

STATE OF NEW YORK
DEPARTMENT OF PUBLIC SERVICE

Meeting of the Public Service Commission

Thursday, September 4, 2014
10:33 a.m.
19th Floor Board Room
Three Empire State Plaza
Albany, New York 12223-1350

COMMISSIONERS:

AUDREY ZIBELMAN, Chair
DIANE X. BURMAN
GREGG C. SAYRE
PATRICIA ACAMPORA
GARRY BROWN

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2 (The meeting commenced at 10:33
3 a.m.)

4 CHAIR ZIBELMAN: Welcome back to
5 school everybody. I hope you all had a good summer
6 vacation. And we're going to start the Commission
7 meeting, so I'd like to call it to order.

8 Secretary Burgess, are there --
9 is there any other items?

10 SECRETARY BURGESS: There are no
11 changes to the agenda this morning.

12 CHAIR ZIBELMAN: Okay. So the
13 first thing we're going to do is we'll move then to
14 the regular agenda. And the first, and actually
15 only item for discussion today is item 201, which
16 is case number 13-M-0026 et al. And it's the
17 proceeding to determine what adjustments should be
18 made to certain National Grid affiliates' rates or
19 earnings based on a forensic audit.

20 Judge Prestemon will be
21 presenting today. And I believe then we also have
22 Joe Lochner will be supplementing. Thank you.

23 Judge?

24 A.L.J. PRESTEMON: Thank you,
25 Chair Zibelman.

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2 Good morning, Commissioners.

3 The draft order you have before
4 you in this case, if adopted, would approve the
5 terms of the joint proposal entered into between
6 the Department Staff and National Grid in May of
7 this year. And it would bring to a close the
8 Commission's investigation of financial and rate
9 issues associated with the allocation of costs by
10 National Grid from its service companies to its New
11 York utilities, specifically during the 2000 to
12 2010 -- 2008 to 2010 time period.

13 Under the terms of the joint
14 proposal, National Grid will create credit accounts
15 in the amount of twenty-four and three-quarters
16 million dollars for the benefit of the customers of
17 its Downstate gas utilities, eleven point four
18 million for the customers of KeySpan Energy
19 Delivery Long Island, and thirteen point three
20 million for the customers of KeySpan Energy
21 Delivery New York. Those accounts will be
22 established upon approval of the order and would
23 immediately begin earning a return for investors
24 and would immediately be available for disposition
25 by the Commission for the benefit of ratepayers.

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2 This case actually had its
3 genesis back in 2010 when Staff's review of an
4 electric rate filing by Niagara Mohawk, National
5 Grid's Upstate electric utility, raised a number of
6 concerns about whether or not excess costs were
7 being allocated to Niagara Mohawk Electric by the
8 National Grid service companies.

9 Those concerns prompted the
10 Commission to authorize the issuance of our request
11 for proposals to hire an auditor to examine the
12 practices and procedures of National Grid in making
13 those service companies allocations. And the
14 Commission, at the same time, established a second
15 case -- a separate case, 10-M-0451, to consider the
16 results of that audit.

17 In February of 2011, Overland
18 Consulting was selected as the auditor to conduct
19 the study. In the meantime, in that rate case that
20 precipitated this effort, the Commission set rates.
21 But in order to protect ratepayers pending the
22 outcome of that -- the audit, the Commission made
23 fifty million dollars in rates temporary and
24 subject to refund.

25 Overland ultimately issued its

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2 report in October of 2011. The methodology it
3 utilized to examine the cost allocation procedures
4 of National Grid essentially involved taking a
5 random sample of the cost allocation transactions,
6 examining the documentation of the transactions to
7 determine whether the allocations had been made
8 properly to the proper utility, in the proper
9 amount, in the proper account, and whether they
10 were adequately documented.

11 Once they had determined the
12 results of the sample, they extrapolated the dollar
13 amount of what they considered to be improperly
14 allocated transactions to the total population of
15 transactions, to come up with an estimate of what
16 might have been the total amount over-allocated to
17 a particular utility.

18 Their study focused on the 2009
19 rate years of each of the utilities and it came up
20 with an estimate of as much as forty-four million
21 dollars over-allocated to the utilities. The
22 results were statistically tested by establishing a
23 confidence interval around the estimate within
24 which it could be said that there was a ninety-five
25 percent probability that the actual number fell,

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2 much like the polls we see in every election where
3 it's fifty percent for so and so plus or minus
4 three percent, meaning it could be forty-seven, it
5 could be fifty-three. So there was a confidence
6 interval and those were fairly large.

7 And then in the case of Niagara
8 Mohawk Electric, it actually did not preclude the
9 possibility that there might have been an
10 under-allocation rather than an over-allocation.
11 But in the case of the other -- the other
12 utilities, it indicated the probability was that
13 there had been an over-allocation.

14 In addition, Overland made one
15 other finding that eleven point two million dollars
16 in costs that had been included in the rates in
17 case 10-E-0050 might not have been recurring and,
18 in other words, they were in the costs incurred by
19 the Company during the historic test year. But,
20 Overland felt that they would not recur during the
21 rate year for which rates were being set and,
22 therefore, should not have been included in rates.

23 National Grid vigorously disputed
24 the results of the audit in comments they filed
25 subsequently. National Grid contended that

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2 virtually all of the transactions, when properly
3 examined, were for proper utility purposes and
4 could be adequately documented. They concluded
5 that misallocations far from forty-four million
6 dollars, as Overland suggested, would net to only
7 about a hundred and seventy-five thousand dollars
8 or about point o two -- two hundredths of a percent
9 of the total transactions.

10 So to sort out this dispute, the
11 Commission established another case. That is the
12 13-M-0026. In that case, Staff directed -- the
13 Commission directed Staff to review the audit
14 process thoroughly and to determine whether there
15 was a need to adjust rates or to adjust the credits
16 that customers were entitled to under earnings
17 sharing mechanisms in effect with some of the
18 National Grid utilities. And it also extended the
19 inquiry from the 2009 year that had been the focus
20 of Overland, to the proceeding and subsequent
21 years, 2008 and 2010.

22 The Commission particularly
23 directed Staff to focus on the transactions that
24 Overland had found to be unsupported, meaning that
25 it did not reach a conclusion as to whether the

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2 transaction was proper or not, but merely that
3 there was insufficient documentation from National
4 Grid for it to make a determination. Those
5 unsupported transactions in dollar terms were by
6 far the majority of the misallocated costs.

7 Staff did, in fact, perform an
8 extensive review. It took a long time. It was a
9 very difficult discovery process, but eventually
10 Staff got the information it needed and made a
11 number of key findings.

12 First, it found that National
13 Grid was able to document about sixty percent of
14 the transactions, twenty-two of thirty-six of the
15 transactions that Overland had found to be
16 unsupported. It also concluded that a slight
17 modification was necessary to Overland's sampling
18 methodology in order to make it consistent with
19 the -- the statistical processes it applied.

20 And Staff found that the eleven
21 point two million dollars included in Niagara
22 Mohawk Electric rates was, in fact, properly
23 included in the rates and that no adjustment was
24 required for that.

25 Applying its findings concerning

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2 the sampling and the -- and the methodology, Staff
3 recalculated the overcharge estimates for 2009. It
4 extrapolated those results then to the years 2008
5 and 2009 -- '10, adjusted for statistical
6 uncertainty, and came up with new estimates of the
7 total amount that was owed to ratepayers due to
8 misallocated service company costs.

9 The number Staff calculated are
10 the credits that are included in the joint
11 proposal. National Grid accepted the results of
12 Staff's analysis for purposes of entering into a
13 joint proposal. The joint proposal, if approved,
14 would, therefore, conclude the investigation
15 ordered by the Commission in 13-M-0026. The rates
16 made temporary in 10-E-0050 would become permanent
17 and no longer subject to refund. And all issues in
18 the audit case, 10-M-0451, would be resolved except
19 for the ongoing implementation of recommendations
20 made by Overland concerning the implementation of
21 accounting systems and controls.

22 Given the divergence of initial
23 positions, a hundred and seventy-five thousand
24 versus forty-four million, I think the result of
25 the joint proposal is clearly within the range of

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2 reasonable outcomes that might have been expected
3 through litigation and it would have been
4 litigation that would likely have been extensive
5 and expensive and required additional audits as a
6 part of the discovery process.

7 The result in the joint proposal
8 accepts essentially what would have been Staff's
9 initial litigating position had it had to go
10 forward. I think it could be said that the result
11 is clearly fair to ratepayers. It is also fair to
12 National Grid. It gives them credit for the
13 transactions that were demonstrated to be proper
14 through Staff's analysis and it eliminates any
15 lingering earnings uncertainty associated with the
16 existence of temporary rates and ongoing
17 litigation.

18 So I think a commendable job, a
19 very commendable job was done by all the parties in
20 this case, and particularly Staff. The joint
21 proposal is fair and reasonable and in the public
22 interest and deserves approval.

23 That's my comments.

24 CHAIR ZIBELMAN: Thank you.

25 Mr. Lochner did you have anything

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2 to add at this time?

3 MR. LOCHNER: No; I think that's
4 a good summary of it.

5 CHAIR ZIBELMAN: Okay. Well,
6 thank you, Judge Prestemon.

7 I agree that I'm really
8 appreciative of the work that Staff has done here.
9 I just want to add just an editorial note out.

10 While I do think it's always a
11 good idea to avoid litigation that you can avoid,
12 certainly I know that our counsel would be more
13 than happy to go litigate if they didn't think that
14 the result was the right result.

15 So I think that the avoidance of
16 litigation risk is simply, in this instance, was
17 because Staff put together such a powerful position
18 that it made sense to everybody to accept their
19 position. And I applaud the work of the --
20 Doris' -- your group, I know in getting this done,
21 so thank you very much.

22 In terms of the settlement, I
23 also noted that the City of New York signed on to
24 the joint proposal. So I assume they also looked
25 at this and made a determination that this result

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2 was a very good result for the City.

3 A.L.J. PRESTEMON: They
4 actually -- they did not sign the joint proposal,
5 but they submitted comments in support. And they
6 were particularly pleased that these credit
7 accounts would be available for disposition by the
8 Commission if a rate case is filed in the near
9 future.

10 CHAIR ZIBELMAN: Great. Thank
11 you. That's helpful.

12 The other piece that I think
13 is -- is helpful to note and perhaps either Judge
14 Prestemon or Mr. Lochner, you want to elaborate on
15 this, is that the underlying problems that we're
16 dealing with here or something that I'm assuming
17 have been either rectified or Staff is looking at
18 to make sure we're not having continuing concerns
19 around misallocations.

20 And if you wanted to speak a
21 little bit about what's happening since then,
22 because I think it's just as critical to the
23 Commission.

24 MR. LOCHNER: Yes. There was a
25 rate case that occurred in the historic year 2011.

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2 And the Company submitted testimony of an outside
3 auditor, Ernst and Young, where they did an audit
4 of the service company charges to determine if they
5 were properly charged to our utilities,
6 particularly Niagara Mohawk.

7 And we reviewed -- examined their
8 work papers, but we also -- Staff also -- Trial
9 Staff performed their own examination of a random
10 sample of transactions and examined the allocation
11 of charges over the historic past to determine if
12 there were similar situations that occurred back in
13 the 2010 rate case. And we didn't see those
14 circumstances and we didn't see the undocumented or
15 the questionable transactions that we saw in the
16 past that caused -- alerted us to having to be in
17 the audit.

18 So in that respect, we felt more
19 comfortable that the Company had become aware of
20 the issues and was solving those problems. But
21 beyond that, in that rate proceeding and the rate
22 plan that came out of it, we created several
23 protections that are operating right now. The
24 first rate year that the Company completed, March
25 of 2014, the Company again had to submit an audit

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2 from an outside order of their service company
3 charge allocations.

4 We received that in July. Staff
5 is ripping that apart. It's going to review the
6 work papers. And again, we have to look at actual
7 transactions. That's the only way you can do this,
8 is verifying that actual transactions that come
9 through the bill are properly accounted for and
10 allocated with necessary support. That's one thing
11 we're doing.

12 We're also examining, in that
13 situation, the fact that they moved now to a
14 one-service company with one allocation methodology
15 that occurred back in 2012. And that will be
16 looked at in this situation, too. So we're
17 following up on those elements.

18 We're also reviewing their
19 management recommendations that come out of the
20 Overland audit. They've said they completed seven
21 of them. We've signed off on four, but there was
22 others that have to be -- we still need to do a
23 review work and make sure we agree with them.

24 Their monthly review of bills,
25 one thing the Company was not doing was actually

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2 looking at their monthly charges that were coming
3 through, looking at the actual transactions being
4 allocated to them. This is their largest vendor
5 and they didn't look at the bill because it came
6 from their affiliate. Now they are. Every month,
7 they have a review of their actual bill and our
8 staff are reviewing the work papers supporting
9 their monthly review of their service company bill.

10 So these are some of the things
11 we are doing. I think it's important that we
12 continue to have this oversight and audit of the
13 Company's transactions with their affiliate.

14 CHAIR ZIBELMAN: Great. Thank
15 you. I -- this is sort of the Ronald Reagan form
16 of government. Commissioner Burman, this is a
17 trust but verify.

18 So -- but I'd like to -- first of
19 all, I think it's -- I'm glad we're doing that
20 because I think it's really important. Having
21 affiliates and having these group companies are
22 terrific from the standpoint of synergies and
23 getting expertise that's broader, and then we can
24 do in this state.

25 But at the same time, there -- it

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2 is the need -- our need to make certain that our
3 consumers are being charged the right rates, the
4 right amounts. And I know this is a continuing
5 work on the part of Staff, not just in terms of
6 National Grid, but on other companies we regulate
7 that are part of holding companies structures. And
8 I appreciate the work and the learnings. And I
9 think it'll -- it will need to be a continuing
10 effort in that regards. Thank you.

11 I -- I'm -- you know, I think
12 that the joint proposal's clearly a fair one. It
13 certainly is in the interest of consumers because
14 it gets the credits back to the customers where
15 they belong. And I'm prepared to vote for it.
16 I'll take any other questions or comments at this
17 time or for Staff.

18 Any of the other Commissioners?
19 Commissioner Burman?

20 COMMISSIONER BURMAN: Thank you.

21 I think it's very good to see
22 Staff working on these issues and the importance of
23 management audits and the lessons learned and
24 looking at the take-aways and the elements that
25 were learned from the management audits and going

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2 forward how to apply them in future cases and other
3 management audits. So I look forward to hearing
4 about this and seeing how it works in other
5 management audits, as well.

6 So thank you.

7 CHAIR ZIBELMAN: Commissioner
8 Acampora? Commissioner Brown?

9 COMMISSIONER ACAMPORA: I'll just
10 say thank you. You really did a good job. Just
11 when we think we have the management audit tool
12 fine-tuned, we find that, you know, there's always
13 more to learn.

14 So we thank you for all your
15 efforts and this was a good outcome. Thank you.

16 COMMISSIONER SAYRE: I can see
17 that it was a heck of a lot of work by Staff to
18 come to this result, an awful lot of digging, an
19 awful lot of sweat, and a result that was so strong
20 that basically everybody who looked at it said oh,
21 okay, and caved. Nice job.

22 CHAIR ZIBELMAN: Thank you.

23 In that case, if no further
24 comments, all those in favor of the recommendation
25 to adopt the terms of the joint proposal that's

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2 going to bring to a conclusion the financial and
3 rate issues associated with the investigation into
4 concerns about National Grid's past practices for
5 the allocation of cost from service companies to
6 its regulated New York City -- New York affiliates,
7 please say aye.

8 COMMISSIONERS: Aye.

9 CHAIR ZIBELMAN: Opposed? There
10 being no opposition, the recommendation is adopted.

11 Thank you, Judge Prestemon and
12 Mr. Lochner. It was great.

13 We'll now move to the consent
14 agenda. With respect to the consent agenda, is
15 there any Commissioner who wants to recuse or
16 abstain from voting on any of the items?

17 Hearing none, any comments on any
18 of the Commissioners on any of the items in the
19 consent agenda? We're good? We're good? We're
20 good?

21 Okay. So in that case, let's
22 just go to a vote.

23 All those in favor of the
24 recommendations on the consent agenda, please
25 indicate by saying aye.

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2 COMMISSIONERS: Aye.

3 CHAIR ZIBELMAN: Opposed? There
4 being no opposition, the recommendations are
5 adopted.

6 Secretary Burgess, are there any
7 other matters before us today?

8 SECRETARY BURGESS: There are no
9 other matters today and the next Commission session
10 is on October 2nd, at ten thirty.

11 CHAIR ZIBELMAN: Okay. Great.

12 Thank you.

13 (The meeting concluded at 10:54
14 a.m.)

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2 STATE OF NEW YORK
3 I, Jamie Lee Greene, do hereby certify that the
4 foregoing was reported by me, in the cause, at the time
5 and place, as stated in the caption hereto, at Page 1
6 hereof; that the foregoing typewritten transcription
7 consisting of pages 1 through 18, is a true record of
8 all proceedings had at the hearing.

9 IN WITNESS WHEREOF, I have hereunto
10 subscribed my name, this the 10th day of September,
11 2014.

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