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April 11, 2008

VIA HAND DELIVERY

Hon. Jaclyn A. Brilling, Secretary
New York State Public Service Commission
Three Empire State Plaza
Albany, New York 12223

Re: Case 07-M-0906 – Joint Petition of Iberdrola, S.A., Energy East Corporation, RGS Energy Group, Inc., Green Acquisition Capital, Inc., New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation for Approval of the Acquisition of Energy East Corporation by Iberdrola, S.A.

Dear Secretary Brilling:

Multiple Intervenors, an unincorporated association of over 50 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State, including the New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation service territories, hereby submits the original and five copies of its Initial Brief in the above-referenced proceeding.

Copies of the enclosed Initial Brief are being served on all active parties via e-mail and, where requested, also by U.S. Mail.

Respectfully submitted,

COUCH WHITE, LLP

Michael B. Mager

Michael B. Mager

MBM/cgw
Enclosures
cc: Judge Rafael A. Epstein (via Hand Delivery and U.S. Mail; w/enc.)
Active Parties (via E-Mail and/or U.S. Mail; w/enc.)
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STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

Joint Petition of Iberdrola, S.A., Energy East Corporation, RGS Energy Group, Inc., Green Acquisition Capital, Inc., New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation for Approval of the Acquisition of Energy East Corporation by Iberdrola, S.A.	Case 07-M-0906

INITIAL BRIEF
OF
MULTIPLE INTERVENORS

Dated: April 11, 2008

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PRELIMINARY STATEMENT

Multiple Intervenors, an unincorporated association of over 50 large industrial, commercial and institutional energy consumers with manufacturing and other facilities located throughout New York State, including the New York State Electric & Gas Corporation ("NYSEG") and Rochester Gas and Electric Corporation ("RG&E") service territories, hereby submits its Initial Brief in Case 07-M-0906.[1] This proceeding was instituted by the New York State Public Service Commission ("Commission") to examine whether Iberdrola, S.A. ("Iberdrola") should be authorized to acquire, via merger, Energy East Corporation ("Energy East"), parent of NYSEG and RG&E. For the reasons set forth herein, Multiple Intervenors urges the Commission to approve the proposed transaction, subject to numerous conditions intended to produce financial and other benefits and protections for customers of NYSEG and RG&E. The imposition of such conditions is absolutely essential to ensure that the proposed transaction is in the public interest.

PROCEDURAL BACKGROUND

On or about August 1, 2007, Energy East, RGS Energy Group, Inc., Green Acquisition Capital, Inc., NYSEG and RG&E (collectively, "Petitioners") filed with the

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[1] Case 07-M-0906, Joint Petition of Iberdrola, S.A., Energy East Corporation, RGS Energy Group, Inc., Green Acquisition Capital, Inc., New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation for Approval of the Acquisition of Energy East Corporation by Iberdrola, S.A.

Commission a "Joint Petition for Approval of the Acquisition of Energy East Corporation by Iberdrola, S.A." ("Joint Petition"). (Ex. 41.)[2]

On September 10, 2007, a prehearing conference was conducted by Administrative Law Judge Rafael A. Epstein. At that conference, the parties agreed upon a litigation schedule for the remainder of the proceeding, which was adopted by Judge Epstein and then memorialized in a ruling.[3] The adopted schedule addressed the possibility that settlement negotiations might – or might not – result in a joint proposal for the Commission's consideration.[4]

Subsequent to the September 10th conference, the parties engaged in settlement negotiations but were not able to achieve an agreement in principle. Consequently, in accordance with the litigation schedule: (a) Petitioners supplemented the Joint Petition with testimony and exhibits filed on or about November 28, 2007; (b) responsive testimony and exhibits were filed by New York State Department of Public Service Staff ("Staff") and intervener parties on or about January 11, 2008; and (c) rebuttal testimony and exhibits were filed by Petitioners on or about January 31, 2008.[5]

Following the submission of rebuttal testimony and exhibits, the parties resumed settlement negotiations but still were not able to achieve an agreement in principle.

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[2] References to the exhibits admitted into evidence during the evidentiary hearing conducted in this proceeding are preceded by the notation, "Ex."; and parenthetical references to the transcript of the hearing are preceded by the notation, "Tr."

[3] See Case 07-M-0906, supra, Procedural Ruling (issued October 4, 2007) at 1-3.

[4] Id. at 2.

[5] See id.

The negotiations did, however, necessitate a modification to the litigation schedule, which was agreed upon by the parties, and adopted and then memorialized by Judge Epstein.[6]

On March 14, 2008, Petitioners circulated to other parties "Joint Petitioners' Partial Acceptance Document" ("Partial Acceptance"), which purportedly was intended "to narrow the issues raised in this proceeding prior to the commencement of evidentiary hearings ...." (Ex. 50.)[7] In the Partial Acceptance, Petitioners conceded unilaterally to certain conditions of merger approval relating to: (a) vertical market power ("VMP"); (b) positive benefit adjustments ("PBAs");[8] (c) future development of renewable generation by Iberdrola Renewables, an unregulated company in which Iberdrola owns a controlling (i.e., 80 percent) share (see Tr. 625); (d) certain electric reliability concerns expressed by electric cooperatives and the Village of Sherburne; and (e) certain environmental and safety concerns expressed by the City of Rochester. (Ex. 50.) For the reasons detailed herein, the concessions offered by Petitioners in the Partial Acceptance, while generally beneficial, are inadequate and must be supplemented.

An evidentiary hearing on the proposed transaction was conducted by Judge Epstein on March 17-20, 2008. The record compiled during the hearing is comprised of 1,908 pages of transcript and 136 exhibits. At the conclusion of the hearing, the parties agreed upon, and Judge Epstein approved, deadlines for initial briefs and reply briefs of April

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[6] See Case 07-M-0906, supra, Procedural Ruling on Scheduling (issued February 25, 2008) at 3-4.

[7] Petitioners' Partial Acceptance was circulated in the afternoon of the business day prior to commencement of the evidentiary hearing.

[8] PBAs refer to financial benefits to be provided to NYSEG and RG&E customers if the proposed transaction is consummated. (See, e.g., Tr. 1367, 1676-77, 1737-38.)

11 and 25, 2008, respectively. (Tr. 1896-99.) That briefing schedule subsequently was memorialized in a ruling issued by Judge Epstein.[9]

SUMMARY OF POSITION

Multiple Intervenors supports the proposed transaction between Iberdrola and Energy East, provided that approval of the merger is subject to numerous conditions designed to produce financial and other tangible benefits and enforceable protections for customers of NYSEG and RG&E. Specifically, such conditions should include, but need not be limited to, Iberdrola's acceptance of: (a) substantial financial and rate-related benefits for customers; (b) more stringent electric and gas reliability, service quality and safety performance standards and revenue adjustments; (c) financial protections for customers; (d) robust reporting requirements; and (e) measures that would mitigate VMP concerns in a manner that would not preclude Iberdrola Renewables' future development of wind generation. Absent such conditions, the proposed transaction would not be in the public interest.

Multiple Intervenors' Initial Brief is organized into eight points. In Point I, Multiple Intervenors addresses the standard of review and the burden of proof that should be applied in this proceeding.

In Points II through VI, Multiple Intervenors advocates that merger approval should be conditioned upon: (a) the provision of substantial financial and rate-related benefits to customers (see Point II); (b) the implementation of more stringent electric and gas reliability, service quality and safety performance standards and revenue adjustments (see

[9] Case 07-M-0906, supra, Procedural Ruling on Scheduling (issued April 2, 2008).

Point III); (c) the adoption of financial protections for customers (see Point IV); (d) the adoption of robust reporting requirements (see Point V); and (e) the adoption of measures that would mitigate VMP concerns in a manner that would not preclude Iberdrola Renewables' future development of wind generation (see Point VI).

In Point VII, Multiple Intervenors advocates that proposals by Staff and Petitioners to implement electric and gas revenue decoupling mechanisms ("RDMs") for NYSEG and RG&E should be rejected at this time.

Finally, in Point VIII, Multiple Intervenors advocates that the rumored future acquisition of Iberdrola increases the risks associated with the proposed transaction herein, thereby warranting the adoption of additional protections for customers.

ARGUMENT

POINT I

THE STANDARD OF REVIEW AND THE BURDEN OF PROOF THAT SHOULD BE APPLIED IN THIS PROCEEDING

The proposed transaction – involving Iberdrola's acquisition of Energy East, parent of NYSEG and RG&E – is governed by New York Public Service Law ("PSL") section 70. Pursuant to that statute, Commission approval of the transaction is required, and such consent shall not be granted "unless it shall have been shown that such acquisition is in the public interest." PSL § 70. Approval of the proposed transaction may be "upon and subject to such terms and conditions as [the Commission] may fix and impose." Id. The burden of proof is on Petitioners. Id.[10]

There is considerable controversy in this proceeding as to how the public interest standard should be defined and interpreted. Multiple Intervenors contends that the Commission possesses broad discretion in evaluating the potential benefits, as well as the potential costs and risks, of the proposed transaction. Such potential benefits, costs and risks must be identified and evaluated, and the proposed transaction should be approved only if it would produce net benefits. (Tr. 999.) Importantly, not all potential benefits, costs and risks can be quantified. As Petitioners witness Meehan testified on cross-examination, potential benefits, costs and risks sometimes need to be evaluated qualitatively:

> I think in meeting the public interest standard you would want to look at both the benefits or the costs and the risks. You can't always do that quantitatively on either side.

(Tr. 1000.) Thus, in determining whether the proposed transaction satisfies the public interest standard, the Commission should utilize its best judgment in evaluating whether the potential benefits exceed, or outweigh, the potential costs and risks.

In this proceeding, Staff advocates that the proposed transaction be rejected. The Staff Policy Panel testified that:

> Staff, after a comprehensive analysis of the risks, costs and benefits of the proposed transaction, has reached the conclusion that the proposed acquisition of [Energy East] by [Iberdrola] is not in the public interest, and as such, should not be approved by the Commission.

[10] Petitioners acknowledge that the burden of proof in this proceeding is on them. For instance, Petitioners' Benefits and Public Interest Panel testified that: "To obtain the Commission's consent for the Proposed Transaction, the Joint Petitioners must show that the Proposed Transaction is in the public interest." (Tr. 473.)

(Tr. 1147; see also Tr. 1365.)[11] While Multiple Intervenors agrees with many of Staff's conclusions regarding the potential benefits, costs and risks of the proposed transaction, it disagrees with Staff's ultimate conclusion. Multiple Intervenors recommends that the Commission grant merger approval, subject to numerous conditions intended to produce financial and other tangible benefits and enforceable protections for customers in the NYSEG and RG&E service territories. The difference in position between Staff and Multiple Intervenors, while very limited in many respects, relates primarily to Multiple Intervenors' contention that the Commission, through the use of its broad powers to withhold merger approval absent Iberdrola's acceptance of certain conditions, is able to exert tremendous influence as to whether the transaction would be in the public interest.[12]

Importantly, while Multiple Intervenors may differ with Staff as to the ultimate outcome in this proceeding, it concurs with Staff in terms of how the public interest standard should be applied. In advancing its recommendations herein, the Staff Policy Panel testified that: "The standard that we use is that the proposal should provide some tangible positive benefits to ratepayers, in the form of lower rates, reduced costs or other monetary value." (Tr. 1148.) Support for that standard can be found in the Commission's recent orders and pronouncements in Case 06-M-0878, wherein the acquisition of KeySpan

[11] Petitioners' circulation of the Partial Acceptance on the eve of the evidentiary hearing apparently did not alter Staff's position regarding the proposed transaction. (See, e.g., Tr. 1456.)

[12] Petitioners witness Meehan testified on cross-examination that, from Iberdrola's perspective, it would be preferable for the Commission to condition merger approval upon the acceptance of additional concessions than to reject the transaction outright. (Tr. 1002-03.)

Corporation ("KeySpan") by National Grid plc ("National Grid"), via merger, was approved subject to numerous conditions.[13]

In Case 06-M-0878, the Commission summarized the public interest standard as follows: "Our statutory responsibility in this case is to determine whether the merger terms ... are in the public interest within the borders of New York, both in the short- and long-term ...."[14] The Commission also noted that "[t]he burden of proof with respect to all the merger and revenue requirement issues rests squarely on the Petitioners."[15] In applying that standard, the Commission clearly accorded substantial weight to the financial benefits that would be accorded to customers:

> The more than $686 million of benefits to New Yorkers can be seen as the positive side of the ledger in a simple cost-benefit analysis. They comprise a significant part of the context within which we evaluate whether the proposed terms ... are collectively in the public interest.[16]

In addressing the public interest standard at Commission's August 15, 2007 public session on the National Grid/KeySpan transaction, the Acting General Counsel

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[13] See Case 06-M-0878, Joint Petition of National Grid plc and KeySpan Corporation for Approval of Stock Acquisition and other Regulatory Authorizations, Abbreviated Order Authorizing Acquisition Subject to Conditions and Making Some Revenue Requirement Determinations for KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island (issued August 23, 2007) ("Abbreviated National Grid Order"), and Order Authorizing Acquisition Subject to Conditions and Making Some Revenue Requirement Determinations for KeySpan Energy Delivery New York and KeySpan Energy Delivery Long Island (issued September 17, 2007) ("National Grid Order").

[14] Case 06-M-0878, supra, Abbreviated National Grid Order at 5-6; see also National Grid Order at 110-11.

[15] Case 06-M-0878, supra, Abbreviated National Grid Order at 6; see also National Grid Order at 111.

[16] Case 06-M-0878, supra, Abbreviated National Grid Order at 9.

emphasized the need to compare benefits to costs, and discussed the level of judgment that must be exercised by the Commission in its evaluation:

> The basic standard is the public interests standard, which is a very broad standard for the Commission to consider, the benefits that the transaction would provide to the State of New York. When those benefits are considered, they have to be considered in light of the potential detriments ... and in the final analysis, the judgment has to be made and a rational basis has to be set forth that the transaction overall will produce benefits for the State of New York. So it's a simple standard, but a lot of judgment has to go into weighing the two sides of the equation.[17]

In interpreting that standard, the Commission has applied a positive, "net benefit test," as opposed to a "no harm test," which is used in some other jurisdictions.[18]

Throughout this proceeding, Petitioners have sought to distinguish the Iberdrola/Energy East transaction from the National Grid/KeySpan transaction. (See, e.g., Tr. 501.) Such arguments largely should be rejected. While the two transactions admittedly present certain differences in circumstances, the similarities are overwhelming and cannot be ignored.

In both cases: (a) a large, international corporation sought to purchase a New York utility corporation; (b) the proposed combination involved multiple electric and/or gas utilities; (c) issues were raised regarding the level and the adequacy of financial benefits that would be provided to customers; (d) issues were raised regarding the potential impacts of the transaction on future electric and gas reliability, service quality and safety performance; (e) issues were raised regarding new or increased financial risks that would be imposed on customers; (f) issues were raised regarding the adequacy of applicable reporting

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[17] Commission Session, August 15, 2007, Transcript at 19.

[18] See id. at 20.

requirements if the combination were approved; and (g) the transaction raised VMP issues regarding the proposed dual ownership or control of generation assets and transmission and distribution ("T&D") assets. When those similarities are considered in light of the fact that the National Grid/KeySpan transaction was resolved less than a year ago and is the most recent merger involving New York electric and/or gas utilities, it strains credulity to argue that the Commission should not be guided here by its decision involving that transaction.

In Case 06-M-0878, many (but not all) of the parties negotiated joint proposals that, if adopted, would have resulted in Commission approval of the National Grid/KeySpan transaction subject to numerous financial and other benefits and protections being provided to customers.[19] In ruling on the joint proposals, the Commission insisted upon numerous modifications that, in all respects, were intended to increase the benefits and/or the protections that would be realized by customers. Ultimately, merger approval was granted, subject to: (a) the provision of substantial and quantifiable financial benefits to customers; (b) the adoption of more stringent performance standards and revenue adjustments with respect to electric and gas reliability, service quality and safety; (c) the adoption of financial protections for customers; (d) the adoption of robust reporting requirements; and (e) the adoption of provisions to address VMP concerns raised by the proposed transaction.[20]

A similar outcome should be adopted in this proceeding, although the Commission should seek to tailor the specific financial and other benefits and protections for customers to the circumstances presented herein. In deciding upon those benefits and

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[19] See, e.g., Case 06-M-0878, supra, Abbreviated National Grid Order at 8-31; National Grid Order at 17-108.

[20] See generally id., Abbreviated National Grid Order at 8-31; National Grid Order at 110-55.

protections, the Commission should bear in mind the goal articulated by Commissioner (then Chairwoman) Acampora in presiding over the National Grid/KeySpan transaction: "to ensure the ratepayers receive the absolute most in terms of benefits that might result from this merger …."[21] She also discussed, as a goal, reaching "a potential decision that could accrue the greatest benefit for the ratepayers …."[22]

Finally, in formulating the specific financial and other benefits and protections that should be accorded to customers as a condition of merger approval in this proceeding, the Commission should ensure that such benefits and protections are tangible and enforceable. As summarized in the direct testimony of the Staff Policy Panel, there were commitments made and understandings fostered in the last merger proceeding involving Energy East which, in the opinion of many, were not honored. (Tr. 1194-97.) The Panel emphasized that "benefits which are not readily enforceable … have no value because there is no substantive way to ensure that the post-acquisition companies will live up to them." (Tr. 1197.) That perspective is similar to one articulated by Commissioner (then Chairwoman) Acampora, when she stated, with respect to the National Grid/KeySpan transaction, that: "We act on guarantees, not promises."[23]

For the foregoing reasons, as well as the reasons articulated, infra, in Points II through VI, the Commission should conclude that: (a) the burden of proving that the proposed transaction is in the public interest rests squarely on Petitioners; (b) application of the public interest standard requires net positive benefits; (c) as proposed by Petitioners, and

[21] Commission Session, August 15, 2007, Transcript at 167.

[22] Id.

[23] Commission Session, August 22, 2007, Transcript at 81.

supplemented by the Partial Acceptance, the transaction does not satisfy the public interest standard; (d) rather than rejecting the proposed transaction outright, it would be preferable to condition merger approval on Iberdrola's acceptance of additional concessions; and (e) conditions similar (but not necessarily identical) to those imposed in Case 06-M-0898; involving National Grid and KeySpan, should be adopted in this proceeding. The conditions of merger approval appropriate for imposition herein should focus on, but need not be limited to: (a) financial and rate-related benefits; (b) electric and gas reliability, service quality and safety performance; (c) new financial protections; (d) new reporting requirements; and (e) measures that would mitigate VMP concerns raised by the proposed transaction in a manner that would not preclude future development of wind generation by Iberdrola Renewables.

POINT II

MERGER APPROVAL SHOULD BE CONDITIONED UPON THE PROVISION OF SUBSTANTIAL FINANCIAL AND RATE-RELATED BENEFITS TO CUSTOMERS

As demonstrated in the evidentiary record developed in this proceeding, the proposed transaction presents numerous costs and risks to customers of NYSEG and RG&E. (See, e.g., Tr. 1152-60, 1163-64, 1178-84, 1221-1364.) In order to at least partially offset those costs and risks, merger approval should be conditioned upon the provision of substantial financial and rate-related benefits to customers.[24]

[24] As detailed in Points III through VI, infra, even substantial financial benefits, by themselves, are not adequate to ensure that the proposed transaction is in the public interest. Therefore, the Commission also should condition merger approval upon: (a) the implementation of more stringent electric and gas reliability, service quality and safety

In evaluating issues pertaining to the financial and rate-related benefits that should be captured for customers as a condition of merger approval, the Commission should conclude that: (a) the PBAs offered in the Partial Acceptance are inadequate; (b) Petitioners purposefully did not attempt to identify synergy savings or other financial benefits; (c) the proposed transaction would produce synergy savings and other financial benefits; (d) customers require substantial financial and rate-related benefits for the proposed transaction to be considered in the public interest; (e) Staff's proposed one-time rate adjustments, if not reflected in conditions to merger approval, should be preserved for future rate proceedings; (f) financial benefits to customers should be used to reduce delivery rates in the near-term; and (g) merger approval should be conditioned on a two-year stay-out agreement by NYSEG and RG&E.

A. The PBAs Offered in the Partial Acceptance Are Inadequate

On the eve of the evidentiary hearing in this proceeding, Petitioners circulated the Partial Acceptance. (Ex. 50.) Perhaps recognizing that merger approval is unlikely absent the provision of financial and rate-related benefits to customers, Petitioners offered to accept certain PBAs proposed by Staff totaling $201.642 million for NYSEG and RG&E.

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performance standards and revenue adjustments; (b) the adoption of financial protections for customers; (c) the adoption of robust reporting requirements; and (d) the adoption of measures that would mitigate VMP concerns in a manner that would not preclude Iberdrola Renewables' future development of wind generation.

(Id. at 1-2.)[25] For the reasons set forth below, the PBAs offered by Petitioners are inadequate and should be increased, substantially, as a condition of merger approval.[26]

Before addressing the adequacy of the PBAs offered by Petitioners in the Partial Acceptance, it is important to place them in the proper context. In the Partial Acceptance, Petitioners contrasted the $201.642 million in PBAs offered therein with the $646 million in PBAs proposed by Staff. (Ex. 50 at 1.)[27] In response to cross-examination, Petitioners explained that: (a) on a post-tax basis, the PBAs offered in the Partial Acceptance total $133.8 million; and (b) would result in rate reductions totaling $54.8 million, allocated between NYSEG ($13.8 million) and RG&E ($41 million).[28] In comparison to the $54.8 million in actual rate reductions, the combined NYSEG and RG&E electric and gas delivery

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[25] Petitioners Policy Panel explained on cross-examination that they essentially backed into proposed PBAs after determining an acceptable total dollar value. (Tr. 611.)

[26] Multiple Intervenors does not advance a specific, recommended amount of PBAs, or other financial benefits, that should be insisted upon by the Commission as a condition to merger approval. From Multiple Intervenors' perspective, the amount of PBAs necessary to justify a finding that the proposed transaction is in the public interest cannot be made in a vacuum, and depends to some extent on how other issues raised herein are resolved. For instance, whether PBAs are flowed-through to customers on an immediate basis, and/or are accompanied by stay-out agreements limiting the ability of NYSEG and RG&E to seek rate relief for some period of time, would influence a determination as to the adequacy of PBAs. The adoption of Multiple Intervenors' position on VMP issues, which is less restrictive than that advanced by other parties with respect to Iberdrola Renewables' ability to develop wind generation, also could justify insistence upon a higher level of PBAs in recognition that VMP concerns would not be mitigated to the same degree as the adoption of a more restrictive position.

[27] The $646 million figure represents Petitioners' characterization of Staff's position in the event the Commission elects to grant merger approval subject to conditions.

[28] Petitioners' Responses to On-the-Record Requests and Items Subject to Check (dated April 4, 2008) ("Petitioners' April 4th Responses") at 9, Schedule 1.

(i.e., excluding commodity) revenues are over $1.247 billion on an annual basis.[29] Placed in that context, the PBAs offered by Petitioners are not substantial, particularly given the costs and risks that would be created by the proposed transaction.

In evaluating the PBAs proposed by Petitioners, the Staff Policy Panel concluded that "the dollar amount is entirely inadequate to compensate for costs and risks associated with this transaction." (Tr. 1456.) That Panel also concluded that the proposed amount of PBAs is "inadequate because it does not fully offset the substantial risks and costs of the transaction." (Tr. 1457.) Multiple Intervenors agrees with Staff's conclusions. The PBAs offered in the Partial Acceptance should be increased materially as a condition of merger approval.

B. Petitioners Purposefully Did Not Attempt to Identify Synergy Savings or Other Financial Benefits

In opposing the imposition of PBAs or comparable financial and rate-related benefits for customers, Petitioners assert that they "have not identified any synergistic benefits resulting from the Proposed Transaction." (Tr. 526.) Significantly, however, Petitioners purposefully did not attempt to identify synergy savings or other financial benefits.

On cross-examination, Petitioners Policy Panel conceded that they did not conduct a study of potential synergy savings that would result from the proposed transaction. (Tr. 644.) Although that Panel acknowledged that the refinancing of certain debt could result in savings, such potential savings never were studied. (Tr. 631-36.) Petitioners witness Meehan, who testified on the issue of synergy savings, admitted that he similarly did not

[29] Id.

conduct any study as to the potential synergy savings associated with the proposed transaction, nor did he ever have occasion to review such a study. (Tr. 1003-04.)

As detailed, infra, the proposed transaction, if consummated, would produce synergy savings and other financial benefits. Petitioners' failure even to examine the existence and possible level of synergy savings and/or other financial benefits has placed Staff and interveners in the unenviable – if not impossible – position of having to identify and evaluate such savings and benefits absent Petitioners' active involvement. Consequently, any failure to identify, and quantify with precision, synergy savings and/or other financial benefits that likely would result from the proposed transaction should not be construed against Staff or interveners – Petitioners are responsible for the paucity of the record on this issue.

C. The Proposed Transaction Would Produce Synergy Savings and Other Financial Benefits

Petitioners assert that "the Proposed Transaction will not result in the synergistic savings that sometimes accompany mergers where the operations of individual operating companies are combined…." (Tr. 475.) Contrary to Petitioners' assertion, the proposed transaction would in fact produce synergy savings and other financial benefits. Those savings and benefits should be captured for customers as a condition of merger approval.

As detailed, supra, Petitioners failed to conduct any studies as to the potential synergy savings and/or other benefits that could result from the proposed transaction. Consequently, the evidentiary record lacks detailed information on this issue. Nevertheless, there are many reasons why the Commission should reject Petitioners' claim of no "synergistic savings." As the Staff Policy Panel observed:

> One expects that large corporations merge because of opportunities for synergies. Otherwise, they could diversify simply by purchasing stock in other companies and avoid paying premiums above the prevailing market price of the stock. The location of corporate headquarters and operating subsidiaries in different countries has not been a barrier to synergy savings in other M&A transactions. For example, it was reported in the media that Iberdrola's recent acquisition of [Scottish Power] led to $374 ... million of synergies, which was double what was originally estimated in the merger. These synergies were achieved despite the language difference and the fact that Iberdrola's headquarters in Bilbao, Spain is over 1,000 miles from Glasgow, Scotland, the headquarters of [Scottish Power].

(Tr. 1189-90.) In fact, in an October 24, 2007 presentation on Iberdrola's 2008-2010 Strategic Plan, the acquisition of Energy East is touted because, inter alia, it "[c]omplements Iberdrola with a synergic business in its value chain."[30]

As detailed below, numerous potential sources of synergy savings and other financial benefits have been identified in this proceeding.

First, the proposed transaction may result in the realization of financial benefits related to federal production tax credits ("PTCs") applicable to certain forms of renewable electric generation. (See Tr. 1212-13.) Staff testified that the proposed transaction may allow Iberdrola, or facilitate its efforts, to take advantage of PTCs:

> [I]t can be inferred from publicly available information that currently, Iberdrola does not pay enough domestic income taxes in order to utilize the full value of its PTCs. Through the acquisition of Energy East, it will acquire taxable income

[30] See Petitioners' April 4th Responses, Attached Presentation, "Iberdrola: Strategic Plan 2008-2010" at 48 (slide 96).

> sufficient to enable it to utilize at least some and perhaps all of the PTCs it has generated.

(Tr. 1213-14.)

Although Petitioners dispute the treatment of PTCs as a potential source of synergy savings, the evidence contradicts their position. In presentations on the proposed transaction, Iberdrola identified PTCs as one of the primary benefits and motivations to acquire Energy East. (Tr. 653-54.)[31] Iberdrola also has not ruled out the possibility of utilizing Energy East income to maximize the value of PTCs. (See, e.g., Tr. 652-54.) Perhaps most tellingly, in a February 2008 publication on Iberdrola, Moody's reported that Iberdrola's proposed acquisition of Energy East would "provide it with a taxable income which it can utilise in its US renewables business which is supported by certain tax incentives." (Ex. 70 at 10.) Petitioners witness Fetter testified that Iberdrola likely provided Moody's with the above information as to the motivation underlying its acquisition of Energy East, and that such information probably was reviewed with Iberdrola shortly before the publication was issued. (Tr. 789-91.)

Second, the proposed transaction may result in the realization of financial benefits related to Spanish tax law provisions applicable to foreign investments. (See Tr. 1211-12.) Although Petitioners dispute reliance on Spanish tax benefits in this proceeding, its Policy Panel acknowledged on cross-examination that: (a) it is possible that Iberdrola would realize Spanish tax benefits from the proposed transaction; and (b) Iberdrola affirmatively would seek favorable tax treatment from Spanish authorities. (Tr. 656-57.)

[31] See also Petitioners' April 4th Responses, Attached Presentation, "Iberdrola: Strategic Plan 2008-2010" (dated October 24, 2007) at 48 (slide 96) (touting that the acquisition of Energy East "[c]onsolidates the renewable position in the US providing a taxable income").

Third, the proposed transaction may result in the realization of financial benefits related to Iberdrola's higher ratings from credit agencies compared to Energy East. As a result of such higher ratings, merger approval likely would lead to the refinancing of certain debt at interest rates below levels embedded in the existing rates of NYSEG and RG&E. (Tr. 630-32.) Such savings would not flow through to customers, however, until rates are reset. (Tr. 633-35.)

Fourth, the proposed transaction may result in synergy savings related to information technology ("IT"). For instance, the Staff Policy Panel testified that "we believe that Iberdrola may be able to consolidate [IT] systems in use at various subsidiaries." (Tr. 1208.) That conclusion was based, in part, on confidential information provided to Staff by Iberdrola. (Id.)

Fifth, the proposed transaction may result in synergy savings related to the consolidation of certain Energy East companies. The Joint Petition, for instance, indicates that Iberdrola "may seek to eliminate certain Energy East intermediate holding companies, thereby causing one or more of Energy East's operating subsidiaries to become direct subsidiaries of I[berdrola]." (Ex. 41 at 9, n.2.) The Staff Policy Panel opines that: "Such consolidations could produce synergy savings." (Tr. 1210.)

Finally, the proposed transaction may result in synergy savings that Staff and interveners have yet to identify or quantify. In opposing the imputation of synergy savings for the benefit of customers, Petitioners assert that because "Iberdrola does not have any other regulated utility interests in the region or elsewhere in the U.S. (*i.e.,* this is a 'first mover' transaction), the Proposed Transaction is not anticipated to result in any tangible and quantifiable synergistic benefits." (Tr. 503-04.) For several reasons, Iberdrola's position should be rejected.

"First mover" transactions can produce synergy savings. For instance, as detailed, supra, Iberdrola recently acquired Scottish Power in what also would qualify as a "first mover" transaction. That acquisition has resulted in significantly more synergy savings than first was estimated. (Tr. 644.) Petitioners witness Meehan acknowledged on cross-examination that synergy savings could be achieved even where a merger does not involve contiguous service territories. (Tr. 1004.) In fact, upon information and belief, prior to its acquisition of Scottish Power, Iberdrola did not own substantial – if any – operating assets in that region.

Furthermore, Iberdrola's current lack of ownership of regulated electric and gas utilities in North America does not prove that the proposed transaction would produce no synergy savings. Petitioners witness Meehan conceded that it is possible for a merger or acquisition to result in synergy savings even if the companies' operations are in different businesses. (Tr. 1005-06.) Iberdrola currently owns substantial energy-related assets in North America, including asset types also owned by Energy East (e.g., gas storage assets). (See Tr. 1169-71.) As the Staff Policy Panel concluded, Iberdrola "owns significant operating energy businesses throughout the United States. *** The size, scale, and scope of these businesses suggest that some level of synergistic savings could be achieved after the acquisition of the Energy East companies." (Tr. 1189.)

The sharing of "best practices" by Iberdrola and Energy East also may result in synergy savings and/or other financial benefits. For instance, as one of the purported benefits of the proposed transaction, Petitioners assert that: "Iberdrola will be in a position to share information regarding best practices." (Tr. 514.) Importantly, however, the sharing of best practices should be a "two-way street." As Petitioners witness Meehan acknowledged, it is possible that Iberdrola could adopt an Energy East practice as a "best practice" and, to the extent such adoption resulted in cost savings to Iberdrola, NYSEG and RG&E customers ordinarily would not benefit from those savings. (Tr. 1016-17.)

In opposing the imputation of any synergy savings, Petitioners argue that such savings automatically would flow to customers. That argument is flawed in two respects. First, customers would not benefit from synergy savings until rates are reset. (See, e.g., Tr. 998.) Inasmuch as Staff asserts that NYSEG and RG&E are realizing excessive returns (see Tr. 1202, 1365-66), it is unclear when customers actually would realize such savings. Second, as alluded to above, certain synergy savings arising from the proposed transaction may be realized by Iberdrola and/or its subsidiaries other than NYSEG and RG&E (Tr. 1016-17), in which case, absent some imputation, customers of the New York regulated utilities would not benefit from those savings.

The proposed transaction, if consummated, will result in synergy savings and other financial benefits. Indeed, Petitioners witness Meehan conceded such synergies are expected and real, but not quantifiable at this time. (Tr. 994.) The present difficulty in quantifying synergy savings and other financial benefits is due, in large part, to Petitioners' failure to conduct any studies of the potential savings and benefits. For the reasons set forth above, however, merger approval would result in the realization of synergy savings and other financial benefits which should be captured for the benefit of customers.

D. Customers Require Substantial Financial and Rate-Related Benefits for the Proposed Transaction to Be Considered in the Public Interest

As detailed extensively by the Staff Policy Panel, the proposed transaction presents numerous costs and risks for NYSEG and RG&E customers. (See, e.g., Tr. 1152-60, 1163-64, 1178-84, 1221-1364.) Consequently, in order for the proposed transaction to satisfy the public interest standard (see Point I, supra), substantial customer benefits and protections must be identified and captured. While certain desirable customer benefits and protections need not be financial in nature (e.g., more stringent reliability performance standards, robust reporting requirements), Multiple Intervenors contends that customers require substantial financial and rate-related benefits for the proposed transaction to be considered in the public interest.

In addition to the virtual certainty that the proposed transaction, if consummated, would result in synergy savings and other financial benefits of unknown (but likely substantial) magnitude (see supra), there are other reasons why customers should be accorded considerably greater financial and rate-related benefits than Petitioners have offered in the Partial Acceptance. For instance, the evidence is compelling that Energy East's New York regulated utilities are realizing returns which indicate that immediate or near-term rate relief is warranted. According to the Staff Policy Panel, NYSEG and RG&E both are earning excessive returns. (Tr. 1202.) That Panel testified that "the utilities are earning in excess of what is considered a reasonable ROE." (Tr. 1365-66.)

Staff's assertion that NYSEG and RG&E are realizing excess returns is based on its timely analysis of the return on equity ("ROE") that likely would be used to set rates for NYSEG and RG&E if those utilities' rates currently were under review by the

Commission. (See Tr. 1389-1400.) Staff asserts that, based on its analysis using the Commission's preferred ROE methodology, an appropriate estimated ROE for NYSEG and RG&E would be 9.12 percent. (Tr. 1396.) In contrast, and according to Staff's calculations: (a) NYSEG is realizing ROEs on its electric and gas operations of 13.0 percent and 15.4 percent, respectively; and (b) RG&E is realizing ROEs on its electric and gas operations of 17.0 percent and 14.96 percent, respectively. (Tr. 1647, 1721.) Based on Staff's analysis, substantial financial and rate-related benefits could be provided to NYSEG and RG&E customers and the resulting rates still would be just and reasonable.

In evaluating the appropriate level of financial and rate-related benefits for customers if the proposed transaction is approved, the Commission also should consider that: (a) Energy East's shareholders would realize a $930 million premium over the per share price at the time the proposed transaction was announced; and (b) Energy East executives and directors would receive approximately $78 million in potential payments, assuming their employment is terminated. (Tr. 1219-20.) Importantly, Multiple Intervenors is not seeking to undo, or capture, those payments (or third-party benefits) for customers. The magnitude of the payments, however, does provide additional context for determining the extent to which customers should benefit from the proposed transaction.[32]

E. Staff's Proposed One-Time Rate Adjustments Should Be Adopted or Preserved For Future Rate Proceedings

In addition to proposed PBAs that should be captured for customers if the Commission decides to approve the proposed transaction with conditions, Staff also

[32] In this regard, it is worth noting that the most of the risks identified herein with respect to the proposed transaction fall on NYSEG and RG&E customers, not shareholders.

presented a number of one-time rate adjustments applicable to NYSEG and RG&E. (See e.g., Tr. 1655-76, 1729-37.) The Commission should consider adopting all or most of Staff's adjustments in this proceeding.[33] In addition to generally being meritorious, the resolution of Staff's one-time adjustments in favor of customers, and the concomitant elimination of future controversy surrounding them, could be construed as a public benefit, thereby helping to justify approval of the proposed transaction. If, arguendo, the Commission is not inclined to approve the one-time adjustments at this time, they should be preserved for consideration in future rate proceedings.

In explaining the inclusion of one-time adjustments relating to RG&E, Staff witness Haslinger testified that:

> This shows that there are significant unresolved regulatory liabilities associated with Energy East that Iberdrola would not be aware of. We are putting Iberdrola on notice that we intend to pursue these adjustments in the near future. Further, presentation of this information at this time provides further support that RG&E's electric rates are too high since significant customer credits will be enabled that can be used to reduce or stabilize those rates, in the absence of the proposed acquisition.

(Tr. 1655.) Staff witness Benedict advanced a similar explanation in testimony for one-time adjustments relating to NYSEG. (Tr. 1756.)

Importantly, if the Commission elects to refrain from adopting Staff's one-time adjustments in this proceeding, it should rule that such adjustments are preserved for consideration in future NYSEG and RG&E rate proceedings.

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[33] Multiple Intervenors' general support for Staff's one-time adjustments in the context of this proceeding should not be interpreted as support for each and every individual adjustment, either herein or in a subsequent proceeding unrelated to the proposed transaction.

F. Financial Benefits to Customers Should Be Used to Reduce Delivery Rates in the Near-Term

In determining the level of financial benefits, or PBAs, upon which merger approval should be conditioned, the Commission should recognize that certain benefits would have an immediate impact on rates paid by customers, while other benefits would not be realized or captured by customers until rates are reset. For the reasons set forth below, financial benefits to customers should be used to reduce delivery rates in the near-term.[34]

The proposed transaction would impose numerous risks on customers that, hopefully, would be outweighed by tangible, financial benefits. The imposition of risks on customers would take effect upon consummation of the merger. Accordingly, equity dictates that customers should realize the financial benefits of the transaction at the same time they are exposed to the risks (i.e., immediately upon merger closing).

Additionally, energy prices in New York are very high, and based on Staff's analysis, NYSEG and RG&E are earning returns well above levels that would be authorized today if rates were reset. (Tr. 1202, 1365-66, 1647, 1721.)[35] Accordingly, the need for near-term rate relief is highly compelling, and should not be delayed unnecessarily.

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[34] Multiple Intervenors' use of the phrase "delivery rates" in this context is meant to include generation-related costs (stranded or otherwise) recovered from NYSEG and RG&E delivery customers through a non-bypassable charge ("NBC"). For instance, while the write-off of certain generation-related costs would not lead to a reduction in base delivery rates, it would lower the NBC imposed on delivery customers, thereby providing an immediate benefit.

[35] In 2007, the average electricity price for all sectors in the United States was 8.91 cents per kWh. The comparable electricity price in new York in 2007 was 15.04 cents per kWh, approximately 69 percent higher than the national average. Last year, only Connecticut and Hawaii had a higher average electricity price than New York. In fact, while New York's average electricity price exceeded 15 cents per kWh in 2007, 36 states had comparable average electricity prices under 10 cents per kWh, and 23 states had average

If the Commission elects to identify specific PBAs upon which to condition merger approval, it should accord priority to those PBAs that would reduce delivery rates, including the NBC, in the near-term. Absent such priority, there are certain PBAs which would not benefit customers until rates are reset, which may not occur until well after merger closing.

G. Merger Approval Should Be Conditioned on a Two-Year Stay-Out Agreement by NYSEG and RG&E

Existing rate plans governing NYSEG's gas operations and RG&E's electric and gas operations are scheduled to expire on December 31, 2008. (Tr. 1648, 1651, 1727.) There is no rate plan governing NYSEG's electric operations. (See Tr. 1722-23.) Thus, both NYSEG and RG&E currently are eligible to file new electric and/or gas rates.[36] From Multiple Intervenors' perspective, rate proceedings involving NYSEG and/or RG&E, wherein customers are exposed to the risk of even higher delivery rates, would be particularly unwelcome in the period immediately following Commission approval of Iberdrola's acquisition of Energy East (with conditions). For several reasons, merger approval should be conditioned on a stay-out agreement pursuant to which neither NYSEG nor RG&E would be permitted to seek higher delivery rates for a minimum period of two years.

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electricity prices under 7.5 cents per kWh (i.e., less than half that of New York). Energy Information Association, Average Retail Price of Electricity to Ultimate Consumers by End-Use Sector, by State (Report Released March 17, 2008).

[36] As a practical matter, it probably is unlikely that NYSEG or RG&E would file a rate case while this proceeding is pending. Significantly, however, absent some stay-out agreement, the utilities would be within their rights to seek delivery rate increases at any time, including shortly after the Commission rules herein.

Initially, the Commission should be concerned about the public reaction to possibly-imminent rate filings by NYSEG and/or RG&E. Petitioners have promoted the proposed transaction as being in the public interest. (See generally Ex. 41.)[37] If merger approval is granted by the Commission, even if subject to conditions, that decision presumably would be based on a finding that the benefits of the transaction exceed the costs and risks. Under such circumstances, it would not be in the public interest if, shortly following merger approval, NYSEG and/or RG&E were to file for increased delivery rates, thereby potentially offsetting whatever financial benefits were identified for customers in this proceeding.

To the extent financial benefits to customers are used to reduce rates in the near-term, as advocated by Multiple Intervenors, supra, a rate freeze would have the effect of "locking in" those benefits for a multi-year period. Furthermore, to the extent the Commission may be concerned about reductions to base delivery rates necessitating larger future rate increases (i.e., sometimes referred to as the "hockey stick effect"), use of a rate freeze could: (a) maximize rate relief to customers in a manner preferable to a larger rate decrease followed by an immediate rate filing; and (b) promote rate stability.[38]

In this proceeding, Petitioners have not proposed to freeze utility delivery rates – electric or gas – for any particular period of time. (See, e.g., Tr. 615-16.) Significantly, however, Petitioners acknowledged on cross-examination that they presently have no plans

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[37] Petitioners also have represented that "there will be no change to the rates, terms or conditions of service provided to NYSEG and RG&E customers in connection with the Proposed Transaction." (Id. at 16.)

[38] Reductions to NBC-related costs similarly would not place future, upward pressure on rates.

to file rate cases on behalf of NYSEG or RG&E. (Tr. 618-19.) That acknowledgement raises two points. First, although Petitioners' plans may be considered beneficial, plans and intentions differ materially from binding enforceable commitments. Second, if the Commission were to condition merger approval upon, inter alia, a stay-out agreement of one-year or, preferably, two-years, such condition should not frustrate Petitioners' stated plans with respect to NYSEG and RG&E.

Importantly, Multiple Intervenors' advocacy for a two-year rate freeze is conditioned upon financial and other rate-related benefits being flowed through to customers in the near-term. If, arguendo, the Commission were to approve the proposed transaction without ensuring that customers' financial benefits are realized upon merger closing, then it might be more advantageous to couple such approval with the issuance of an order requiring NYSEG and RG&E to show cause as to why existing rates should not be reduced.

For all the foregoing reasons, merger approval should be conditioned upon the provision of substantial financial and rate-related benefits to customers.

POINT III

MERGER APPROVAL SHOULD BE CONDITIONED UPON THE IMPLEMENTATION OF MORE STRINGENT ELECTRIC AND GAS RELIABILITY, SERVICE QUALITY AND SAFETY PERFORMANCE STANDARDS AND REVENUE ADJUSTMENTS

Reliability, service quality and safety are extremely important to customers. Due to the energy-intensive nature of their respective businesses, Multiple Intervenors members are particularly dependent upon very reliable electric and gas service. The proposed transaction, which, if approved, would result in a new corporate parent for NYSEG and RG&E, and potentially place increased financial pressure on those utilities, has raised concerns regarding future reliability, service quality and safety performance. (See, e.g., Tr. 1205-06.) Notwithstanding those concerns, Petitioners have opposed proposals to implement new or more stringent performance standards or revenue adjustments related to reliability, service quality and safety. (See Tr. 119-20, 145, 203.) For the reasons set forth below, Petitioners' opposition to such proposals should be rejected – the Commission should condition merger approval upon the implementation of more stringent reliability, service quality and safety performance standards and revenue adjustments.

A. Petitioners Cannot Have It Both Ways

Throughout this proceeding, Petitioners have relied upon Iberdrola's claimed experience and expertise in terms of reliability and service quality – particularly electric reliability – as a purported benefit of the proposed transaction. (See, e.g., Tr. 145, 253, 490-91, 505; Ex. 41 at 15-16.) Petitioners claim that reliability, customer service and safety would remain top priorities following Iberdrola's acquisition of Energy East. (Tr. 513.) Petitioners, however, also have: (a) refrained from committing to any quantifiable improvements in electric or gas reliability, service quality, or safety performance (see Tr. 636); and (b) opposed all proposals to implement more stringent performance standards and/or revenue adjustments relating to reliability, service quality and safety.[39] Petitioners cannot have it both ways – either the proposed transaction would lead to real improvements

[39] The Staff Policy Panel observed that: "There are no terms and conditions in the acquisition that ensure increased or enhanced service quality, safety or reliability in the future. More troubling is that [P]etitioners did not put forward any provisions to prevent backsliding after the rate plans/orders expire." (Tr. 1205-06.)

in terms of reliability, service quality and/or safety, or it would not (in which case the Commission should focus on how best to avoid "backsliding").

Importantly, absent the implementation of more stringent performance standards and/or revenue adjustments, the proposed transaction should be evaluated as producing absolutely no benefits with respect to reliability, service quality and safety. As detailed, supra, the Staff Policy Panel testified that "benefits which are not readily enforceable … have no value because there is no substantive way to ensure that the post-acquisition companies will live up to them." (Tr. 1197.) As also detailed, supra, Commissioner (then Chairwoman) Acampora, speaking for the Commission, noted with respect to the National Grid/KeySpan merger that: "We act on guarantees, not promises."[40]

Petitioners have not demonstrated that the Iberdrola/Energy East transaction, as proposed, would result in any benefits for NYSEG and RG&E customers with respect to electric and gas reliability, service quality and safety. Petitioners also have failed to proffer any meaningful commitments that performance in those critically-important areas would not decline following merger closing. These failures must be remedied in conditions established by the Commission for merger approval.

B. The Relevance of the Niagara Mohawk Experience

In testimony, Petitioners attempt repeatedly to distinguish the performance of NYSEG and RG&E with that of Niagara Mohawk Power Corporation d/b/a National Grid ("Niagara Mohawk"), particularly with respect to electric reliability. (See, e.g., Tr. 130-31, 148-49, 203-04.) While the performance of NYSEG and RG&E with respect to reliability, service quality and safety admittedly is different from that of Niagara Mohawk, the

[40] Commission Session, August 22, 2007, Transcript at 81.

significance of the comparison is that Niagara Mohawk's performance – particularly with respect to electric reliability – declined following its acquisition by another company (i.e., National Grid).[41] Indeed, Petitioners even acknowledge that Niagara Mohawk's quality of service has declined since it was acquired by National Grid. (Tr. 131.)

Based on its concerns regarding the impact of a merger on reliability, service quality and safety, the Commission imposed more stringent performance standards and revenue adjustments on Niagara Mohawk and KeySpan's gas utilities as a condition to approval of the National Grid/KeySpan merger.[42] More stringent performance standards and revenue adjustments similarly are needed here to ensure that Iberdrola's acquisition of Energy East, if approved, does not lead to declining performance by NYSEG and/or RG&E in the important areas of reliability, service quality and safety.

C. The Implementation of More Stringent Reliability, Service Quality and Safety Performance Standards and Revenue Adjustments Would Constitute a Benefit

Multiple Intervenors supports the positions of certain parties – particularly Staff – advocating for the implementation of more stringent reliability, service quality and safety performance standards and revenue adjustments as a condition of merger approval. As the Staff Policy Panel testified:

> The existing rate plans [of NYSEG and RG&E] should be further modified to ameliorate the potential for increased risk to electric system and gas system reliability. Additional changes are also needed to ensure that gas safety and customer service quality are maintained going forward.

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[41] See, e.g., Commission Session, August 15, 2007, Transcript at 152.

[42] Case 06-M-0878, supra, National Grid Order at 143-49.

(Tr. 1366.) Staff sponsored testimony advocating for more stringent performance standards and/or revenue adjustments in the areas of electric and gas reliability, service quality and safety. (See, e.g., Tr. 1799-1839, 1856-62, 1871-84.)[43]

The performance standards and revenue adjustments advanced by Staff, if adopted, would produce customer benefits strengthening contentions that the proposed transaction is in the public interest. For instance, the Staff Gas Safety Panel testified that:

> The purpose of our testimony is to recommend safety performance targets which become incentives for NYSEG and RG&E to maintain and improve specific areas regarding the safety of each gas distribution system. The targets also focus the company's attention to areas widely accepted as of high importance, and help ensure service reliability.

(Tr. 1799.)[44] The Panel advanced numerous reasons why increased revenue adjustments should be adopted. (Tr. 1836-38.)

Similarly, the Staff Electric Reliability and Safety Panel testified that based on prior Commission decisions, in a transaction involving New York electric and gas utilities, maintaining reliability of service subsequent to the transaction is of paramount concern. (Tr. 1858-59.) The Panel recommended that Commission decisions in the National Grid/KeySpan merger proceeding increasing potential revenue adjustments when utility

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[43] Multiple Intervenors advocates no position on the specific performance standards and revenue adjustments that should be adopted as conditions in this proceeding. Generally, Multiple Intervenors supports Staff's efforts to make existing performance standards and revenue adjustments more stringent to promote improved performance and discourage backsliding.

[44] The Panel also testified that current safety-related performance targets for NYSEG and RG&E are not adequate. (Tr. 1800.) A number of those standards were established many years ago and have not been updated. (See, e.g., Tr. 244.)

performance is unsatisfactory and imposing additional, reliability-related reporting requirements also be applied to NYSEG and RG&E. (Tr. 1859-62.)

The Staff Consumer Services Panel also testified that:

> We recommend certain measures that if adopted could provide enhanced consumer benefits and protections should Iberdrola acquire Energy East and its affiliated local distribution companies (LDCs) NYSEG and RG&E. Specifically, the Commission should direct the continuation and expansion of customer service performance incentives for NYSEG and RG&E ....

(Tr. 1871.) The Panel explained that the purpose of performance standards and revenue adjustments are to "align shareholder and ratepayer interests by providing earnings consequences to shareholders for the quality of service provided by a utility to its customers." (Tr. 1872.)

Importantly, Petitioners' own witnesses acknowledge the potential benefits of more stringent performance standards and revenue adjustments. For instance, Petitioners Gas Safety and Reliability Panel testified that performance standards, coupled with revenue adjustments, have the following effect: "you make sure you don't miss your performance targets." (Tr. 246.) The Panel acknowledged that if potential revenue adjustments are increased, that would provide an additional incentive not to "miss" performance standards. (Id.) Finally, the Panel conceded that at least some of the more stringent performance standards recommended by Staff, if adopted, could be interpreted as a benefit of the merger. (Tr. 252.)

As addressed in Point II, supra, as well as the testimony of the Staff Policy Panel, the proposed transaction raises numerous risks. For the reasons set forth in Point I, supra, those risks must be more than offset by tangible benefits for the transaction to satisfy the public interest standard. With respect to electric and gas reliability, service quality and safety, the proposed transaction raises risks but offers no tangible benefits. In evaluating possible conditions to merger approval, the Commission should not overlook those important aspects of utility performance. If, for example, more stringent reliability, service quality and safety performance standards and revenue adjustments were implemented as a result of this proceeding, they would constitute meaningful benefits upon which merger approval could, in part, be justified.[45]

D. Merger Approval Also Should Be Conditioned on the Maintenance of Existing Manpower Levels at NYSEG and RG&E

Multiple Intervenors is concerned that if existing manpower levels at NYSEG and RG&E are reduced as a result of the proposed transaction, electric and gas reliability, service quality and safety performance may suffer. In addition to the adoption of more stringent performance standards and revenue adjustments, the Commission should condition merger approval on the maintenance of existing manpower levels at NYSEG and RG&E for some reasonable period (e.g., three years) following the transaction. Such a condition, if imposed, generally would be consistent with Iberdrola's stated intentions.

Petitioners Policy Panel testifies that "Iberdrola has committed that existing employee compensation and benefits will remain substantially unchanged for a period of at least eighteen months after consummation of the Proposed Transaction." (Tr. 524.) That Panel also testified that no job losses were anticipated as a result of the proposed

[45] In the Joint Petition, Petitioners tout that Iberdrola "is committed to excellence in customer service and reliability and understands the need for infrastructure to support the goal on enhanced reliability." (Ex. 41 at 15.) It is incumbent upon the Commission to ensure Iberdrola's claimed commitment is reflected in conditions that are enforceable.

Iberdrola/Energy East merger. (Id.) When questioned as to the scope of the commitments being offered, Petitioners Policy Panel acknowledged that manpower levels at NYSEG and RG&E could in fact change – either up or down – following merger approval. (Tr. 637-42.) For instance, the Panel agreed that, although inconsistent with expectations, Iberdrola would not be precluded from reducing manpower by, for example, 10 percent. (Tr. 639.)

Multiple Intervenors is concerned that, notwithstanding Petitioners' intentions, manpower at NYSEG and/or RG&E may decline due to, inter alia, merger-related retirement incentives, decisions purportedly unrelated to the merger, and job attrition that is not equaled by new hires. A reduction in manpower could have detrimental impacts on reliability, service quality and safety.

Inasmuch as customers are very concerned about reliability, service quality and safety, and Petitioners claim that the proposed transaction would not result in job losses, the Commission should consider requiring NYSEG and RG&E to maintain existing manpower levels for some reasonable period of time following consummation of the proposed transaction. In particular, NYSEG and RG&E should be encouraged to maintain, if not increase, manpower assigned to positions impacting electric reliability.

POINT IV

MERGER APPROVAL SHOULD BE CONDITIONED UPON THE ADOPTION OF FINANCIAL PROTECTIONS FOR CUSTOMERS

As detailed more fully below, the proposed transaction would expose customers of NYSEG and RG&E to a myriad of financial risks. (See generally Tr. 1221-25, 1277-1325, 1400-19.) Therefore, merger approval should be conditioned upon Iberdrola's acceptance of financial protections for customers.

A. The Proposed Transaction Would Expose Customers to Financial Risks

The proposed transaction, if consummated, would expose NYSEG and RG&E customers to at least four different types of financial risk.

First, the proposed transaction would increase the amount of goodwill on Iberdrola's books. As structured, Iberdrola would retain the goodwill arising from the transaction. Iberdrola estimates that the transaction would result in approximately $1.4 billion of incremental goodwill, which would increase the total amount of goodwill recorded on the consolidated books of Iberdrola to $13.4 billion. (Tr. 1317-18.) Including goodwill associated with the acquisition of Energy East, 46 percent of the equity of Iberdrola would consist of goodwill and other intangible assets. (Tr. 1325.) Because goodwill associated with regulated utilities generally begins to suffer from impairment relatively quickly, it likely soon would become necessary to write down the goodwill and, accordingly, to take a charge against Iberdrola's earnings. (Tr. 1319-21.) This would result in a reduction in the amount of company equity and, according to Staff, likely would compel Iberdrola to assume more debt. (Tr. 1325.) Therefore, the fact that almost half of Iberdrola's equity would consist of goodwill and other intangible assets creates a risk of increased costs to NYSEG and RG&E customers.[46]

[46] The Staff Policy Panel testified that "the massive amount of Goodwill recorded on the books of Iberdrola is a major concern affecting whether this acquisition should be approved." (Tr. 1318.)

Second, analysis of the transaction, recent financings of other acquisitions, and the aggressive policy of expansion pursued by Iberdrola all have led Staff to conclude that Iberdrola is likely to experience a credit downgrade. (Tr. 1285.) In support of that conclusion, S&P and Moody's each recently downgraded Iberdrola credit by one notch. (Tr. 1290.) Also, those credit rating agencies placed both NYSEG and RG&E on negative outlook in response to, inter alia, concerns arising from the proposed transaction. (Id.) Moreover, Iberdrola's pro forma debt ratio of 58 percent implies a BBB bond rating, which would represent a downgrade and effectively would eliminate one purported benefit of the transaction – access by NYSEG and RG&E to cheaper capital by virtue of Iberdrola's stronger credit rating. (Tr. 1291.) A further decline in Iberdrola's credit rating, combined with its aggressive capital investment program and payment for the acquisition of Energy East, could combine to threaten the NYSEG and RG&E credit ratings and increase those utilities' financing costs. (Tr. 1297-98.)

Third, NYSEG and RG&E are financially healthy companies that present to Iberdrola an attractive source of funds for assisting weaker affiliates or to boost dividends to Iberdrola shareholders. (Tr. 1405-06.) Consequently, there is at least some risk that Iberdrola would use NYSEG and/or RG&E as a source of money for purposes not related to the provision of safe and adequate service to those companies' customers.

Finally, Staff expressed its concern that, under certain circumstances, Iberdrola could force NYSEG and RG&E into bankruptcy in order to satisfy debts of the corporate parent. (Tr. 1417.) According to Staff, directors of the subsidiary must follow the orders of its corporate parent. (Tr. 1414.) Therefore, to protect NYSEG and RG&E customers against the harm that would result from this worst-case scenario, conditions on merger approval should include safeguards against a forced bankruptcy.

B. Staff's Proposed Financial Protections

Staff proposed a number of measures designed to protect NYSEG and RG&E customers from financial risks related to the proposed transaction. (See Tr. 1400-19.) The protections advanced by Staff are necessary, and should be adequate, to shield customers from adverse financial consequences arising from Iberdrola's acquisition of Energy East. Multiple Intervenors advocates that merger approval be conditioned on Iberdrola's acceptance of those financial protections.

The financial protections that should be adopted as merger conditions in this proceeding include, at a minimum, provisions relating to: (a) the treatment of goodwill arising; (b) credit quality conditions; (c) dividend limitations; (d) money pool rules; and (e) structural protections. These protections are discussed below.

Initially, Staff recommended that the goodwill and transaction costs of the proposed transaction, if consummated, not be reflected on the books of Energy East, NYSEG or RG&E. (Tr. 1402.) Moreover, Staff recommended such goodwill and transaction costs be excluded from any determination of rates and earned returns for NYSEG and RG&E. (Id.) Finally, Staff proposed that if an impairment test is performed on goodwill, Iberdrola should be required to provide the results of each such test to the Commission on an annual basis. (Tr. 1403.)

Staff proposed four measures to protect customers from a deterioration in the credit quality of Iberdrola, Energy East, NYSEG and/or RG&E. First, Staff recommended requiring an independent risk assessment by obligating Iberdrola, Energy East, NYSEG and

RG&E to maintain securities credit ratings with both S&P and Moody's. (Tr. 1403-04.) Second, Staff asserted that each of those companies should be required to state a goal of maintaining the ratings of their securities at the investment grade level. (Tr. 1404.) Third, Staff recommended that the companies be required to provide the Commission with copies of presentations to credit agencies, including the backup to such presentations, which would provide greater insight into the financial health of the companies. (Tr. 1404-05.) Finally, Staff recommended that any credit rating downgrade suffered by NYSEG or RG&E should trigger the need to file with the Commission a plan to counteract the downgrade. (Tr. 1405.)

Next, Staff expressed its concern that Iberdrola could drain capital from NYSEG or RG&E, either to support Iberdrola (or an affiliate thereof) or to increase dividends to shareholders. (Tr. 1405-06.) To counteract the risk that capital would be siphoned from NYSEG and/or RG&E, Staff proposed certain restrictions on the amount of dividends that those companies would be allowed to send up the corporate chain. (Tr. 1406.) Staff also recommended restricting the conditions under which NYSEG and RG&E could issue dividends, as well as restricting the total value of dividends issued. (Tr. 1406-08.) Moreover, Staff recommended that in response to a dividend restriction, NYSEG and RG&E should be barred from transferring, lending or leasing any asset or right of value to any affiliate unless the Commission approves such transfer. (Tr. 1408.)

Staff also identified a potential risk to NYSEG and RG&E customers arising from the participation of those companies in a money pool. To counter such risk, Staff recommended limiting to lender status Iberdrola's participation in a money pool with domestic regulated entities. (Tr. 1409.) Staff also recommended that NYSEG and RG&E be prohibited from: (a) participating in a money pool with any non-regulated foreign entity; and

(b) indirectly loaning money to any affiliate. (Id.) According to Staff, NYSEG and RG&E should not be permitted to be affected by any cross-default provision, either now or in the future. (Tr. 1410.)

Finally, Staff advocated for the imposition of structural protections in addition to the financial covenants described above. Specifically, Staff asserted that perhaps the most important financial protection that should be imposed as a condition of merger is the creation of a limited purpose entity ("LPE"). (Tr. 1413.) Briefly, an LPE is a permanent addition to the corporation that has a director independent from the corporate parent and exists to perform one specific task. (Id.) The independent director of the LPE would represent the public interest of NYSEG and RG&E (i.e., customers and debt holders) and is intended, in part, to protect against a corporate parent forcing its subsidiary into bankruptcy. (Tr. 1414.) The LPE essentially would be equivalent to the "golden share" that was imposed as a condition of merger approval for KeySpan and National Grid, and is similar to protections imposed in other jurisdictions. (Tr. 1415–16.)

In authorizing National Grid's acquisition of KeySpan last year, the Commission conditioned merger approval on, inter alia, acceptance of numerous financial conditions intended to protect customers of the effected New York regulated utilities.[47] In this proceeding, the Staff Policy Panel testified that its proposed financial protections for customers are no more stringent than those adopted previously by the Commission in Case 06-M-0878. (Tr. 1403, 1405, 1408, 1410, 1419.)

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[47] Case 06-M-0878, supra, National Grid Order at 122-27.

C. Petitioners' Response to Staff's Proposed Financial Protections

Petitioners raised numerous objections to Staff's proposed financial protections. Petitioners' response on this issue is summarized briefly below. As detailed, infra, Petitioners' response, if adopted, would not protect customers adequately against the financial risks raised by the proposed transaction.

With respect to potential negative impacts associated with goodwill, Petitioners argued that Staff's concerns are unfounded. Petitioners Policy Panel contended that goodwill is not a primary indicator of a company's risk profile. (Tr. 546.) That Panel also argued that pursuant to International Financial Reporting Standards ("IFRS") and Generally Accepted Accounting Principles ("GAAP") used in the United States, goodwill is accounted for at the level of cash generating units. (Tr. 547.) As a result, Petitioners asserted that goodwill only would be impaired by a reduction in expected future cash flows, a result the Panel claimed is highly unlikely. (Id.) Petitioners did, however, agree with Staff on one point regarding the treatment of goodwill – Petitioners reiterated their prior commitment not to record any merger-related goodwill on the books of Energy East, NYSEG or RG&E. (Id.)

On the issue of credit quality risks, Petitioners argued that Staff was incorrect in its characterization of how credit rating agencies regard Iberdrola. (Tr. 552.) Petitioners contend that Iberdrola currently possesses a strong credit rating, the status of which is not in question, and that it already reflects an evaluation of Iberdrola's capital structure and capital investment program. (Tr. 553.) Petitioners Policy Panel also attempted to distinguish the proposed transaction from the National Grid/KeySpan merger and, in so doing, argued that the same credit issues are not present here. (Id.) Although Petitioners contended that the likelihood of a credit downgrade is small, they agreed to the following Staff proposals: (a) the goal of maintaining existing credit ratings; (b) the reporting of any credit downgrades, along with the filing of a plan to remedy same; (c) providing the Commission with confidential copies of all presentations to credit ratings agencies; and (d) exempting NYSEG and RG&E customers from responsibility for any increase in the cost of debt for those companies resulting from Iberdrola's financial status. (Tr. 553–54.)

Petitioners disputed Staff's concern that the resources of NYSEG and RG&E could be drained through dividends aimed at supporting Iberdrola or weaker subsidiaries, or to maximize shareholder profit. According to Petitioners Policy Panel, Iberdrola published its dividend policy as part of a strategic plan for the period 2008–2010. (Tr. 555.) The strategic plan was evaluated by credit rating agencies, and, therefore, purportedly should not represent a concern in this proceeding. (Id.) Regardless, Petitioners stated that NYSEG and RG&E would maintain their respective dividend policies without regard to the financial performance and needs of Iberdrola. (Tr. 557.)

Similarly, although Petitioners disputed the validity of Staff's concerns, they agreed to limit the participation of NYSEG and RG&E in money pools. (Tr. 556.) Specifically, Petitioners represented that absent Commission authorization, NYSEG and RG&E only would participate in Iberdrola money pools in which the other participants are limited to regulated utilities. (Tr. 556–57.) Petitioners also agreed that Iberdrola would forego borrowing from money pools in which NYSEG and RG&E are participants. (Tr. 557.)

Finally, Petitioners rejected as "extreme" the Staff recommendation to adopt an LPE or golden share. (Tr. 558.) According to Petitioners, Iberdrola is stronger and more financially stable than Energy East, and that such financial strength: (a) represents a benefit to NYSEG and RG&E; and (b) distinguishes the proposed transaction from the National Grid/KeySpan merger. (Tr. 557.) Petitioners contend that there are no potential credit issues raised by the proposed transaction and, therefore, no need to protect NYSEG and RG&E customers by from such issues by implementing measures such as a golden share. (Tr. 558.)

D. The Financial Protections Proposed by Staff Should Be Adopted in This Proceeding

Staff proposed a series of provisions intended to protection NYSEG and RG&E customers from certain identified financial risks raised by the proposed transaction. Not surprisingly, Petitioners dispute the notion that the proposed transaction creates any financial risks to customers. To their credit, Petitioners have indicated a willingness to accept many – but not all – of the financial protections proposed by Staff. Importantly, however, Petitioners rejected two Staff proposals that, for the reasons set forth below, should be adopted as conditions of merger approval in this proceeding.

First, Staff recommended that an LPE, similar to a golden share, be created to facilitate the effectiveness of the other financial protections. (Tr. 1413.) Staff asserted that the LPE is "perhaps the most important tool that the Commission can use to isolate NYSEG and RG&E from the risks of Iberdrola." (Tr. 1417.) Staff also contended that the LPE would facilitate compliance with dividend and money pool restrictions. (Id.) An LPE would provide customers with additional, and desirable, financial protections against the possibility of NYSEG and/or RG&E being forced into bankruptcy as a result of Iberdrola's financial condition. Importantly, Petitioners have failed to identify any substantial harm in adhering to Staff's proposal. Indeed, if the prospects of an Iberdrola bankruptcy are as remote as claimed by Petitioners, the LPE proposed by Staff should not have the slightest impact on Iberdrola's future operations.

Second, NYSEG and RG&E should be prohibited from issuing dividends unless they meet or exceed a threshold credit rating. Petitioners' proposal merely to continue NYSEG and RG&E's dividend policies does not provide sufficient protection for customers. For instance, such policies could be changed in the future – for example, subsequent to a credit downgrade. Relying merely on adherence to policies is difficult to enforce because those policies could change. On the other hand, an established prohibition against the issuance of dividends if a specified minimum credit rating is not maintained would be enforceable, and ensure that resources are not drained from NYSEG and RG&E at an inappropriate time. Similar to the Staff-proposed LPE, the recommended dividend restrictions should not come into play, at all, if Petitioners' perspective on the financial benefits accorded by the proposed transaction come to fruition. If, however, Petitioners are wrong, or circumstances change for the worse, the dividend restrictions proposed herein could provide valuable protection to customers.

In summary, Petitioners agreed to accept a number of financial protections proposed in this proceeding as conditions of merger approval. Those protections include the following: (a) merger-related goodwill would not be reflected on the books of NYSEG or RG&E (Tr. 547); (b) maintenance of NYSEG and RG&E credit ratings (Tr. 554); (c) the reporting of a NYSEG or RG&E credit downgrade and the filing of a plan to remedy same (id.); (d) providing the Commission with confidential copies of all presentations to credit ratings agencies (id.); (e) shielding NYSEG and RG&E customers from responsibility for any increase in the cost of debt for those companies resulting from Iberdrola's financial condition (id.); (f) NYSEG and RG&E would maintain their respective dividend policies without regard to the financial performance and needs of Iberdrola (Tr. 557); (g) limitations on the participation of NYSEG and RG&E in money pools (Tr. 556–57); (h) transaction costs would not be recovered from NYSEG and RG&E customers through rates (Tr. 562); (i) NYSEG and RG&E would be prohibited from transferring or selling material assets or facilities to Iberdrola or any affiliate thereof, absent Commission authorization (Tr. 560). Petitioners' acceptance of these financial protections should be a condition of merger approval.

Additionally, for the reasons detailed above, Petitioners' refusal to consent to protections related to an LPE and dividend restrictions should be rejected. If, arguendo, the Commission declines to adopt the full panoply of customer protections proposed by Staff, it should insist upon greater financial and rate-related benefits for NYSEG and RG&E customers to help offset the unmitigated financial risks resulting from the proposed transaction.

POINT V

MERGER APPROVAL SHOULD BE CONDITIONED UPON THE ADOPTION OF ROBUST REPORTING REQUIREMENTS

If the proposed transaction is consummated, one outcome is that Energy East no longer would be subject to certain Federal laws and national accounting standards. The net result would be to diminish the transparency of its operations and make it more difficult for the Commission and Staff to evaluate costs and other financial information presented by NYSEG and RG&E. Such lack of transparency also would impede the efforts of interveners in Commission proceedings involving the rates of NYSEG and/or RG&E. (See generally, Tr. 1239-47, 1342-52.) To protect customers against the risks, including the potential for abuse, that arise from this potential loss of transparency, the Commission should condition merger approval upon Iberdrola's acceptance of robust reporting requirements.

A. The Proposed Transaction Would Create Risks Regarding the Transparency of Information Relevant to the Regulation of NYSEG and RG&E

The Staff Policy Panel raised several important concerns relating to changes in the information that would be reported and available to the Commission and Staff if Iberdrola acquires Energy East. For instance, the Staff Policy Panel testified that "the combination of companies will create increased risks and opportunities for abuses that cannot be detected by regulators." (Tr. 1239.) Although Petitioners have offered certain commitments to continue providing regulatory reports, such reports apparently would not provide information or details on the activities of the service, or holding companies, or other business interests of Iberdrola. (Id.) According to the Staff Policy Panel, such information is essential for Staff to evaluate whether the utility has stated its costs fairly. (Tr. 1240.)

The Staff Policy Panel described four reporting-related issues that would present a risk to customers if Energy East is acquired by Iberdrola. First, Energy East would become a subsidiary of Iberdrola and would be removed from the jurisdiction of the Securities and Exchange Commission ("SEC"). (Tr. 1342.) As a result, Energy East no longer would be required to file SEC reports. (Id.) Additionally, certain reporting requirements applicable to Energy East might not apply to Iberdrola. (Tr. 1342-43.)

Second, passage of the Public Utility Holding Company Act of 2005 ("PUHCA 2005") effectuated a transfer of holding company audit responsibility from the SEC to the Federal Energy Regulatory Commission. (Tr. 1343-44.) Additional reporting requirements of the SEC also would be eliminated as a result of the proposed transaction. (Id.) The Staff Policy Panel testified that Staff has relied on the SEC reports for certain information not reported elsewhere. (Tr. 1345-46.)

Third, as a subsidiary of Iberdrola, Energy East would be governed by the IFRS and not the GAAP. The two accounting standards are very different. (Tr. 1348.) A switch to the IFRS accounting standards would reduce the financial information available to Staff, thereby diminishing the transparency of NYSEG and RG&E operations and hampering efforts to regulate those utilities effectively. (Id.) According to the Staff Policy Panel, this concern is heightened by Iberdrola's use of special purpose entities ("SPEs"), which are subsidiaries formed to achieve one specific goal. (Id.) Importantly, however, SPEs also can be used to obfuscate the financial health of a utility holding company. (Tr. 1348–49.) The Staff Policy Panel testified that: "The presence of SPEs lends a complexity to Iberdrola's operations that potentially could make ratemaking difficult." (Tr. 1349.)

Fourth, Energy East would not remain subject to the Sarbanes-Oxley Act ("SOX") if it is acquired by Iberdrola. (Tr. 1351.) The Staff Panel testified that: "There may be a reduction of internal controls and regulatory oversight due to the loss of SOX protections. (Tr. 1352.)

Thus, the proposed transaction, if consummated, would increase risks to customers due to a loss of transparency compared to existing, applicable report requirements. Summarizing its concerns, the Staff Policy Panel indicated that: "We are concerned that there will be a significant reduction in the Commission's ability to acquire a complete picture of Iberdrola's operations because of the company's status as a foreign holding company operating under IFRS rules and the repeal of the Public Utility Holding Company Act of 1935." (Id.)

B. Staff's Proposed Reporting Requirements

To mitigate the risks associated with reduced financial transparency that could result from the proposed transaction, Staff proposed five reporting requirements to ensure that it, and the Commission, would have access to the information necessary to regulate NYSEG and RG&E. First, Staff recommended that Iberdrola make available, within New York State and in English, copies of the books and records of Iberdrola and its majority owned affiliates. (Tr. 1432.) Second, Staff recommended that NYSEG and RG&E be obligated to continue satisfying their currently-applicable reporting requirements, including those required by SOX. (Tr. 1432–33.) Third, Staff proposed to continue the annual audit of Energy East, NYSEG and RG&E by an independent auditor. (Tr. 1433.) Fourth, Staff asserted that the requirements imposed on NYSEG by an August 16, 2000 information order in Case 9187 be continued and also extended to RG&E. (Tr. 1434.) Fifth, Staff advocated that Iberdrola be required to report certain financial information annually, for itself as well as Energy East and its direct subsidiaries, and that such filings reflect audited GAAP financial statements in U.S. dollars. (Tr. 1435-36.)

According to Staff, the recommended reporting requirements upon which any merger approval should be conditioned would not impose an additional or undue burden because they simply extend existing obligations. (Tr. 1436.)

C. Petitioners' Response to Staff's Proposed Reporting Requirements

Petitioners opposed Staff's concerns relating to diminished financial transparency and reporting as being without foundation. First, Iberdrola contended that the differences between IFRS and GAAP are not as pronounced as suggested by Staff, and that a number of foreign utilities successfully have invested in domestic utilities without incident, despite use of IFRS. (Tr. 548.)

Importantly, however, Petitioners agreed to accept all or part of several of the reporting requirements proposed by Staff. First, Petitioners Policy Panel testified that "Iberdrola will continue to comply with all U.S. laws and regulations regarding financial reporting." (Tr. 548.) Also, Petitioners offered to provide assistance with understanding the differences between GAAP and IFRS. (Id.) Petitioners Policy Panel represented that Energy East would continue to follow GAAP, and also comply with all relevant requirements of SOX. (Tr. 548-49.)

Petitioners asserted that the above commitments should be adequate to address concerns regarding post-merger reporting requirements. (Tr. 549.) Nevertheless, Petitioners also offered to provide access to the Commission, with New York and in English, to: (a) the books and records of NYSEG, RG&E, Iberdrola, and any Iberdrola affiliates that are related to NYSEG or RG&E, as well as access to the minutes of Iberdrola's Board of Directors meetings to the extent such minutes discuss Energy East; (b) all internal and external audit reports and recommendations for NYSEG, RG&E, and any Iberdrola affiliate with respect to the provision of goods and services for compensation to NYSEG or RG&E; and (c)

Iberdrola's consolidated balance sheets, income and cash flow statements in accordance with IFRS. (Tr. 549-50.)

D. The Reporting Requirements Proposed by Staff Should Be Adopted In This Proceeding

As detailed above, Staff proposed a number of reporting requirements that would become effective upon consummation of the proposed transaction. The underlying purpose of those reporting requirements is to protect customers against the risks, including the potential for abuse, that arise from a potential loss of financial transparency. To their credit, Petitioners have indicated a willingness to accept some – but not all – of the reporting requirements proposed by Staff. Importantly, however, for the reasons set forth below, the requirements opposed by Petitioners nevertheless should be adopted as conditions of merger approval in this proceeding.

First, although the Petitioners agreed that Energy East would remain subject to SOX, that commitment was not extended to include NYSEG and RG&E. The standards and attestation requirements imposed by SOX provide useful financial information, while also bestowing confidence in the validity of that information. Compliance with SOX, therefore, constitutes a valuable reporting requirement which should remain applicable to NYSEG and RG&E.

Second, Energy East, NYSEG and RG&E should be required to continue providing the information that otherwise would be reported in SEC filings, as recommended by Staff. (Tr. 1435.) The financial information contained in those filings has been identified as useful data for Staff in fulfilling its regulatory obligations. Accordingly, Staff's proposal to require that information as a condition of merger approval should be adopted.

Third, the Staff Policy Panel has testified to the desirability of receiving financial information presented in accordance with GAAP, which in Staff's opinion provides a higher level of transparency for its purposes. (Tr. 1435-36.) Although Petitioners commit Energy East to the continued use of GAAP "for all financial reporting" (Tr. 549), they do not offer to extend that commitment to encompass other financial reports. Instead, Petitioners offer to provide assistance with understanding IFRS. (Tr. 548.) That proposal is inadequate. Staff currently operates under a heavy burden to compile and analyze the vast quantities of financial data necessary to regulate NYSEG and RG&E. The additional complexity and burden of having to become expert in the standards of a foreign accounting system would be extremely burdensome to Staff. Importantly, to the extent reliance on IFRS makes Staff's job more difficult, such an outcome would increase risks borne by NYSEG and RG&E customers as a result of the proposed transaction. Inasmuch as concerns related to a possible transition away from GAAP are due to Iberdrola's plans to acquire Energy East, Petitioners should bear the burden of presenting financial information in the format with which Staff is familiar.

Fourth, the requirements of NYSEG's August 16, 2000 information order in Case 9187 provide additional information and financial transparency into that company. To ensure adequate financial information for regulatory purposes, Staff recommended continuing those requirements, as well as extending them to RG&E. This recommendation is reasonable and should be adopted as a condition of merger approval.

Multiple Intervenors is very concerned that the proposed transaction may result in a detrimental loss of transparency impacting the ability of the Commission and Staff to regulate NYSEG and RG&E effectively. There can be little doubt that any such loss in the transparency would constitute a new – and possibly significant – risk borne by those utilities' captive customers. The reporting requirements proposed by Staff would provide beneficial protections and constitute reasonable mitigation of the concerns raised. Accordingly, the Commission should adopt robust reporting requirements as a condition of merger approval.

POINT VI

MERGER APPROVAL SHOULD BE CONDITIONED UPON THE ADOPTION OF MEASURES THAT WOULD MITIGATE VMP CONCERNS IN A MANNER THAT DOES NOT PRECLUDE IBERDROLA RENEWABLES' FUTURE DEVELOPMENT OF WIND GENERATION

The proposed transaction raises VMP concerns related to Iberdrola's planned, simultaneous ownership of electric generation assets and T&D assets. Specifically, Iberdrola, which already owns certain generation assets in New York, seeks to acquire, via merger, T&D assets owned by Energy East (and operated by NYSEG and RG&E). The VMP concerns are exacerbated by: (a) the fact that Energy East currently owns certain electric generation assets within the NYSEG and RG&E service territories; and (b) Iberdrola Renewables, an unregulated company in which Iberdrola owns a controlling (i.e., 80 percent) share (see Tr. 625), has plans to build additional wind generation New York. For the reasons set forth below, Multiple Intervenors advocates that merger approval be conditioned upon the adoption of measures that would mitigate VMP concerns in a manner that does not preclude Iberdrola Renewables' future development of wind generation.

A. The Divestiture of Generation Assets Proposed in the Partial Acceptance Should Be Adopted and Supplemented to Produce Greater Customer Benefits

Petitioners advance a proposal in the Partial Acceptance to address VMP concerns raised by other parties. Specifically, Petitioners propose to competitively bid and auction Russell Station, the 63 MW Allegany Station, the 14 MW Peaker Station 3, and the 14 MW Peaker Station 9, all of which are owned by RG&E. (Ex. 50 at 1.) Petitioners further propose that: (a) the above-book proceeds from the sale of such generation assets "be shared with ratepayers in a manner to be determined by the Commission"; (b) Cayuga Energy, an unregulated subsidiary of Energy East, would competitively bid and auction the 67 MW Carthage Peaking Unit; (c) the proceeds from the sale of the Carthage Peaking Unit would accrue to shareholders; and (d) the aforementioned commitments would be subject to reasonable protocols determined by the Commission, which would include that the assets not be sold for below book value. (Id.) Multiple Intervenors generally supports Petitioners' proposals to divest generation assets owned by Energy East. Significantly, however, those proposals should be supplemented to provide that all – or almost all – of the above-book proceeds from the sale of RG&E's generation assets be allocated to customers.[48]

Initially, divestiture of Energy East's non-wind generation assets would help, to some extent, to address VMP concerns raised by the proposed transaction. (See, e.g., Tr. 910-23, 1247-54.) Such divestiture, to the extent it occurs at prices above book value, should provide financial benefits to customers. Upon information and belief, there is no opposition to Petitioners' general proposal to divest generation assets owned by Energy East. Thus, the

[48] Multiple Intervenors advocates no position with respect to the treatment of auction proceeds stemming from the sale of Cayuga Energy's generation assets.

Commission should condition merger approval upon Petitioners' proposed divestiture of Energy East's generation assets.

Importantly, however, Petitioners' proposals should be supplemented by the condition that all – or almost all – of the above-book proceeds from the sale of RG&E's generation assets be allocated to customers. Inasmuch as the Partial Acceptance provides that "[t]he above-book proceeds from the auction of RG&E's regulated assets (*i.e.*, Russell, Allegany and peakers) will be shared with ratepayers in a manner to be determined by the Commission" (Ex. 50 at 1), Multiple Intervenors' proposed supplemental condition is not contradictory to the Partial Acceptance but, rather, simply calls for such allocation to be determined now, and accepted by Petitioners as a condition to merger approval.[49]

The allocation of 100 percent of the above-book auction proceeds to customers is justified upon several grounds. First, the above-market value of the energy produced by the subject generation assets currently is allocated to RG&E's customers. (Tr. 609.) If customers are to lose this benefit, they should receive the auction proceeds in return. Second, as acknowledged by Petitioners Policy Panel, customers paid for the construction, operation and maintenance of the subject generating assets through rates. (Tr. 608.) Third, the allocation of all above-book auction proceeds to customers can be characterized, in some sense, as a benefit of the proposed transaction. As such, an allocation favorable to customers simply would increase the benefits against which the costs and risks of the transaction must

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[49] See Petitioners' April 4th Responses at 9 (indicating that the approximate book value of the Allegany Station, Peaker Station 3, Peaker Station 4 and the Carthage Peaking Unit on a combined basis, as of December 31, 2007, is $15.23 million; Multiple Intervenors notes that the Partial Acceptance proposes the divestiture of Peaker Station 9, not 4, suggesting that some clarification is needed). Russell Station is fully depreciated at this time. (Tr. 606.)

be evaluated. Finally, it also should be considered that the timing of the proposed asset divestiture – which may or may not prove beneficial to customers – is related to Energy East's decision to be acquired by Iberdrola.

The only justification for allocating something less than 100 percent of the above-book auction proceeds to customers would be if the Commission considered some financial incentive to Petitioners to be necessary for a successful auction. In other instances where utilities divested generation assets, the Commission has allowed a small – and often capped – allocation of above-book proceeds to shareholders.[50] If the Commission elects to follow that practice in this proceeding, Multiple Intervenors asserts that the maximum amount allocable to shareholders should be limited both in percentage terms (e.g., 5 percent) and nominal dollars (e.g., $3 million maximum).

For the foregoing reasons, Multiple Intervenors urges the Commission to approve the divestiture of generation assets proposed in the Partial Acceptance as a condition of merger closing, and also rule that all – or almost all – of the above-book proceeds from the sale of RG&E's generation assets be allocated to customers.

B. The Commission Should Seek to Limit Petitioners' Ability to Exercise VMP in a Manner That Does Not Preclude Iberdrola Renewables' Future Development of Wind Generation

Multiple Intervenors recognizes that the possible simultaneous ownership of electric T&D assets and generation assets raises VMP concerns. (See, e.g., Tr. 910-23,

[50] See, e.g., Cases 03-E-0765, 03-G-0766, 02-E-0198, Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of Rochester Gas and Electric Corporation for Electric and Gas Service, Order Adopting Provisions of Joint Proposals with Conditions (issued May 20, 2004, at 21 [describing RG&E's agreement to retain, for shareholders, approximately 5% of the above-book proceeds from the sale of the much larger Ginna Nuclear Power Plant, capped at $10 million].

1247-54.) In response to those concerns, Staff advocated that Petitioners be required to divest all generation assets, including wind generation, as a condition of merger approval. (Tr. 288-91.) The Independent Power Producers of New York, Inc. ("IPPNY") asserted that Petitioners should: (a) auction Russell Station; (b) divest all other existing, regulated electric generation facilities; and (c) "commit to not construct or otherwise acquire any ownership interests in other electric generating facilities located in RG&E's and NYSEG's respective service territories." (Tr. 922-23.) As detailed below, Multiple Intervenors generally supports the positions of Staff and IPPNY with respect to fossil-fuel generating units. For the reasons set forth below, Multiple Intervenors recommends that the Commission grant merger approval subject to Iberdrola's acceptance of conditions that limit Petitioners' ability to exercise VMP in a manner that would not preclude Iberdrola Renewables' future development of wind generation.[51]

Petitioners' Partial Acceptance seeks to narrow the issues in dispute in this proceeding by consenting to divest certain existing generation facilities. (Ex. 50 at 1.) Upon information and belief, no party has objections to that portion of the Partial Acceptance, although, as detailed, supra, Multiple Intervenors does advocate that all – or almost all – of the above-book proceeds from the divestiture of RG&E-owned facilities be allocated to customers.

The Partial Acceptance also contains the following proposal:

> So long as the Commission does not impose any limitations on the ability of Iberdrola Renewables to develop renewable

[51] Multiple Intervenors' position reflects, inter alia, certain unique characteristics pertaining to wind generation and the proposed transaction in general. Accordingly, Multiple Intervenors' position herein should not be construed as indicative of its general position with respect to VMP issues.

> generation in New York State as a result of this proceeding, Iberdrola will support and encourage investments by Iberdrola Renewables (through its upstream voting interest in Iberdrola Renewables) in excess of $100 million in the development of wind generation in New York State within the next 3 years, subject to all necessary development permits and authorizations, and provided that there is no material adverse change to the existing fundamental economics of wind generation development in New York State (*e.g.*, values associated with PTCs, RPS and NYISO market pricing).

(Ex. 50 at 2.) Petitioners also proposed that "all renewable generation ownership and development will be accomplished through an unregulated affiliate of Iberdrola that is not a direct or indirect subsidiary of NYSEG or RG&E." (Id.)

In evaluating the benefits of the proposed transaction against the costs and risks, Multiple Intervenors contends that the above proposal constitutes a slight benefit that should be adopted – or made more favorable – as a condition of merger approval. Generally, Multiple Intervenors is supportive of proposals to invest in New York's energy infrastructure, and the above proposal would increase generating capacity Upstate in a manner that also should contribute positively to the environment. Multiple Intervenors does not believe it would be in the public interest to preclude Iberdrola Renewables from developing future wind generation projects in the State.

Additionally, in evaluating potential VMP concerns, there are certain characteristics of wind generation that may warrant a different treatment than more traditional, fossil-fuel generation. For instance, Petitioners witness Hieronymus points out that: (a) wind is "energy limited," in that its energy and capacity value is much less than its nameplate capacity; (b) "wind resources have unpredictable and rapidly variable output levels," thereby causing most wind generation to participate in real-time energy markets, as opposed to day-ahead energy markets; and (c) wind facilities have zero fuel costs, thereby causing them to bid into competitive markets as "price takers." (Tr. 863-64.)

Thus, Multiple Intervenors favors merger approval upon conditions that address and mitigate VMP issues, but which also would not preclude Iberdrola Renewables' future development of wind generation. Importantly, however, for several reasons Multiple Intervenors does not consider Petitioners' "Renewable Commitment" (Ex. 50 at 2) to constitute a particularly large public benefit. Initially, the "commitment" to develop additional wind generation is weakened by numerous caveats and conditions that would obviate any obligation if: (a) the value of PTCs changed materially; (d) the value of customer-funded subsidies available under Case 03-E-0188, the Renewable Portfolio Standard proceeding, changed materially; and (c) prices in New York's wholesale electricity market changed materially. (Tr. 628-29; see also Ex. 50 at 2.) Second, given Petitioners' estimate that wind generation costs approximately $2 million per MW to develop, the entire commitment is roughly equivalent to 50 MW, which represents only a small fraction of the 998 MW of wind projects currently under consideration by Iberdrola Renewables. (See Ex. 57.) Third, there may be VMP issues regarding wind development that cannot be mitigated entirely by conditions imposed upon merger approval.[52]

For the foregoing reasons, Multiple Intervenors urges the Commission to grant merger approval subject to Iberdrola's acceptance of conditions that, inter alia, mitigate VMP

[52] Inasmuch as Multiple Intervenors' position on VMP issues is not quite as restrictive as that advanced by other parties in this proceeding (e.g., Staff, IPPNY), the resolution of such issues in a manner that would not preclude Iberdrola Renewables' future development of wind generation should, if anything, warrant a greater amount of financial and rate-related benefits to customers (i.e., because customers still would be subject to certain risks related to VMP that would not be present if Petitioners hereinafter were prohibited from owning generation of any type in New York).

concerns in a matter that does not preclude Iberdrola Renewables' future development of wind generation. The exceptions for wind generation that may be acceptable to Multiple Intervenors within the context of this proceeding: (a) would not apply to fossil-fuel generation; and (b) may be unacceptable in other contexts.

POINT VII

PROPOSALS BY STAFF AND PETITIONERS TO IMPLEMENT ELECTRIC AND GAS RDMs FOR NYSEG AND RG&E SHOULD BE REJECTED AT THIS TIME

In response to the Joint Petition, Staff proposed that: "NYSEG and RG&E should be directed to file an RDM proposal for review by the parties and approved by the Commission for implementation on January 1, 2009, to be in effect for calendar year 2009." (Tr. 1629.) On rebuttal, Petitioners agreed that NYSEG and RG&E should file RDM plans. (Tr. at 258.) For the reasons set forth below, proposals by Staff and Petitioners to implement electric and gas RDMs should be rejected at this time – RDMs only should considered, if at all, in the context of rate proceedings.

A. The Possible Implementation of RDMs Is Not Relevant to the Proposed Transaction

Initially, it is important for the Commission to recognize that, notwithstanding proposals herein by Staff and Petitioners, the possible implementation of RDMs by NYSEG and/or RG&E is not relevant to the proposed transaction. On cross-examination, Staff witness Dickens conceded that the issue of RDMs had no bearing on whether the transaction is in the public interest. (Tr. 1637.) Similarly, Petitioners' RDM Panel testified that: "We do not believe that approval of an RDM, or specific decoupling methodology, is relevant to the

Commission's determination as to whether the proposed acquisition is in the public interest." (Tr. at 258.) Thus, in ruling on the proposed transaction, the Commission need not reach any conclusions with respect to the implementation of RDMs.

B. RDMs Can Have Negative Consequences

RDMs are not the panacea to achieving the Commission's energy efficiency goals. Indeed, a poorly-designed RDM can have negative consequences far in excess of any purported benefits. The decision to implement an RDM of a particular design should not be made lightly, or upon a poorly-developed evidentiary record.

In a well-reasoned analysis, Staff recommended previously that RDMs not be required:

> The Commission and Staff have ... recognized that there are some inherent public policy conflicts between tying utility revenues and profits to the throughput of the utilities' systems .... Consequently, the issue is how best to overcome these conflicts. While, theoretically, imposition of an RDM could resolve some of the conflicts, as the proponents of the RDM concept argue, there are serious concerns with such an approach, such as the difficulty that would be involved in developing an appropriate mechanism, and the risk of rate instability that might result. Further, other approaches, such as improved rate designs, targeted rate incentives and performance incentives, may be just as effective as or even better than such a broadbased incentive ratemaking approach. *** Accordingly, Staff recommends that an RDM not be required at this time.

(Ex. 117 at 7-8.)[53]

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[53] Exhibit 117 is a Staff Report, dated July 9, 2004, from Case 03-E-0640, Proceeding on Motion of the Commission to Investigate Potential Electric Delivery Rate Disincentives Against the Promotion of Energy Efficiency, Renewable Technologies and Distributed Generation.

In so recommending, Staff alluded to the State's prior, negative experience with RDMs:

> Staff's previous experience with comprehensive RDMs is that they tend to generate large revenue accruals, nearly all caused by weather. Such accruals can either re-introduce rate instability or create large revenue deferrals. When the true up is applied with a one year or more delay, as is typical, customer confusion and large bill swings can result. In effect, the risks of weather fluctuations are shifted from the utility to the customers.

(Id. at 8.)

The relative pros and cons associated with possible RDM designs have not been examined in sufficient detail to be acted upon in this proceeding. This shortcoming is particularly relevant where, as demonstrated, infra, parties are seeking Commission approval of RDMs outside of a rate proceeding and, in the case of RG&E, without adequate public notice.

C. RDMs Only Should Be Considered in Rate Proceedings

Last year, the Commission issued an order requiring utilities to develop proposals to implement RDMs.[54] Significantly, the Commission directed that such proposals be advanced in the context of rate proceedings.

For instance, the Commission directed that:

> These revenue decoupling proposals should be filed in ongoing and new rate cases, whereby the utilities, Department of Public

[54] Cases 03-E-0640, supra, and 06-G-0746, In the Matter of the Investigation of Potential Gas Delivery Rate Disincentives Against the Promotion of Energy Efficiency, Renewable Technologies and Distributed Generation, Order Requiring Proposals for Revenue Decoupling Mechanisms (hereinafter, "RDM Order") (issued April 20, 2007).

> Service staff (Staff) and interested parties can address specific design details.[55]

The Commission ruled that rate proceedings – as opposed to merger proceedings – were the appropriate forums for designing RDMs: "We believe that the proper forum for designing an appropriate delivery service revenue decoupling mechanism is in utility rate cases."[56]

The design and implementation of an RDM needs to account for, inter alia, the utility's projected sales levels, rates and revenues. (See, e.g., Tr. 270, 288-89.) Examining RDMs in the context of rate proceedings also allows for other issues, such as the impact of an RDM on a utility's risk and appropriate rate of return.[57]

This proceeding is examining whether the proposed transaction is in the public interest. This is not a rate proceeding. (Tr. 285.)[58] There is no compelling need to condition merger approval upon the institution of a subsequent phase of this proceeding to implement RDMs effective January 1, 2009. Indeed, such a ruling, if followed by a rate filing by NYSEG and/or RG&E, could result in a duplication of efforts (i.e., the examination of RDM issues as part of this proceeding and in a subsequent rate proceeding) and the possible need to modify an existing RDM shortly after it is implemented. (See Tr. 290.) It would be far more efficient (see Tr. 287), and consistent with the Commission's generic order on RDMs, to

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[55] Cases 03-E-0640 and 06-G-0746, supra, RDM Order at 3; see also id. at 16-17.

[56] Id. at 13.

[57] See id. at 15 (holding that: "We agree that the effect of a delivery service revenue decoupling mechanism on utility rate of return should be considered, to the extent appropriate, along with other factors, in the context of individual rate proceedings").

[58] The provision of financial benefits to customers, however, could impact existing rate levels.

require the submission of proposals to implement RDMs as part of NYSEG and RG&E's next rate proceedings.

D. There Has Been Inadequate Public Notice That RDM Proposals Relating to RG&E Would Be Considered in This Proceeding

On August 29, 2007, the Commission instituted Case 07-E-0996 to consider an RDM for NYSEG.[59] On October 22, 2007, the Commission transferred RDM issues involving NYSEG to this proceeding, and closed Case 07-E-0996.[60] In contrast, there has been no Commission ruling directing the consideration of RDM issues for RG&E in this proceeding. Absent such ruling, there has been inadequate public notice that RDM issues related to RG&E even would be addressed in this proceeding.

Initially, it is not clear why the Commission transferred RDM issues related to NYSEG to this proceeding. Presumably, the Commission assumed, or hoped, that NYSEG's existing rate levels – and possibly sales and revenue levels – would be addressed in this proceeding, possibly as part of a negotiated joint proposal. For that reason, the Commission apparently determined that RDM issues "can more effectively be considered" in this proceeding, as opposed to a separate proceeding.[61] Given the absence of a joint proposal, as well as the dearth of evidence pertaining to the appropriate, forward-looking sales forecasts,

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[59] Case 07-M-0996, Proceeding on Motion of the Commission to Consider a Revenue Decoupling Mechanism for New York State Electric & Gas Corporation, Order Instituting Proceeding (issued August 29, 2007). This proceeding initially was docketed as Case 07-E-0996.

[60] Cases 07-M-0906, supra, and 07-M-0996, supra, Notice Consolidating Proceedings (issued October 22, 2007).

[61] See Cases 07-M-0906 and 07-M-0996, supra, Notice Consolidating Proceedings at 1.

rates and revenue levels for NYSEG, the Commission should determine that RDM issues "can more effectively be considered" in NYSEG's next electric and gas rate proceeding, as opposed to a subsequent phase of this merger proceeding.

Importantly, even if, arguendo, the Commission concludes that there has been adequate public notice that RDM issues would – and still should – be addressed for NYSEG in this proceeding, the same cannot be said with respect to the consideration of RDMs for RG&E. For instance, there is no counterpart to Case 07-M-0996, directing the consideration of an RDM for RG&E outside of the utility's next rate proceeding, nor is there any counterpart to the Notice Consolidated Proceedings issued herein that transfers the consideration of RDM issues pertaining to RG&E to this proceeding for resolution. Thus, at a minimum, the possible implementation of an RDM for RG&E should be examined within the context of that utility's next rate proceeding.

E. Specific RDM Design Elements Should Not Be Adopted at This Time

Both Staff and Petitioners advance various elements to be adopted as part of new electric and gas RDMs for NYSEG and RG&E. (See, e.g., Tr. 264-70.) Significantly, Staff and Petitioners agree that the specific design of the RDMs should not be decided now but, rather, be addressed in a subsequent phase to this proceeding. (Tr. 285-86.) For the reasons set forth above, Multiple Intervenors urges the Commission to refrain from addressing RDM issues now and, instead, asserts that such issues should be addressed, if at all, within the context of rate proceedings where related issues and considerations can be addressed comprehensively and efficiently. If, notwithstanding Multiple Intervenors' arguments, the Commission elects to institute a separate phase of this proceeding to examine

RDMs for NYSEG and/or RG&E, then there is no compelling reason to resolve any RDM-related issue now. Thus, specific RDM design elements should not be adopted at this time.[62]

In particular, the Commission should refrain from deciding now which customer classes would be subject to RDMs implemented in the future. Multiple Intervenors, and other large customers, generally do not favor RDMs because, inter alia, they: (a) shift business and financial risk from the utility to customers; (b) are complicated and often produce undesirable and/or unanticipated outcomes; (c) diminish delivery rate stability – which is very important to large customers for budgeting purposes – due to periodic reconciliations; (d) can diminish a utility's incentive to promote economic development and beneficial load growth; and (e) are unnecessary if rates are cost-based.

The Commission already has ruled that RDMs need not apply to all customer classes:

> There are a number of design and implementation issues that would need to be considered in the development of an effective revenue decoupling mechanism. These include: whether the mechanism is applied to all or only some customer classes ....[63]

In so ruling, the Commission recognized that to the extent customer rates are cost-based (e.g., such as rates applicable to large customers), the rate disincentives intended to be addressed by RDMs are less prevalent or non-existent:

> With respect to the different customer classes and whether the rate design impacts are more prominent for certain classes than

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[62] For instance, Petitioners' proposals to implement RDMs for NYSEG and RG&E that could result in automatic rate increases to the utilities, or accomplish revenue reconciliations through volumetric surcharges, should not be adopted for the reasons made apparent during cross-examination of Petitioners RDM Panel. (See Tr. 290-97.)

[63] Cases 03-E-0640 and 06-G-0746, supra, RDM Order at 8.

> others, we recognize that more movement toward fully cost-based rates has been or can more easily be accommodated within the larger commercial and industrial classes, thereby largely breaking the link between utility sales and profits attributable to these customers.[64]

In the case of NYSEG and RG&E, delivery rates for large customers are predominantly – if not exclusively – comprised of monthly and demand-based charges with comparatively little (if any) revenues recovered through volumetric charges. (See, e.g., Tr. 299.)

Thus, to the extent RDMs are addressed in a subsequent phase of this proceeding or, better yet, in the next NYSEG and RG&E rate proceedings, parties should be free to advocate that selected customer classes should be excluded from the implementation of RDMs. On cross-examination, Staff and Petitioners indicated that they were willing to consider future exemptions from RDMs for large customer classes. (Tr. 300-01, 1640.)

For the foregoing reasons, proposals by Staff and Petitioners to implement electric and gas RDMs for NYSEG and RG&E should be rejected at this time.

POINT VIII

THE POSSIBLE TAKEOVER OF IBERDROLA INCREASES THE RISKS ASSOCIATED WITH THE PROPOSED TRANSACTION

The parties to this proceeding have expended substantial energy and resources in an attempt to determine whether the proposed transaction is in the public interest. That examination has focused on, inter alia, the particular characteristics of Iberdrola as a corporate parent and potential steward of the New York utilities. As a result, any indication

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[64] Id. at 10-11.

that the identity or ownership of Iberdrola might change necessarily would compel a re-examination of the purported benefits of the proposed transaction.

News organizations have been reporting for months that Iberdrola is the focus of takeover interest by multiple European utilities companies.[65] Iberdrola's stock price rose in response to these reports, suggesting that they reflect more than idle speculation.[66] One recent report states that two companies – Electricite de France S.A. and Actividades de Construccion y Servicios S.A. ("ACS") – are in "advanced discussions" regarding a joint bid for Iberdrola, and that ACS would break up Iberdrola if it acquired that company.[67]

At the conclusion of hearings, Judge Epstein informed the active parties that he intended to present to the Commission issues relating to the potential takeover of Iberdrola. (Tr. 1898-1903.)[68] Generally, Judge Epstein's concerns relate to whether the Commission would retain jurisdiction to oversee a subsequent transfer of ownership of Energy East, NYSEG and/or RG&E from Iberdrola to a third party. Judge Epstein invited the parties to brief the issue of whether the Commission's jurisdiction to review any subsequent transfer involving Energy East, NYSEG and RG&E would be diminished by

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[65] See, e.g., Matthew Karnitschnig, et al., *$100 Billion Power Deal Moves Closer in Europe*, WALL STREET JOURNAL, March 21, 2008, at A1 (stating that "French and Spanish companies are in advanced discussions about pursuing" Iberdrola).

[66] See, e.g., Kristian Rix and Tara Patel, *Iberdrola, Fenosa Climb After Report of Possible Bids*, Bloomberg.com, *at* http://www.bloomberg.com/apps/news?pid=20601085&sid=a3M5si1o4E30&refer=europe# (last visited April 7, 2008).

[67] See Karnitsching, *$100 Billion Power Deal Moves Closer in Europe,* WALL STREET JOURNAL, March 28, 2008 at A1.

[68] See also Rafael A. Epstein, Administrative Law Judge, Letter to Active Parties (April 4, 2008).

approval of the proposed transaction.[69] For the reasons discussed below, the Commission would possess jurisdiction to review a post-merger attempt to acquire Iberdrola. Practical considerations, however, may hinder the ability of the Commission to exercise its authority effectively and, therefore, additional customer protections may be warranted at this time.

Pursuant to PSL section 70, no gas corporation[70] or electric corporation[71] may acquire, directly or indirectly, the stocks or bonds of any other corporation engaged in the same or similar business in New York State without obtaining Commission approval.[72] The Commission must determine that the acquisition is in the public interest before it approves any such stock transfer.[73] Historically, the Commission has asserted its jurisdiction under PSL section 70 broadly, stating that "acquisition of the corporate parent should be treated as acquisition of the wholly owned" jurisdictional corporation.[74] The Commission also has

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[69] Id.

[70] A "gas corporation" is an entity that owns, operates or manages any gas plant (PSL § 2(11)), which is defined broadly to include all real estate, fixtures and personal property operated, owned, used or to be used for or in connection with or to facilitate the manufacture, conveying, transportation, distribution, sale or furnishing of gas ... for light, heat or power." PSL § 2(10).

[71] An "electric corporation" is an entity that owns, operates or manages any electric plant (PSL § 2(13)), which is defined broadly to include "all real estate, fixtures and personal property operated, owned, used or to be used for or in connection with or to facilitate the generation, transmission, distribution, sale or furnishing of electricity for light, heat or power." PSL § 2(12).

[72] PSL § 70.

[73] Id.

[74] Case 95-C-0078, Petition of Sprint Corporation for a Declaratory Ruling Disclaiming Jurisdiction to Review the Purchase of 20% Equity Ownership in Sprint by France Telecom and Deutsche Telekom for an Aggregate Investment of $4.2 billion or, in the alternative, for approval of the Transaction, Order Approving Transaction at 5 (issued May

expressed the particular intent to protect captive retail customers from the transactions of corporate entities upstream from the jurisdictional corporation.[75]

The Commission possesses authority under PSL section 70 to require its approval, with respect to the impact on NYSEG and RG&E customers, prior to consummation of a takeover of Iberdrola (assuming Iberdrola has acquired Energy East and its subsidiaries). As detailed above, PSL section 70 provides the Commission with the authority, and the affirmative obligation, to review a transaction involving corporate parents if the transaction holds the potential to harm captive customers, despite the number of corporate layers between the acquirer and the New York corporation.[76]

Any takeover of Iberdrola undoubtedly would hold the potential to harm the customers of both NYSEG and RG&E. A possible takeover increases risks in at least two ways. First, if the transaction proposed in this proceeding is approved, ownership of NYSEG

19, 1995) ("Sprint Order"). Although the Sprint Order involved the application of PSL § 100 with respect to a telephone corporation, sections 70 and 100 are phrased similarly and are to be interpreted similarly. Spring Brook Water Co. v. Vill. of Hudson, 269 A.D. 515, 518–19 (3d Dep't 1945). The Commission has applied its analysis of PSL section 100 to proceedings that involve PSL section 70 and gas and electric corporations. See, e.g., Case 97-E-1390, Joint Petition of New York State Electric & Gas Corporation, the Hon. Frederick Crouch, and the Hon. Warren Anderson for a Declaratory Ruling That CalEnergy Company, Inc. and its Subsidiaries May Not Acquire Any of the Company's Stocks or Bonds Without the Commission's Prior Approval and for an Order Enjoining CalEnergy and its Subsidiaries From Acquiring Any Such Securities, Order Confirming Prior Order and Reflecting Changed Circumstances (issued August 21, 1997).

[75] See, e.g., Case 93-E-0272, Re Niagara Mohawk Power Corporation, additional party: Sithe/Independence Power Partners, L.P., Order adopting a regulatory framework to govern retail electric sales by the Independence generating station – a planned 1,040 MW, gas-fired qualifying cogeneration facility (QF) – to customers located in the service territory of a retail electric utility, Niagara Mohawk Power Corp. (issued April 19, 1994) at 11-12.

[76] Case 97-E-1390, supra, Order Confirming Prior Order and Reflecting Changed Circumstances at 24-25.

and RG&E would be acquired by Iberdrola. If Iberdrola subsequently is taken over, what entity would own NYSEG and RG&E, and would that entity's potential ownership of NYSEG and RG&E be in the public interest? The uncertainty surrounding the answer to this question is magnified by reports that a takeover of Iberdrola likely would result in its breakup. The proposed transaction cannot be considered in a vacuum, and the Commission must confront the possibility that, shortly after approving the proposed transaction, Energy East, NYSEG and RG&E could be acquired by a corporation other than Iberdrola.

Second, the acquirer may not consent to Commission jurisdiction. Although, the Commission would possess authority under PSL section 70 to review a proposed takeover of Iberdrola, there may be issues as to whether the Commission's jurisdiction over such a transaction is enforceable in Europe. For instance, the Commission may not be able to compel a European corporation to seek its consent before acquiring Iberdrola through some type of hostile takeover. Therefore, additional protections are needed, and warranted, to mitigate the risk of an Iberdrola takeover for which Commission jurisdiction is not recognized or otherwise is contested.

The additional protections should provide a strong incentive – or compulsion – for a foreign corporation to seek Commission approval before acquiring Iberdrola. In practice, the protections would be triggered by a proposed takeover of Iberdrola and would remain in effect until the acquiring corporation seeks Commission consent for the takeover. Specifically, Multiple Intervenors recommends that the following two protections be adopted as a condition of any merger approval in this proceeding: (a) Energy East, NYSEG and RG&E should be barred from transmitting any dividends upstream if and when any agreement to acquire Iberdrola – either hostile or friendly – becomes public; and (b) to the extent Commission jurisdiction over the acquisition of Iberdrola (and, by extension, NYSEG and RG&E) is not recognized or otherwise is contested, the Commission would be permitted to implement an immediate 25 percent reduction in delivery rates. The protections would cease to be operational once Commission authorization of the transaction is sought, and in no way would pre-judge the outcome of the future proceeding under PSL section 70.

The adoption of the aforementioned protections in this proceeding would serve two beneficial purposes. First, they would protect NYSEG and RG&E customers in the event Iberdrola is the subject of a corporate takeover for which Commission authorization is not recognized or otherwise is contested. Second, the protections, which would be adopted in a final Commission order, would place potential acquirors of Iberdrola on notice of the need to submit to Commission jurisdiction in conjunction with any takeover of the corporate parent of NSYEG and RG&E. Multiple Intervenors notes that, absent the attempted acquisition of Iberdrola and a subsequent decision not to seek, or to contest, Commission jurisdiction of that transaction, the protections proposed herein would have no impact or consequences.

CONCLUSION

For all the foregoing reasons, Multiple Intervenors urges the Commission to approve the proposed transaction between Iberdrola and Energy East, subject to numerous conditions intended to benefit and protect customers of NYSEG and RG&E.

As demonstrated in Point I, supra, the burden of proving that the transaction would produce net positive benefits, thereby satisfying the public interest standard, is on Petitioners.

As demonstrated in Points II through VI, supra, that burden cannot be satisfied absent Petitioners' acceptance of additional benefits and protections for customers. Such benefits and protections should include, at a minimum: (a) the provision of substantial financial and rate-related benefits to customers; (b) the adoption of more stringent electric and gas reliability, service quality and safety performance standards and revenue adjustments; (c) the adoption of financial protections for customers; (d) the adoption of robust reporting requirements; and (e) the adoption of measures that would mitigate VMP concerns in a manner that would not preclude Iberdrola Renewables' future development of wind generation.

As demonstrated in Point VII, supra, proposals by Staff and Petitioners to implement elective and gas RDMs for NYSEG and RG&E should be rejected at this time.

Finally, as demonstrated in point VIII, supra, the possible takeover of Iberdrola increases the risks associated with the proposed transaction.

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Respectfully submitted,

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