nature or causation from those already addressed in the FGEIS.

1. Construction of New Generating Plants

Projections in the FGEIS suggest that new capacity will be required on the New York State system within several years. This capacity might be provided by constructing new facilities, repowering existing plants, additional firm power imports or a combination of the above. It is also possible that some investors will find it attractive to construct new power plants (or refurbish existing less efficient plants) to compete as merchant plants in the new open power market being established by the Commission.

If new or repowered plants in excess of 80 MW, or significant transmission construction is required, those projects will be subject to full environmental review under Articles X and VII of the Public Service Law. In any event, under current air quality regulations (particularly the emissions offset policies for NO_x) construction of new facilities tends to improve air quality for critical emissions.

2. Transfer of Ownership of NMPC Non-Nuclear Generation

Under the Agreement, the company is required to auction its non-nuclear generation. The company has prepared an auction plan which will be the subject of a separate Commission proceeding. The potential environmental consequences of the auction are beyond the scope of this EAF. Staff will examine the auction plan and advise the Commission about whether a separate SEQRA analysis of the auction is required.

However, the City of Oswego and other parties have raised concerns about the possible effects of the settlement agreement on existing NMPC plants. It is possible to make some general observations about the possible environmental impacts of the divestiture of the company’s generation assets.

It is likely that the company’s lowest cost generating facilities will be acquired by another owner. These plants may be operated in much the same fashion by the new owners as they have been by NMPC. In general, the permitting and licensing restrictions and environmental standards which apply to these plants under Niagara Mohawk’s ownership will continue to apply. However, it is possible that competitive pressures will cause the new owners to seek to cut environmental expenditures in non-mandated areas. Such problems could be mitigated through specific agreements between NMPC and bidders if required by the auction plan.

The company estimates that most plant staff will be retained by new owners, but it is possible that transfer of these low operating cost plants would result in replacement of some existing NMPC employees or a reduction in work force.

The effect of divestiture on higher cost plants is more speculative. It is possible that new owners will acquire some or all of these less efficient plants and invest money to make them more competitive. Even plants with high operating costs may have significant advantages over "green field" sites in terms of existing transmission links and fuel access, as well as community acceptance and relative ease of environmental licensing. We note that

Niagara Mohawk is currently in the early stages of an Article X licensing proceeding for the repowering of its Albany Steam Station. This application is intended expressly to increase the value of that facility to prospective bidders.

The combination of incentives for prompt auctioning of these sites and the opportunity for NMPC to recover much of its stranded costs may mean that currently inefficient plants will be available at reasonable prices to developers. The result could be a willingness to invest in plant refurbishment to make them competitive in the market. The transfer of ownership from a regulated utility to an unregulated owner may also provide an opportunity for the new owner to negotiate lower property tax payments--further improving the plant's competitiveness.

3. <u>Retirement of NMPC Generating Facilities</u>

If no market for a given facility is revealed by the auction, retirement of that facility is a likely outcome. However, retirement of a major NMPC generating facility could have a variety of local fiscal, economic, employment and other environmental impacts. The City of Oswego cited concerns about the potential local impacts of retirement of the Oswego Steam Station.

The potential impact of early plant retirements was considered by the Commission in the FGEIS. The FGEIS concluded that accelerated retirement of less efficient plants is an unavoidable potential consequence of a more competitive electric industry. It further concluded that such changes could have significant adverse impacts on individuals and communities. Impacts discussed in the EAF included local economic impacts, decreased employment and reduced local tax revenues. While the EAF predicted that competition would lead to lower electric rates and an enhanced economy which would more than offset these impacts on a statewide basis, it stated that permanent displacement of some workers might result and that not all communities would share equally in the benefits of competition.

In Opinion No. 96-12, the Commission determined that "adverse environmental impacts will be avoided or minimized to the maximum extent practicable by incorporating as conditions to the decision those mitigative measures that were identified as practicable." One measure adopted by the Commission was a charge to Staff to monitor and, if indicated, mitigate specific impacts that may occur. The Settlement includes a commitment from the company to establish a $10 million fund which will be used for programs such as retraining, outplacement and early retirement of its employees to mitigate any employment impacts caused by the auction or retirement of its generating plants.

The potential impacts on the City of Oswego, and other communities potentially affected, fall within the range considered in the FGEIS and no further analysis is required in this proceeding.

4. Effect of Competitive Transition Charge (CTC) on Plant Dispatch

The proposed Settlement includes a provision which will allow the company to partially recover its above-market generation costs through a non-avoidable CTC charge. In its motion filed on May 13, 1997 in Case 96-E-0952, PII contended that since potential competitors will not receive a similar income stream, companies receiving a CTC would offer generation to the ISO at a subsidized and uneconomic price. This, PII asserted, could result in a company operating less efficient and dirtier plants than the competitive plants which would have operated in the absence of the CTC.

However, under the provisions of the proposed settlement, collection of NMPC’s stranded costs is not dependent on operating a Niagara Mohawk plant (i.e., is not marginal revenue). Both Niagara Mohawk and any competitors would face the same short term decision criterion. They would maximize profits (or minimize losses) on existing facilities by selling on the market whenever the clearing price equals or exceeds their marginal operating costs--as they themselves calculate marginal costs given their best information.

While not addressed in any filed comments, some parties in public hearings have objected to the collection of the CTC from customers who choose to install solar panels or other renewable technologies to supply their power but remain connected with the company for back-up. They contend that, by increasing their costs, the CTC slows the development of renewable energy and increases environmental impacts. It appears to Staff that even-handed application of the CTC merely puts all power sources on an even footing. Since the CTC costs avoided by installers of renewable equipment would be ultimately born by other ratepayers or company stockholders, special exemptions from the CTC would constitute an indirect and uneconomic subsidy. If subsidies for renewables are in the public interest, they can be provided directly through the SBC or through legislative action.

4. Fuel Burned by Niagara Mohawk

Various Niagara Mohawk units have the capacity to burn either coal, oil or gas within existing air quality limits. Decisions about which fuel to burn at these facilities will continue to be based on economic considerations and unrelated to restructuring regardless of ownership.

D. Effects of the MRA

For a number of years the company has been locked into "must run" contracts requiring it to purchase power, whenever offered, at above-market prices. Most of these plants are either small hydro-electric facilities or modern gas-fired cogenerators. In July of 1997, the company reached a Master Restructuring Agreement with 29 IPPs representing 80% of the company’s above-market costs. Under the MRA, the settling IPPs agreed to "restructure, amend or replace" their current contracts in return for payments from NMPC, purchase by NMPC or other contract modifications.

1. Potential Air Quality Impacts of Changes in IPP Contracts

It is not feasible to predict how the operation of each of these plants will be changed by the MRA. However, in general, the MRA could impact the operation of the settling IPP plants through changes in the dispatch of the IPPs and changes in steam sales to steam hosts. According to NMPC estimates, at most about 15% of the total IPP steam production would be retired or moth balled due to the MRA. The remainder will continue operating but will either enter into bi-lateral contracts or bid into the market on a basis that reflects true marginal costs.

The FGEIS examined the possibility that all the "must run" IPP contracts in New York State would be renegotiated so that these plants would be economically dispatched. The model used for the FGEIS showed that economic dispatch of IPPs would result in increased SO_2 emissions and decreased NO_x and CO_2 emissions, relative to the base case, during most of the study period. However, during the later years of the period, economic dispatch of IPPs would result in lower SO_2 emissions.

In Opinion No. 96-12, which adopted the FGEIS, the Commission observed that the analysis of retail market structures (which included consideration of economic dispatch of IPPs) forecast that competition would result in greater air quality impacts then the no action alternative, but that moving towards competition was still desirable when these effects were balanced against the likely economic benefits of the policy.

The proposed MRA would have smaller effects than those reported in the FGEIS since the FGEIS assumed that all the IPPs in the state with "must run" contracts would be economically dispatched, while the MRA affects only some of the IPPs having contracts with NMPC. It should be noted that, although there is likely to be a temporary increase in SO_2 emissions resulting from the MRA, NMPC has agreed to permanently donate 5,000 SO_2 allowances to the Adirondack Council for retirement.

Many of the IPP units affected by the MRA have steam hosts which currently purchase byproduct steam or hot water from generating activities. To the extent that IPPs are retired or mothballed, the steam hosts may have to build new auxiliary boilers or refurbish retired boilers. Niagara Mohawk, in its EAF, estimates that the steam host steam requirements directly affected by retirement of settling IPPs would represent only about 0.8% of total IPP steam production. In addition, it is possible that changes in the operation of an IPP[1] due to renegotiation of contracts with NMPC could result in a higher steam price or limited steam availability and thus cause increased operation of auxiliary boilers. These single purpose boilers could be less efficient and somewhat more polluting than the cogeneration units they replace.

In general, we would assume that the indirect air quality impacts of increased operation of new or existing auxiliary steam host boilers would have only marginal air quality impacts since most steam hosts currently served by an adjacent gas fired IPP would probably have relatively easy physical access to clean burning natural gas to feed their own boilers[2] and since the amount of steam involved is relatively low in the context of this assessment.

2. Potential Socio-economic Impacts of Interruption of Steam Supply to Steam Hosts

As noted above, it is possible that the MRA, which modifies or terminates contracts between NMPC and a number of IPPs, may affect the price or availability of steam or hot water currently provided by these IPPs to industrial steam hosts.

[1] For example, if a cogenerator which formerly ran around the clock under a "must run" contract, moved to a more limited or irregular operating regime under economic dispatch.

[2] The possible economic and employment impacts of changes or discontinuation of IPP steam sales to steam hosts will be discussed in another section of this EAF.

This could have a variety of impacts on the costs or operations of the steam hosts. For example:

- steam prices charged to the steam hosts could rise because of changes in the cogenerators' revenue structure;

- steam hosts may have to change production schedules because cogenerators operate less frequently or less regularly;

- steam may no longer be available from cogenerators who cease operation;

- the installation or refurbishment of auxiliary boilers to replace cogenerated steam may result in higher capital and operating costs or in disruption of steam host operations during the period of permitting and construction.

Such changes could have short term effects on profits, worker incomes, employment and local economies if, for example, production curtailments and layoffs or reduced shifts were required during a transition period. Long term local socio-economic impacts might result if the steam host saw a major permanent change in its capital or operating costs which made it less competitive in the market.

These adverse local socio-economic impacts would be balanced by positive socio-economic impacts on a larger scale. In many cases, IPPs sought out steam hosts primarily to become "qualifying facilities" (QFs) under the Public Utilities Regulatory Policy Act of 1978 (PURPA) and thus eligible for legislatively mandated above-market price must-run contracts with Niagara Mohawk. As a result of the MRA, these plants will be dispatched economically based on their marginal costs. The resulting improvement in economic efficiency will lower costs and benefit ratepayers and the state's economy.

This is not to say that the local economic disruption which might be caused by the MRA is inconsequential. However, it is likely that such impacts can be adequately mitigated. We note that the parties to the settlement have committed (section 13.8) to "pursue diligently ways to minimize any economic or operational difficulties due to changes in IPP steam production which could occur as a result of the MRA..."

E. Effect of Restructuring Plan on Construction of New Transmission Facilities

In its EAF, Niagara Mohawk states that no new transmission facilities are required to implement the October 10 agreement. It is possible, however, that load pockets could occur within the franchise in certain combinations of load and weather.

Load pockets are of potential concern in a competitive environment because the owner of facilities in the load pocket could exercise market power during load pocket conditions unless there were sufficient competing generation sources within the load pocket. In many areas of the NMPC franchise there is a mix of generating facilities owned by NMPC and IPPs. Where this diversity of ownership occurs, the exercise of market power is less likely to occur. However, ownership of NMPC facilities is likely to change within the next few years because NMPC has committed to auctioning its non-nuclear generation. Conceivably the ownership of generation could become more dispersed in some areas (lessening market power concerns) and more concentrated in other regions (increasing the potential market power of owners).

Additional transmission could be constructed by the regulated T&D utility to prevent the exercise of market power. The construction of new transmission facilities can be anticipated to have a variety of environmental impacts. These were discussed generically in the FGEIS. However, any construction of significant new transmission would require environmental review and approval by the Public Service Commission under Article VII of the Public Service Law. Under this law the Commission is obligated to weigh the costs and benefits of the transmission addition and to consider alternatives.

In many situations, the Commission could take other steps to relieve or prevent market power which would not have incremental environmental impacts. For example, it could impose requirements on Niagara Mohawk’s auction process which would limit the amount of generation any one bidder could buy in a potential load pocket, or could require purchasers to enter into special contracts with the T&D utility which would limit or index prices which could be charged during load pocket conditions. In some situations the Commission might encourage T&D utilities to offer targeted DSM programs to prevent the exercise of market power. In Section 7.2(1) of the settlement, the company committed itself to evaluate and implement cost effective alternatives to major T&D projects including DSM and distributed generation.

F. Miscellaneous Environmental Issues

1. Remediation of Coal Gas Sites

For several years the company has been conducting a site remediation program designed primarily to clean up environmental damage at old coal gas sites which the company had acquired during its consolidation. Section 2.6.5.2 of the settlement commits the company to continue this effort. No incremental environmental impacts are anticipated.

2. Environmentally Significant Lands Owned By Niagara Mohawk

The company currently owns extensive undeveloped land associated primarily with its hydro facilities. Some portions of this land have considerable ecological or scenic value. Divestiture of these hydro facilities could result in the development of these lands and the loss of their ecological values. However, in sections 7.2 (iv through x) the company commits to donate or sell conservation and development right easements to the State of New York for these critical parcels. No incremental negative environmental impacts are anticipated.

3. Environmental Disclosure

Various parties suggested that some customers in a competitive power market may wish to consider environmental values in their power purchase decisions. In the absence of reliable and consistently presented information on the generation sources used by suppliers, customers may be unable to make informed decisions based on environmental as well as economic considerations. A well defined environmental disclosure program would encourage the use of environmentally responsible generation sources.

Section 7.2 (xvi) of the settlement states that the company and Staff have agreed to " ... work with load serving entities and others to develop and implement, where feasible, meaningful and cost effective, an approach to providing customers with fuel mix and emission characteristics of the generation sources relied upon by the load serving entity."

VI. Mitigation of Impacts -- Monitoring

It is important to note that the FGEIS explicitly recognized that "the likely environmental effects of a shift to a more competitive market for electricity are not fully predictable[1] due to the absence of precedence, complexity of the New York electric industry, future regulatory activities, including those of other states and the federal government, and the nature and degree of market response. The same uncertainty persists with respect to Niagara Mohawk's restructuring plan.

In Opinion 96-12 (Opinion and Order Regarding Competitive Opportunities for Electric Service), the Commission made certain "findings" pursuant to the State Environmental Quality Review Act. The Commission determined that "...adverse environmental impacts will be avoided or minimized to the maximum extent practicable by incorporating as conditions to the decision those mitigative measures that were identified as practicable;... These mitigation measures are: (1) monitoring environmental impacts; (2) system benefits charge; and (3) assisting efforts undertaken by other agencies to address interstate pollution transport."

Staff analysis of the Niagara Mohawk restructuring plan shows that its implementation would result in environmental effects which would most likely be less than the impact values assessed in the FGEIS. To address any uncertainty and to

[1] FGEIS, p. 77.

evaluate unknown outcomes, a monitoring program, as envisioned in the FGEIS should be developed.

Environmental impacts which could be monitored are described in Section 6.2.3 of the Final Generic Environmental Impact Statement (FGEIS) issued May 3, 1996 in Case 94-E-0952 (Competitive Opportunities Regarding Electric Service). In addition, this EAF discuss a number of activities and environmental changes that would be important to monitor during the transition to competition. Examples of environmental issues that could require monitoring include:

- imported electricity from the midwest,
- SO_2 and NO_x emissions,
- retirement of Niagara Mohawk power plants,
- in-state and out-of-state purchased generation,
- fuel mixture of generation,
- reduction in environmental RD&D,
- loss of environmentally significant land,
- new electric and gas transmission line construction,
- acid precipitation in the Adirondacks and Catskills, and
- mitigation of load pockets.

The proposed environmental monitoring plan currently being developed by Staff will be organized around the major environmental impacts considered in the FGEIS and this EAF, including information necessary for analysis of any restructuring environmental impacts, confirmation of expected impacts and exposition of unexpected outcomes and their significance. Staff anticipates Niagara Mohawk's cooperation in the development and implementation of this monitoring plan.

VII. Conclusions

We have considered the proposed October 10 settlement agreement and have analyzed the potential impacts of that agreement on the environment. We have compared these likely impacts to those addressed in the FGEIS. Our analysis has been broadly framed and has looked at limiting cases in order to encompass any modifications to that agreement likely to be adopted by the Commission. In our analysis we have also considered issues raised by other parties commenting on the Niagara Mohawk EAF.

We conclude that the Niagara Mohawk restructuring plan would not result in significant new environmental impacts not considered in the FGEIS, nor would it result in impacts likely to be greater than those considered in the FGEIS. Therefore no SEIS is required under the provisions of SEQRA. Staff recommends that the Commission determine that no further SEQRA compliance is required with regard to the transitional restructuring plan for this company.

Although no further SEQRA compliance is required before Commission action on the NMPC restructuring agreement, the Commission should institute mechanisms for monitoring and, if indicated, mitigating some of the potential impacts of restructuring. Staff is developing a proposed monitoring plan for the Commission’s consideration.

In the future, the Commission will be asked to act on NMPC’s detailed auction plan. Staff is considering the potential impacts of the auction plan and will advise the Commission on the possible need for an EAF on that action.

APPENDIX
IMPACT OF POSSIBLE RATE DECREASES ON SALES GROWTH

Several of the potential impacts of deregulation examined in the Final Generic Environmental Impact Statement (FGEIS) are a result of the increased sales that are expected to accompany deregulation. Rate reductions, which are a primary driver of the increased sales, are not considered explicitly in the FGEIS; rather it was assumed that, beginning in 1997, sales would increase by an additional 1% per year for 15 years. That is, if statewide growth without deregulation is 1.2% per year (as was assumed in the FGEIS evolving regulatory model), growth with deregulation would be 2.2%.

In each of the restructuring cases, specific rate reductions are now being considered. Using price elasticity of demand, these proposed rate reductions now permit the calculation of an estimate of increased sales to be expected from restructuring.

The following tables (developed by the Office of Energy Efficiency and Environment with the assistance of the Office of Regulatory Economics) consider both short-run elasticity (the increase in sales which occurs immediately after the rate reduction) and long-run elasticity (increases which occur in subsequent years). No other growth inducing factors are included, so the analysis only reflects the incremental impact of rate changes. The first step in the calculation (Table F) is to determine the weighted average elasticities based on the elasticities for each sector (industrial, commercial and residential) and the fraction of the utility’ load in each sector (sales weight). Also, the average price reduction per year is calculated based on the expected rate decrease for each sector and the sales weight.

Five price reduction scenarios (A through E) are considered. Scenario B is based on the price reductions from the Agreement and is the scenario used in the EAF. Other scenarios explore alternative hypothetical rate reductions.

Tables A through E then calculate the year by year increase in sales due to competition (short-run, long-run and total), the cumulative change in sales, and the annual average rate of sales growth. Residential Delta (Res Delta) is the possible residential rate reduction considered in the table; Percent Total Impact per Year (%TI/Yr) is the average price reduction per year from Table F. The end of the five year settlement period and the end of the 15 year modeling period are highlighted.

NIAGARA MOHAWK PRICE ELASTICITY IMPACT

Sales ch = (price elasticity * % price ch) + lambda * (sales ch lag 1)

A.

%Res Delta	%Tl/ Yr	Lambda	SR Elas	LR Elas
1.0	1.35	0.71	0.33	1.14

Year	SR Sales	LR Sales	Total	Cumu-lative	Annual Rate
1998	0.439	0.000	0.439	0.439	0.44
1999	0.439	0.313	0.752	1.191	0.59
2000	0.439	0.537	0.976	2.167	0.72
2001	0.000	0.697	0.697	2.865	0.71
2002	**0.000**	**0.498**	**0.498**	**3.363**	**0.66**
2003	0.000	0.356	0.356	3.718	0.61
2004	0.000	0.254	0.254	3.973	0.56
2005	0.000	0.182	0.182	4.154	0.51
2006	0.000	0.130	0.130	4.284	0.47
2007	0.000	0.093	0.093	4.376	0.43
2008	0.000	0.066	0.066	4.442	0.40
2009	0.000	0.047	0.047	4.490	0.37
2010	0.000	0.034	0.034	4.523	0.34
2011	0.000	0.024	0.024	4.548	0.32
2012	**0.000**	**0.017**	**0.017**	**4.565**	**0.30**

B.

%Res Delta	%Tl/ Yr	Lambda	SR Elas	LR Elas
3.2	2.31	0.71	0.33	1.14

Year	SR Sales	LR Sales	Total	Cumu-lative	Annual Rate
1998	0.751	0.000	0.751	0.751	0.75
1999	0.751	0.536	1.287	2.037	1.01
2000	0.751	0.919	1.670	3.707	1.22
2001	0.000	1.193	1.193	4.899	1.20
2002	**0.000**	**0.852**	**0.852**	**5.751**	**1.12**
2003	0.000	0.608	0.608	6.360	1.03
2004	0.000	0.435	0.435	6.794	0.94
2005	0.000	0.310	0.310	7.105	0.86
2006	0.000	0.222	0.222	7.326	0.79
2007	0.000	0.158	0.158	7.485	0.72
2008	0.000	0.113	0.113	7.598	0.67
2009	0.000	0.081	0.081	7.679	0.62
2010	0.000	0.058	0.058	7.736	0.57
2011	0.000	0.041	0.041	7.778	0.54
2012	**0.000**	**0.029**	**0.029**	**7.807**	**0.50**

NIAGARA MOHAWK

Sales ch = (price elasticity * % price ch) + lambda * (sales ch lag 1)

C.

%Res Delta	%Tl/ Yr	Lambda	SR Elas	LR Elas
5.0	2.73	0.71	0.33	1.14

Year	SR Sales	LR Sales	Total	Cumu-lative	Rate
1998	0.887	0.000	0.887	0.887	0.89
1999	0.887	0.633	1.520	2.407	1.20
2000	0.887	1.086	1.973	4.380	1.44
2001	0.000	1.409	1.409	5.789	1.42
2002	**0.000**	**1.006**	**1.006**	**6.795**	**1.32**
2003	0.000	0.719	0.719	7.514	1.21
2004	0.000	0.514	0.514	8.028	1.11
2005	0.000	0.367	0.367	8.394	1.01
2006	0.000	0.262	0.262	8.656	0.93
2007	0.000	0.187	0.187	8.844	0.85
2008	0.000	0.134	0.134	8.977	0.78
2009	0.000	0.095	0.095	9.073	0.73
2010	0.000	0.068	0.068	9.141	0.68
2011	0.000	0.049	0.049	9.190	0.63
2012	**0.000**	**0.035**	**0.035**	**9.224**	**0.59**

D.

%Res Delta	%Tl/ Yr	Lambda	SR Elas	LR Elas
7.0	3.64	0.71	0.33	1.14

Year	SR Sales	LR Sales	Total	Cumu-lative	Annual Rate
1998	1.185	0.000	1.185	1.185	1.18
1999	1.185	0.846	2.031	3.215	1.59
2000	1.185	1.451	2.635	5.850	1.91
2001	0.000	1.882	1.882	7.733	1.88
2002	**0.000**	**1.344**	**1.344**	**9.077**	**1.75**
2003	0.000	0.960	0.960	10.037	1.61
2004	0.000	0.686	0.686	10.723	1.47
2005	0.000	0.490	0.490	11.213	1.34
2006	0.000	0.350	0.350	11.563	1.22
2007	0.000	0.250	0.250	11.813	1.12
2008	0.000	0.179	0.179	11.992	1.03
2009	0.000	0.128	0.128	12.119	0.96
2010	0.000	0.091	0.091	12.210	0.89
2011	0.000	0.065	0.065	12.275	0.83
2012	**0.000**	**0.046**	**0.046**	**12.322**	**0.78**

NIAGARA MOHAWK

Sales ch = (price elasticity * % price ch) + lambda * (sales ch lag 1)

E.	%Res Delta	%Tl/ Yr	Lambda	SR Elas	LR Elas
	9.0	4.55	0.71	0.33	1.14

Year	SR Sales	LR Sales	Total	Cumu-lative	Annual Rate
1998	1.477	0.000	1.477	1.477	1.48
1999	1.477	1.055	2.532	4.010	1.99
2000	1.477	1.809	3.286	7.296	2.37
2001	0.000	2.347	2.347	9.643	2.33
2002	**0.000**	**1.677**	**1.677**	**11.319**	**2.17**
2003	0.000	1.198	1.198	12.517	1.98
2004	0.000	0.855	0.855	13.372	1.81
2005	0.000	0.611	0.611	13.983	1.65
2006	0.000	0.436	0.436	14.419	1.51
2007	0.000	0.312	0.312	14.731	1.38
2008	0.000	0.223	0.223	14.954	1.27
2009	0.000	0.159	0.159	15.113	1.18
2010	0.000	0.114	0.114	15.226	1.10
2011	0.000	0.081	0.081	15.308	1.02
2012	**0.000**	**0.058**	**0.058**	**15.366**	**0.96**

F.	LARGE IND	SMALL IND/COM	RES/ OTHER	WGTED AVG	PRICE PER YR
Sales Weight	0.31	0.32	0.37		
SR Price Elas.	0.43	0.31	0.25	0.33	
LR Price Elas.	1.28	1.17	0.99	1.14	
Price Red. A	10.00	2.00	1.00	4.11	1.35
Price Red. B	13.31	5.56	3.22	7.10	2.31
Price Red. C	15.00	6.00	5.00	8.42	2.73
Price Red. D	20.00	8.00	7.00	11.35	3.64
Price Red. E	25.00	10.00	9.00	14.28	4.55

Lambda (1- SR Elas/LR Elas): 0.71