STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 07-S-1315 – Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service.

STATEMENT OF THE NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE STAFF IN SUPPORT OF THE JOINT PROPOSAL

DAKIN D. LECAKES
Assistant Counsel
Department of Public Service
Three Empire State Plaza
Albany, New York 12223
(518) 474-4536

Dated: June 26, 2008
Albany, New York

TABLE OF CONTENTS

INTRODUCTION 1

OVERVIEW OF THE JOINT PROPOSAL 2

COMPLIANCE WITH THE COMMISSION'S SETTLEMENT GUIDELINES 4
THE JOINT PROPOSAL IS IN THE PUBLIC INTEREST 6

A. Term of the Rate Plan 6

B. Rate and Economic Provisions 6
1. Base Rates 6
2. Cost of Capital 8
3. Return on Equity 8
4. Earnings Sharing Mechanism 9
5. Reconciliations 10
6. Property Taxes 11
7. Interference 11
8. Production Plant Expenditures 12
9. Pension and OPEB Expenses 13
10. Environmental Remediation 13
11. Steam Incident Action Plan Reconciliation 13
12. Additional Reconciliation Provisions 14
13. Limitations on Deferrals 14
14. Depreciation and Reserves 15
15. Interest on Deferred Costs 15
16. Allocations of Common Costs 15

C. Other Revenue Requirement and Rate Issues 15
1. Steam Sales 15
2. East River Repowering Project 16
3. Fuel Adjustment Clause 17
4. ECOS and Rate Design 17
5. Demand Rates 18

D. Non-Rate and Other Issues 18
1. Steam Business Development 19
2. Thermal Efficiency/Losses 19
3. Steam Resource Plan 19
4. Energy Efficiency 20
5. Safety Performance Measures 20

CONCLUSION 21

APPENDIX A

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 07-S-1315 – Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service.

STATEMENT OF THE STAFF OF THE NEW YORK STATE DEPARTMENT OF PUBLIC SERVICE IN SUPPORT OF THE JOINT PROPOSAL

INTRODUCTION

Consolidated Edison Company of New York, Inc. (Con Edison or the Company) is operating its steam business pursuant to a rate plan approved by the Commission in 2006 that expires on September 30, 2008.[1] On November 2, 2007, Con Edison filed proposed tariff leaves that would take effect December 2, 2007, and testimony and exhibits supporting the modifications set forth in those proposed tariff leaves (the Steam Rate Filing). By Orders dated November 8, 2007, and February 15, 2008, the Commission suspended the effective date of Con Edison's proposed tariff leaves to October 1, 2008.

On February 29, 2008, Department of Public Service Staff (Staff) and other intervening parties filed testimony in response to the Steam Rate Filing. On March 17, 2008, Con Edison and some intervening parties filed rebuttal testimony. On April 7, 2008, evidentiary hearings were commenced, ending on April 10, 2008.

On April 11, 2008, as required by 16 NYCRR §3.9(a), Con Edison submitted to the Secretary a Notice of Impending Settlement Negotiations. Thereafter, settlement discussions were conducted both in person and by phone over the next two months, resulting in a Joint Proposal. On June 16, 2008, Staff, on behalf of all settling parties, filed the Joint Proposal with the Secretary.

---

[1] Case 05-S-1376, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service, Order Determining Revenue Requirement and rate Design (issued September 22, 2006) (2006 Rate Order).

As of June 26, 2006, the signatories to the Joint Proposal are Con Edison, Staff, the City of New York (NYC), Consumer Power Advocates, and New York Energy Consumers Council, Inc. The provisions of the Joint Proposal, if approved or adopted by the Commission, will take effect October 1, 2008.

This Statement in Support represents the basis and rationale for Staff's agreement with the Joint Proposal and recommendation to the Commission that it approve or adopt the Joint Proposal's terms and conditions. Staff will be available at a July 2008 hearing to respond to questions by the Administrative Law Judge (ALJ) and other parties on the Joint Proposal and this Statement.

OVERVIEW OF THE JOINT PROPOSAL

The Joint Proposal recommends a two-year rate plan that runs from October 1, 2008 to September 30, 2010. The Joint Proposal includes increases to the Company's base delivery service rates designed to produce an additional $53.0 million in revenues on an annual basis in RY1 (12 months ended September 30, 2009) and an additional $24.7 million in revenues on an annual basis in RY2(12 months ended September 30, 2010). To mitigate the impact of the RY1 increase on customers, the Joint Proposal recommends that these two base rate increases be implemented on a levelized basis. The levelized annual rate increases would be $43.7 million in revenues on an annual basis in RY1 and an additional $43.7 million in revenues on an annual basis in RY2.

Phasing-in the RY1 increase over two years produces higher base revenues for the Company at the end of RY2 of approximately $9.6 million than if the revenues were not phased in. However, the one-time credit to customers in Rate Years 1 and 2 representing the proceeds from the sale of the First Avenue Properties will be fully utilized and will create a revenue shortfall of approximately $12.8 million at the end of RY2.

The Joint Proposal's revenue requirement reflects a 7.50% overall cost of capital, including a 48.0% equity ratio and an authorized return on equity (ROE) of 9.3% (Joint Proposal, Page 4 of 5, Appendix A). If the return on equity ("ROE") in any rate year exceeds 10.1 percent, the earnings above the threshold would be shared equally by customers and the Company. The

Joint Proposal prescribes in detail how the ROE would be calculated for purposes of the sharing mechanism.

The revenue allocation agreed to in the Joint Proposal reflects, among other things, a phase-in of the revenue surpluses and deficiencies as identified in the Company's embedded cost of service ("ECOS") Study submitted in this proceeding. The Joint Proposals eliminates 50 percent of the deficiencies and surpluses in RY1 and the remaining 50 percent of the deficiencies and surpluses in RY2.

The Joint Proposal provides for increases in the customer charge and re-designed usage rates for SC 2 Rate II demand rate customers on a revenue neutral basis, which reflect a declining block rate structure.

Additionally, the Joint Proposal continues to move Con Edison's steam customer base to demand billing. The Company implemented demand billing commencing November 1, 2007, for SC 2 and SC 3 customers with usage equal to or greater than 22,000 Mlbs. As part of this Joint Proposal, the Company will provide demand meters to customers with usage greater than 14,000 Mlbs but less than 22,000 Mlbs. Thereafter, Con Edison will study the impacts of demand billing on customers using greater than 22,000 Mlbs and the potential impact of demand billing on customers above 14,000 Mlbs but less than 22,000 Mlbs, for the 2008-2009 winter period. The Company will hold a technical conference in July 2009 to present the results of the study and to provide sample winter demand rates that the Company is planning to use to sample-bill customers in the 14,000 Mlbs to 22,000 Mlbs category during the 2009-2010 winter period. The Company will implement demand billing for these customers in the 2010-2011 winter period.

Variations between the actual cost of fuel and the base cost of fuel will continue to be recovered through the Fuel Adjustment Clause ("FAC"), including continuation of the annual reconciliation of the steam fuel expenses and revenues. The Company will also continue to recover through the FAC its fuel costs associated with the steam system variance, subject to the existing incentive mechanism, to the extent such costs are not recovered in base rates. In addition all costs associated with oil storage and handling, including Company labor, will continue to be recovered through the FAC. As part of its next steam rate filing, however, Con Edison is to propose recovery of all Company labor costs currently recovered through the FAC

in base rates, as well as certain other oil storage and handling costs to be decided through discussions with Staff during the term of the rate plan reflected in the Joint Proposal.

The Company's rates will continue to reflect the current allocation of the costs of the East River Repowering Project ("ERRP") between Electric and Steam. During RY1, the Company, with input from Staff and other interested parties, will perform a detailed study on the allocation of the costs of ERRP and will file the study with the Commission on or before April 30, 2009. Staff expects that the study results will inform the record sufficiently to allow Con Edison, Staff, or any other party to recommend changes to the allocation of ERRP costs through the Company's next general steam base rate filing.

The Joint Proposal continues performance metrics for steam business development efforts that are intended to promote growth in Con Edison's steam business. Additionally, the Joint Proposal contains for the first time, a Safety Performance Metric that is intended to prescribe minimum standards for Company response to steam vapor and leak conditions, as well as provide a mechanism for instituting performance metrics for reducing Con Edison's backlog of unrepaired steam leaks.

The Joint Proposal should be read and considered in its entirety and arguments against any specific provision should not be considered outside of the context of the whole agreement. Staff recommends that the Joint Proposal be approved or adopted as proposed because it represents a fair balancing of customer and shareholder interests, as evidenced by the large number of signatories.

COMPLIANCE WITH THE COMMISSION'S SETTLEMENT GUIDELINES

In Opinion No. 92-2, the Commission identified the criteria for judging whether a joint proposal is in the public interest.[2] The Commission explained that in considering a joint proposal it reviews the extent to which that proposal is supported by generally adverse parties, and it also determines whether the record for the decision to adopt a joint proposal is adequate. To be approved, a joint proposal should be consistent with law and public policy, have a rational basis, balance the interests of customers and shareholders, and compare favorably with the

[2] Case 90-M-0255, Proceeding on Settlement Procedures and Guidelines, Opinion No. 92-2 (issued March 24, 1992).

probable outcome of litigation. The Joint Proposal here satisfies these criteria and should, therefore, be adopted.

All parties to this proceeding received reasonable and sufficient notice of settlement negotiations as required by 16 NYCRR §3.9(a). Con Edison and/or Staff routinely circulated e-mails to all active parties advising them of upcoming dates for negotiating sessions. Moreover, telephone conferencing was made available to all parties for every negotiating session. No interested party was denied an opportunity to participate in the negotiations, and many parties participated during every single negotiating session.

The settlement negotiations resulted in a Joint Proposal that has received broad support among the active parties to this proceeding. In addition to Staff and Con Edison, other signatories to the Joint Proposal include NYC and a number of consumer groups and advocates. Although some parties may oppose discrete provisions of the Joint Proposal, Staff believes that the Joint Proposal must be considered as a whole as the product of fair and balanced negotiation. When considered in its proper context, it is clear that the Joint Proposal protects customers, is fair to shareholders, promotes the objective of ensuring the future viability of Con Edison's steam business, and that its provisions are reasonable relative to the possible outcome of this case had it been fully litigated.

Additionally, the record is adequate to justify adoption of the Joint Proposal. The testimony and exhibits filed by Con Edison, Staff, and the other active parties provide and explain the rationale and basis for many of elements of the Joint Proposal.[3] Additionally, a review of rebuttal testimony submitted by some of the parties shows the wide range of disputed issues that have been brought to balance in the Joint Proposal. That testimony and the exhibits thereto, combined with the hearing transcripts from the evidentiary hearings conducted in April 2008, provide ample support for the provisions contained in the Joint Proposal. Moreover, Staff expects there to be further support provided at the hearing to be conducted in July 2008.

The Commission's remaining criteria for judging whether a joint proposal is reasonable is determining whether the terms in such proposal are in the public interest. For the reasons discussed below, the Joint Proposal offered here meets that standard.

---

[3] Staff incorporates by reference in this Statement its pre-filed testimony, as identified in Appendix A.

THE JOINT PROPOSAL IS IN THE PUBLIC INTEREST

The terms of the Joint Proposal are in the public interest. In considering the provisions below, Staff notes that some provisions may seem to appear to favor one or another party. Such a view of individual elements is inappropriate and should be tempered by the fact that the Joint Proposal is intended to be considered as a whole, with each individual section providing support to the others.

In executing and submitting the Joint Proposal to the Commission, Staff is aware that such Proposal is only a series of recommendations to the Commission and is not a contract.[4] The Commission may accept, reject, or modify, in whole or in part, any recommendation contained therein. Moreover, such adoption of any of the terms of the Joint Proposal do not create a contract between the Commission and Con Edison or any other signatory party, but only represents the Commission's execution of its statutory responsibility and duty to determine the rates and rules applicable to Con Edison's steam business for the duration of the rate plan. Any belief that the Joint Proposal is a binding agreement on the Commission or that it gives rise to contractual claims against the Commission is erroneous as a matter of law.[5]

A. Term of the Rate Plan

The rate plan contained in the Joint Proposal covers two years with each rate year comprising a 12-month period. Thus, RY1 is the period October 1, 2008 to September 30, 2009, and RY2 is the period October 1, 2009 to September 30, 2010. Although Staff's testimony in this case advocated for a one-year rate plan, the benefits to customers that could be achieved in a negotiated rate plan led Staff to agree to a two-year proposal.

B. Rate and Economic Provisions

1. Base Rates

The Joint Proposal adopts revenue increases of $53.0 million in Rate Year 1(Joint Proposal, Appendix A, page 1) and $24.7 million in Rate year 2 (Joint Proposal, Appendix A, page 2). However, in order to mitigate the customer impact associated with the increase in rate

---

[4] MCI Telecommunications Corp. v. Public Serv. Comm'n, 231 A.D.2d 284, 291 (3d Dep't 1997).

[5] *See, e.g.*, United Water New York, Inc. v. Public Serv. Comm'n, 252 A.D.2d 810, 811 (3d Dep't 1988).

Year 1, the revenue increase is phased in over the two year term of the rate plan, in each of the two years (Joint Proposal, Appendix A, page 5). The annual rate allowances for the Company's Pensions and Other Post Retirement Employment Benefits ("OPEB") were adjusted to bring the calculated revenue requirement in line with the phased-in revenue requirement. The overall bill impact of the levelized base rate increase equates to approximately 6.3% per rate year versus 8% and 3.4% in Rate Year 1 and 2 respectively for the non-levelized increases.

The revenue requirement contemplated by the Joint Proposal compares favorably with a litigated outcome for the rate year ending September 30, 2009 (Rate Year 1). Staff's filed case of $58.7 million is $5.7 million more than the Joint Proposal increase of $53.0 million. The principal drivers behind the Joint Proposal's Rate Year 1 increases/decreases, as compared to Staff's litigated case are:

Increases

- Sales forecast adjustment ~ $2.8 million
- Allowance for a placeholder for Steam Incident Action Plan ~ $3.6 million
- Staff's updated capital structure, including ROE from 9.1% to 9.3% ~ $3 million
- Various O&M adjustments ~ $1.5 million
- Property Tax Update ~ $2 million
- All Other ~ $0.7 million

Offset by:

- Depreciation adjustments to eliminate the reserve deficiency, depreciation rate change and water treatment ~ ($15 million)
- Amortization of First Avenue Property sales proceeds (3 years vs. 2 years) ~ ($4.3 million)

The Joint Proposal, in essence, adopts a revenue increase in Rate Year 2 of $24.7 million. The Rate Year 2 forecasts were developed using Rate Year 1 as the base for the projections. The major components of the rate year two increases are:

- inflation (2.1% GDP deflator) on various O&M and labor costs (labor growth rate 2.0%) ~ $6 million
- Rate Base additions (demineralization plant going online) ~ $11 million
- Property taxes ~ $3.2 million
- Depreciation ~ $3.7 million
- Other Operating revenue (ERRP-Rent) ~ $1.9 million
- All Other ~ $0.6 million

Offset by:

- sales forecast, net of fuel ~ ($1.7 million)

2. Cost of Capital

The Joint Proposal's revenue requirement reflects a 7.50% overall rate of return, including a 48.0% equity ratio and an authorized return on equity (ROE) of 9.3% (Joint Proposal, Page 4 of 5, Appendix A). The Company's testimony proposed an 8.58% rate of return based on a 48.37% common equity ratio and an 11.5% ROE for a multi-year plan, and argued that an 11.2% ROE is reasonable for a one-year case (Morin testimony p. 61.).[6]

In contrast, Staff recommended that a more appropriate rate of return for Con Edison's steam business would be 7.35%, including a 47.92% common equity ratio and a 9.1% ROE. The 7.50% rate of return contained in the Joint Proposal is a reasonable outcome given the modest increase in the Company's business risk, the multi-year term of the rate plan, and the current interest rate environment. The 48% equity ratio is also reasonable given the long-term nature of the rate plan and the potential impact of the sale of the parent's non-regulated generating assets and the subsequent retirement of debt on the consolidated capital structure. (Perkins rebuttal at p.14).

3. Return on Equity

The Joint Proposal's recommended 9.3% multi-year Rate Plan ROE is only 20 basis points higher than Staff's 9.1% ROE testimony recommendation and 220 basis points lower than the Company's pre-filed 11.5% ROE position. The 9.3% ROE is fair and reasonable, particularly given the recent developments which have increased risk and the particular dynamics of the multi-year Rate Plan. To begin with, in late March, both of the major credit rating agencies concluded that there was a material increase in Con Edison's business risk. As a result, the Company's senior unsecured debt rating was downgraded one notch by Standard & Poor's from "A" to "A-", while the outlook of Con Edison's "A1" senior unsecured rating was revised from "stable" to "negative" by Moody's Investors Service.

Over the past four months risk in the broader credit markets has also increased. One indication of this increased risk is the prospective cost of issuing new debt securities. While benchmark treasury rates have not changed all that much, the yield spreads required by investors for new debt obligations has increased for both utility and non-utility issuers. For instance, when

[6] Additionally, no adjustments were made to the cost rates for the Company's one-year case.

Staff's pre-filed testimony was filed the yield spread required for new 10-year "A" rated utility debt obligations was 165 basis points above the ten-year treasury yield, while the yield spread for new 30-year debt was 170 basis points (Staff Finance Panel testimony p 33). Currently, based upon the actual cost rates incurred by the Company in its April 7, 2008, issuance of $600 million of ten-year debt securities and $600 million of thirty-year obligations, spread requirements have increased appreciably, and are now 230 basis points for 10-year debt and 240 basis points for 30-year debt. The higher prospective borrowing costs also support the reasonableness of the 5.91% weighted cost of debt contained in the Joint Proposal.

Another example of the elevated risk in the broader credit markets is the increased scrutiny facing bond insurers as a result of the sub-prime mortgage crisis. This development has resulted in significantly higher borrowing costs for five issues of the Company's variable rate tax-exempt debt, each of which is re-priced periodically via an auction and insured by either Ambac Assurance Corporation or XL Capital Assurance Inc. Recognizing the uncertainty related to this debt, the Joint Proposal allows the Company to true-up its actual interest costs related to these obligations to the amount reflected in rates. As the Commission recognized in the Company's most recent electric rates proceeding in Case 07-E-0523, these uncertainties are beyond the Company's control and thus the true-up of these interest costs is reasonable.

Finally, with respect to the risks inherent in a multi-year plan, it is common practice to add a modest premium to the allowed ROE to account for a utility's risk that much of its non-commodity operation and maintenance (O&M) expenses, such as labor costs and health care costs, will increase faster than is expected over the term of the rate plan. Such a premium is reasonable given that these risks will be borne by the Company's shareholders. Moreover, the premium in this case, which is no more than 20 basis points, is consistent with other recently-adopted Joint Proposals.

4. Earnings Sharing Mechanism

There is a 50/50 earnings sharing mechanism for the Company and customers, if the earned common equity return exceeds 10.1% or 80 basis points above the allowed return of 9.3%, subject to a weather adjustment detailed in Appendix G. Earnings sharing will be performed at the end of the two year rate plan on a cumulative basis.

The equity ratio used in the earnings sharing mechanism will be limited to the lower of the Company's actual equity ratio or 50%. This assures that if Con Edison's parent corporation,

Con Edison, Inc. (CEI), issues debt which is then treated by Con Edison as equity, the intent of the earnings sharing mechanism will not be thwarted. The use of actual equity ratios (assuming they are below 50%) acts as an incentive to Con Edison to keep its equity level close to what is forecast in the Rate Plan and not to decrease it substantially, which could have negative consequences for the Company's bond rating.

Staff's direct testimony was for a one-year rate case and, as such, appropriately did not provide for an earnings sharing mechanism. The earnings sharing mechanism as detailed in the Joint Proposal is an important part of any multi-year rate plan. Such a mechanism provides Con Edison with a strong incentive to minimize costs and improve efficiencies, by allowing its shareholders to share in savings produced by those efforts. In addition, if Con Edison exceeds the parties' expectations of its financial performance, the mechanism ensures that customers receive a fair share of the benefits associated with that performance and prevents the Company from wholly retaining unanticipated benefits. Further, the incentive provided by the mechanism could result in the Company having lower-than-forecast expenses at the end of the Rate Plan and when rates are reset.

The 80 basis point deadband is similarly reasonable. It provides a sufficient incentive for the Company to increase efficiencies or otherwise reduce costs, but it is not so large that benefits from such activities will inure only to shareholders. From a comparability perspective, the deadband is smaller than the 100 basis point deadband adopted in the 2006 Rate Order.[7]

5. Reconciliations

Section E of the Joint Proposal lists the cost and revenue categories that will be reconciled annually and for which Con Edison may use deferral accounting to account for differences between actual costs or proceeds and those levels provided for in the Rate Plan. Such costs include:

- Property Taxes 90/10 true-up
- Municipal Infrastructure Support (aka Interference) (excl. Co. labor) 90/10 true-up
- Production Plant Expenditures (to the downside only)
- Pension/OPEBs (Policy Statement)
- Environmental Remediation (SIR costs)

---

[7] Case 05-S-1376, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Consolidated Edison Company of New York, Inc. for Steam Service, Order Determining Revenue Requirement and rate Design (issued September 22, 2006) (2006 Rate Order).

- SO2 Allowances (revenue)
- Deferred Income Taxes (263A and Bonus Depreciation)
- Tax Exempt Debt
- Ravenswood (downside only)
- Steam Incident Action Plan (placeholder)

Each of these costs or imputations will be reconciled based on the levels delineated in Appendix D of the Joint Proposal. Staff's testimony supported the Company's request to reconcile Pension and OPEB expenses, Staff opposed reconciliation of property taxes, interference expense and certain other costs in its pre-filed testimony because such reconciliations are unnecessary in a one-year rate case.

With respect to property taxes, interference expense, Steam Incident Action Plan, Environmental Remediation, S02 Allowances, tax exempt debt and certain deferred taxes, we believe that these are material items, and largely beyond the Company's ability to control, which is why we believe reconciling these items in a multi-year rate plan is appropriate.

The Ravenswood and Production Plant Expenditures are only reconciled to the downside and are designed to protect customers if the Company spends less than is forecasted in this rate case.

6. Property Taxes

The Joint Proposal allows for reconciliation of 90% of the variation from the specified annual expense level for property taxes. The expense levels in the Joint Proposal assume that there will be no increase in the tax rate in either rate year. Staff's testimony advocated for such a zero percent escalation rate.

Additionally, 86% of any property tax refunds, including credits against tax payments, received by the Company as a result of its efforts to collect such will be deferred to be available as credits if future rate proceedings. Any incremental costs incurred by Con Edison to achieve tax refunds or credits will be taken from the refunds or credits before such sharing factor is applied. The Company's retention of any property tax refunds remains subject to an annual showing by Con Edison of its ongoing efforts to reduce its property tax burden (Joint Proposal, p. 21). Such treatment of property taxes is reasonable because those costs, to a large extent, are outside Con Edison's control and their partial reconciliation is appropriate as an incentive for the Company to minimize its costs to the extent possible.

7. Interference

Reconciliation of interference expenses, exclusive of Company labor, has been included in Con Edison's rate plans for some time. As with the property taxes, the Company will absorb or retain 10% of any variance from the specified annual expense level (Joint Proposal, p. 12). Reconciliation of this item is appropriate given the two-year term of the rate plan because these costs are largely beyond the Company's control. Additionally, Con Edison has committed to continue to work with New York City to plan this work in order to reduce costs. Partial reconciliation is appropriate to provide the Company an incentive to control, to the extent practicable, the costs associated with its interference work.

8. Production Plant Expenditures

The projected production plant expenditures embodied in this Joint Proposal represent a reasonable level of expenditures that are necessary to continue the safe and reliable operation of the production facilities. In testimony, Staff took issue with the Company's proposed changes to the water treatment facilities at both the 59th Street and 74th Street plants. Specifically, to the proposed replacement of existing water softening facilities installed in 1999, with demineralization water treatment facilities. The Joint Proposal addresses Staff's concerns and insures that ratepayers do not continue to pay depreciation, property and other taxes, and a return on the investment in the water softening facilities that are being replaced prematurely.

The Joint Proposal requires Con Edison to defer the revenue requirement impact of any shortfall between a target set for net steam production plant expenditures, as set forth in Appendix D of the Joint Proposal, and the actual average net steam production plant expenditures at the end of each rate year. The deferral protects customers from shortfalls in capital spending by Con Edison and ensures that the Company does not earn a return on investments that it has not actually made.

Con Edison is at risk for any capital expenditures above the levels specified in Appendix D. Should the Company incur an unplanned and unexpected capital investment in steam production plant greater than $5 million, Con Edison may petition the Commission to defer carrying cost associated with that new project, subject to the criteria applied by the Commission to such deferral petitions.[8] The specified limitations contained in Appendix D are appropriate

[8] This provision applies to extraordinary and unanticipated events, such an explosion or major equipment failure. It does not apply to projects of which the Company was aware, but, for whatever reason, omitted from its capital budget.

because they assign to Con Edison the responsibility for keeping within its forecast for plant additions and ensure that customers will not pay for plant that is not in service. Additionally, the Company will not be permitted to defer costs associated with such unplanned production plant expenditures without Commission approval.

9. Pension and OPEB Expenses

The Joint Proposal requires Con Edison to comply with the Commission's Statement of Policy and Order Concerning the Accounting and Ratemaking Treatment for Pensions and Postretirement Benefits Other Than Pensions in Case 91-M-0890, which requires the Company to defer any difference between actual Pension and OPEB costs, as well as certain tax benefits related to Medicare subsidies to the levels specified in the Rate Plan (Joint Proposal, p. 13).

10. Environmental Remediation

Environmental remediation costs will be reconciled to the levels provided in the Rate Plan (Joint Proposal, pp. 13-14). The deferral balances will be subject to interest and reduced by accruals, insurance recoveries, associated reserves and deferred taxes. Full reconciliation of these costs should eliminate any Company disincentive to clean up its environmental liabilities in a timely fashion.

Additionally, the Company will provide to Staff a report showing (i) its environmental reserve balance as of March 31, 2009 and changes in such balance in the prior twelve months; (ii) its environmental regulatory asset balance as of March 31, 2009 and changes in such balance in the prior twelve months; and (iii) remediation expenditures for the twelve month period ending March 31, 2009. Such report will allow Staff to better monitor how the Company is spending for its environmental remediation costs.

11. Steam Incident Action Plan Reconciliation

The Joint Proposal provides for the Company to defer for recovery in its next steam rate filing the difference between the amounts included in rates and the Company's actual costs, subject to the outcome of the Commission's review of the Company's identification of the costs that are incremental to the program costs already funded in rates, net of any savings and efficiencies obtained by implementing these programs. We believe that these costs may be significant, and if a placeholder was not put into rates now, there is a likelihood of building up a large deferral that would need to be collected from customers in the next rate proceeding.

12. Additional Reconciliation Provisions

The Joint Proposal continues other specified reconciliations and/or deferral accounting provisions for term of the Rate Plan and thereafter (Joint Proposal, p. 14). Certain costs are subject to full or partial reconciliation in the event projected costs differ from actual costs. These costs include proceeds from the sale of SO_2 allowances, deferred income taxes, tax exempt debt, Ravenswood O&M contract expenses, and steam incident-related program costs.

As to the steam incident-related program costs, the Joint Proposal provides for the Company to defer for recovery in its next steam rate filing the difference between the amounts included in rates and the Company's actual costs, subject to the outcome of the Commission's review of the Company's identifying the costs that are incremental to the costs of programs already funded in rates, net of any savings and efficiencies obtained by implementing these programs.

The revenue requirement also reflects the continued amortization of $4.0 million per rate year of World Trade Center ("WTC")-related costs that the Company has deferred. Treatment of deferred World Trade Center (WTC) capital costs allocated to steam will continue to be deferred in accordance with the Commission's determination in Case 01-M-1958 and subject to interest at Con Edison's allowed pretax Allowance for Funds Used During Construction (AFUDC) rate of return. Recovery of any WTC costs received by the Company from governmental agencies and insurance carriers will be applied to reduce the deferred balance.

The reconciliation provisions are standard accounting practices for utilities in New York, with the exception of the provision related to WTC costs and costs related to the steam incident. Their inclusion is therefore reasonable. Requiring the Company to offset WTC costs with recoveries or awards from governmental agencies and insurance carriers is appropriate because recovery of the costs related to that extraordinary and tragic event should be sought first from sources other than customers. Additionally, deferral of the costs related to the steam incident allows the Commission and Company to continue to review and implement plans for dealing with the incident, and to allow the Commission to provide guidance on how it wants such costs handled, including the outcome of any prudence review.

13. Limitations on Deferrals

For earnings above the Earnings Sharing Threshold, the Company will apply 50 percent of its share of any such earnings to reduce deferred undercollections of property taxes, if any.

This analysis will be performed at the end of the two-year rate plan on a cumulative rate year basis.

14. Depreciation and Reserves

The Joint Proposal keeps current depreciation rates unchanged. In addition, it provides for the Company to terminate the five-year amortization of the reserve deficiency established by the 2006 Steam Rate Order. Staff's initial testimony did not address this issue, but terminating the amortization decreases the overall revenue requirement, thereby benefiting customers.

15. Interest on Deferred Costs

As in most utility rate plans, the Joint Proposal specifies that interest will, subject to a few specified exceptions, accrue on the deferred net-of-tax balances at the unadjusted customer deposit rate as determined by the Commission on an annual basis (Joint Proposal, p. 20). Such treatment is reasonable because it applies equally to balances owed to and from customers and because it is consistent with past practice.

16. Allocations of Common Costs

The Joint Proposal proposes to continue the common expenses and common plant allocations according to the percentages reflected in the steam revenue requirement calculation (Joint Proposal, p. 20). Should the Commission approve different common cost allocation factors prior to the next steam rate case, the Joint Proposal requires the Company to defer the resulting change in the steam revenue requirement for future credit to, or collection from, customers. Such treatment of common costs also is consistent with past practice.

C. Other Revenue Requirement and Rate Issues

1. Steam Sales

Staff's filed testimony essentially accepted the Company's methodology and forecast results with the notable exception of the Company's elasticity adjustment. In essence, Staff took issue with the lack of fundamental support in the Company's filing for such adjustment. Notwithstanding that discrepancy, the Company did provide Staff with updates on actual sales for the months of November 2007 through April 2008.

The sales forecast specified in the JP reflects Staff's litigation forecast less $3.1 million in Rate Year 1 and $6.65 million in Rate Year 2. These figures reflect a reasonable balancing of the difference between Staff's and the Company's forecast of steam sales.

Staff testified that the Company's proposed 541 MMlb initial testimony price elasticity adjustment should be rejected given its lack of support. Staff also did not accept the Company's 635 MMlb update. In revenue requirement terms, this 1,176 MMlb litigation difference represents $14.2 million - $5.6 million for the price elasticity adjustment in the Company's original filing and $8.6 million for the Company's update.

The 1,176 MMlb difference in the two sales forecasts should immediately be discounted for two reasons. First, given that JP ensures that customers will only face a price increase reflective of $54.4 million of the company's originally requested $126.6 revenue requirement, the 541 MMlb price elasticity reduction would change to a 232 MMlb reduction based upon the Company's methodology [Hearing Exhibit 205] (which assumed a $100M initial revenue requirement [TR 731]). Second, Company witness Yaegel indicated that 211 of the 635 MMlb rebuttal testimony adjustment was related to the original forecast being too high because an extraordinary weather related 211 MMlb addition was made to the original forecast that was not warranted [TR 726]. Thus, a reasonable representation of the litigation difference between Staff and the Company is 656 MMlbs or $8.3 million in revenue requirement.

Staff, in the interests of compromise and recognition that the Company's actual updated sales would be included in the test year in the next filing, absent a multi-year agreement, made some movement on sales, more in the second year than the first.[9] Therefore, Staff views these sales numbers as reasonable and in line with Staff's testimony in light of the Company's updates of recent actual sales figures.

2. East River Repowering Project

Staff testimony recommended that a proceeding be instituted to re-examine the Steam-Electric cost allocation of the East River Repowering Project (ERRP). The proposed rates reflected in the Joint Proposal reflect the current allocation of the costs of the ERRP between Steam and Electric and requires that the Company, with input from Staff and other interested parties, to perform a detailed study on the allocation of the ERRP costs (e.g., capital, property taxes, O&M and fuel) between Steam and Electric. This study will be filed with the Commission on or before April 30, 2009. The Commission can then establish a procedure for comments.

[9] The JP's forecast provides the company $3.1M of the $8.3M revenue requirement difference between staff and the company in RY1 or 37%. The JP also provides the company $6.65M of the $8.3M in disputed revenue requirement RY2 or 80%.

Parties, including the Company, will be able to use the results of this study to recommend changes to the allocation in the Company's next general steam base rate filing. This provision of the Joint Proposal results in a similar outcome to that advocated by Staff in testimony.

3. Fuel Adjustment Clause

The Joint Proposal allows the Company to continue to recover through the FAC its total fuel costs associated with the actual steam system variance (i.e., the difference between sendout and sales), to the extent such costs are not recovered in base rates, subject to the reconciliation mechanism established by the 2004 Steam Rate Order[10] and set forth in the steam tariff. Continuation of the steam variance reconciliation mechanism will insure that the Company continues to have an incentive to reduce losses which will benefit all ratepayers.

In its testimony, Staff took issue with the cost recovery mechanism (either base rates or FAC) of various elements of costs that the Company was either currently recovering through the FAC or had proposed to begin to recover through the FAC. The Joint Proposal contains provisions that allow the Company to continue to use the FAC to recover all costs associated with oil storage and handling, including Company labor, through the FAC. By no later than June 30, 2009, the Company will review with Staff and other interested parties the oil storage and handling costs that the Company currently recovers through the FAC (e.g., dredging costs, dock repairs) to consider which of these costs, if any, should be recovered in base rates the next time the Company's steam base rates are reset. This process will allow for a thorough discussion and review of the nature of the oil storage and handling costs to ultimately determine the proper cost recovery mechanism.

4. ECOS and Rate Design

The revenue allocation agreed to in the Joint Proposal reflects, among other things, a phase-in of the revenue surpluses and deficiencies as identified in the Company's embedded cost of service ("ECOS") Study submitted in this proceeding. Staff's testimony supported the recognition of the revenue surpluses and deficiencies as identified in the ECOS. The Joint Proposals eliminates 50 percent of the deficiencies and surpluses in RY1 and the remaining 50 percent of the deficiencies and surpluses in RY2. This phase-in eventually arrives at the position supported by Staff in its filed case, while mitigating the impact to customers.

---

[10] Case 03-S-1672, Consolidated Edison Company of New York, Inc. – Steam Rates, Order Adopting The Terms of A Joint Proposal (September 27, 2004) ("2004 Steam Rate Order").

The Joint Proposal provides for increases in the customer charge and re-designed usage rates for SC 2 Rate II demand rate customers on a revenue neutral basis, which reflect a declining block rate structure. Staff's testimony supported the revisions to the customer charge levels to further reflect cost based amounts shown in the ECOS study. In addition, the proposed changes to the usage block rates are reasonable in that they achieve rate structures based on sound ratemaking principles that are fair and equitable for both customers and the Company.

5. Demand Rates

In its testimony, Staff recommended that the Company be required to submit a proposal to expand the applicability of demand billing beyond the current requirement of those customers with average annual usage exceeding 22,000 Mlbs and / or to increase the amount of fixed costs currently collected through demand charges. The Joint Proposal requires that the Company study the impact(s) of demand billing on SC 2 and SC 3 customers with usage equal to or greater than 22,000 Mlbs (those customers currently on demand billing) for the 2007-2008 and 2008-2009 winter periods and the potential impact of demand billing on customers with annual usage of less than 22,000 Mlbs but equal to or greater than 14,000 Mlbs for the 2008-2009 winter period.

The Company would also be required to present to Staff and interested parties, at a technical conference during July 2009, the results of the above-mentioned study and the proposed sample winter demand rates for customers to be sample billed during the 2009-2010 winter period, with actual demand billing to be implemented in the following rate year, 2010-2011. The Company will file to implement proposed demand rates to be effective beginning at the start of the 2010-2011 winter demand period (i.e., December 2010 through March 2011), on a Company revenue neutral basis. The expansion of demand billing will provide additional customers with a direct incentive to reduce peak usage, which in turn should reduce the Company's winter peak load potentially reducing or eliminating the need to build additional production plant in the future.

D. Non-Rate and Other Issues

Staff and other parties have had significant concerns with the manner in which Con Edison has operated the steam department for a number of years. The need for heightened focus and emphasis was a primary issue in Case 03-S-1376 and Case 05-S-1376, and continues in this

proceeding. Towards this end, the Joint Proposal incorporates a number of performance metrics designed to incent the Company to improve performance in critical areas.

1. Steam Business Development

The Joint Proposal requires the Company to continue to perform several activities related to market share preservation and expansion. The business development activities specifically require the Company to actively meet and follow up with industry representatives and to measure and monitor customer satisfaction through the use of customer focus groups and customer satisfaction surveys. In addition, these activities have associated revenue adjustments for non-performance and annual reporting requirements. In testimony, Staff recommended the continuation of these specific steam business development performance mechanisms and associated revenue adjustment mechanisms as contained in the Joint Proposal. The provisions will provide Con Edison with the necessary direction and incentive to maintain and improve its steam business development efforts.

2. Thermal Efficiency/Losses

The Joint Proposal requires that the Company in collaboration with Staff and interested parties to select a consultant to review the thermal efficiency studies performed by the Company since 1995 and to develop a detailed action plan that would prioritize implement and maintain economic projects for reducing overall steam losses. Staff supports these provisions and will actively participate in the collaboration. Improving the Company's steam system thermal efficiency, through the development and implementation of cost effective measures, will ultimately benefit all steam ratepayers.

3. Steam Resource Plan

In testimony, Staff recommended that the Commission consider instituting a proceeding in which the Steam Resource Plan (SRP) can be fully reviewed and considered in the context of other statewide and New York City wide system planning objectives.

The Joint Proposal requires that the Company complete the investment grade study of a cogeneration plant, of up to 500 MW, at the Hudson Avenue Station that is currently being conducted by an independent consultant retained by the Company ("Cogeneration Study"). The Company will then file a supplement to the Steam Resource Plan (SRP) with the Commission on or before December 31, 2008 that will incorporate updated fuel and energy price forecasts and include the results of the Cogeneration Study. In addition, consideration will be given to various

other cogeneration plant designs, and electric and steam outputs, as well as the Hudson Avenue options presented in the SRP. The Company will select an option that meets its reliability and capacity needs and considers cost-effectiveness and statewide and NYC-wide energy planning objectives.

The Joint Proposal envisions that the Commission will establish a procedure for parties to file comments on the Supplement. This process will result in a similar outcome as recommended by Staff in testimony, and provides for the most up to date fuel and energy price forecasts and the results of an investment grade analysis of a cogeneration plant, previously not included in the SRP.

4. Energy Efficiency

In testimony, Staff explained that the Company's energy efficiency proposals lacked the planning and detail that would improve their likelihood of success and that an understanding of the market potential for steam energy efficiency measures is necessary. Staff recommended that the Company use the first six months of RY 1 to conduct a collaborative effort with Staff, NYSERDA, and other stakeholders to develop more fully realized plans.

The Joint Proposal requires that the Company convene a collaborative of interested parties to consider (1) the market potential for steam energy efficiency programs for steam customers proposed for RY 2, and (2) customer incentives and Company incentives associated with such programs. This process will insure that the Company's energy efficiency plan will be fully developed and increase the potential success of the program.

5. Safety Performance Measures

Staff testimony recommended that the Commission adopt a Steam Safety Performance mechanism to encourage the Company to maintain and improve its operations in specific areas that affect the safety and reliability of its steam distribution system. The Company's current rate plan does not provide for any safety related performance targets.

The Joint Proposal provides for the implementation of an Emergency Response Time safety performance measures, and associated negative revenue adjustments, to be in place during calendar years 2009 and 2010. In addition, the provisions allow for the development of a Steam Leak Backlog Management safety performance measure, and associated negative revenue adjustment, to take effect for calendar year 2010.

Staff finds that these provisions are necessary to ensure that the Company continually improves its level of safety so that it may better serve and protect the public.

CONCLUSION

Staff respectfully requests that the ALJ and the Commission approve or adopt the Joint Proposal. The proposed terms and conditions avoid an overall rate increase for two years, provides an incentive to Con Edison to increase its focus and emphasis on all aspects of its steam system, furthers the Commission's objectives in ensuring the continued viability of Con Edison's steam service, furthers the Commission's Pension Policy Statement and other policy objectives, balances the interests of all parties, is within the bounds of the potential outcome of a litigated result in this proceeding, and constitutes fair resolution of the issues in dispute.

Respectfully submitted,

Dakin D. Lecakes
Assistant Counsel

Dated: June 26, 2008
Albany, New York

APPENDIX A

STAFF PRE-FILED TESTIMONY

WITNESS	TOPIC(S)
Accounting Panel	Revenue Requirement Issues
Fred Barney	Steam Sales
Matt Cinadr	Steam Production
Energy Efficiency Panel	Energy Efficiency Proposal
Finance Panel	Return on Equity, Cost of Capital
Marco Padula	Steam Business Development
Rate Panel	Cost of Service, Rate Design
Safety Panel	Saftey Issues, Performance Metrics