DIRECT TESTIMONY
OF
COST OF SERVICE PANEL

Q. Please state your name and business address.

A. Glynis L. Bunt and Lauren M. Guido, Central Hudson Gas & Electric Corporation ("Central Hudson" or the "Company"), 284 South Avenue, Poughkeepsie, New York 12601.

Q. In what capacity are you employed by Central Hudson?

A. (Bunt) I am Director of Cost, Rates and Forecasts.

(Guido) I am an Assistant Cost and Rate Analyst.

Q. Please summarize your education and experience.

A. (Bunt) I received an Associate in Science Degree in Business Administration from Dutchess Community College in 1984. In 1986, I graduated from the State University of New York at New Paltz with a Bachelor of Science Degree in Business Administration. I received a Master of Business Administration Degree with a concentration in Finance from Marist College in January 1994. Following about one year of employment as an internal auditor for a retail chain I was employed by Central Hudson in June 1987 as an Accounting Trainee in the Internal Audit Division. I was promoted to Assistant Auditor in 1989 and subsequently transferred to the position of Assistant Financial Analyst in the Financial Planning Division later that year. I was promoted to Associate Financial Analyst in 1991, to Regulatory and

Financial Analyst in 1993 and to Senior Regulatory and Financial Analyst in 1996. I was transferred to the position of Rates and Forecasts Analyst in the Cost and Rate Division in 1997 and promoted to my current position in September 2002.

(Guido) I received an Associate in Science Degree in Business Administration from Ulster County Community College in 2005. In 2007, I graduated from the State University of New York at New Paltz with a Bachelor of Science Degree with a double major in Marketing and Management. I received a Master of Business Administration Degree with a concentration in Management from the State University of New York at New Paltz in May 2009. I was employed by Central Hudson in January 2008 as an Assistant Cost and Rate Analyst.

Q. Have you previously testified before this Commission?

A. (Bunt) Yes. I have testified before this Commission in Cases 95-G-1034, 05-E-0934, 05-G-0935, 08-E-0887 and 08-G-0888, and have submitted an affidavit in 07-M-1139.

(Guido) No.

Q. What is the purpose of your testimony in this proceeding?

A. Our testimony presents Cost of Service (COS) information regarding the Company's gas and electric operations. We have prepared four separate

embedded COS studies (fully allocated and unbundled per Case 00-M-0504 Unbundling Track guidelines): a historical study and a pro forma study of gas operations; and, a historical study and a pro forma study of electric operations. In addition, as discussed later, we have prepared a hypothetical historical delivery-only electric study. The historical studies pertain to the calendar year ended December 31, 2007. The pro forma studies pertain to the Rate Year of the twelve months ending June 30, 2011.

Q. Have you prepared any exhibits to support your testimony?

A. Yes. We have prepared Exhibits (COSP-1), (COSP-2) and (COSP-3) which include the following schedules:

Exhibit (COSP-1)-Gas Department Embedded Study:

Schedule A - Gas Department Rate of Return Statement for the Historical Year 2007;

Schedule B - Gas Department Rate of Return Statement for the Pro Forma Rate Year 7/2010-6/2011;

Schedule C - Gas Department Levelized Revenue Requirement for the Pro Forma Rate Year 7/2010-6/2011 with a targeted ROR to illustrate a potential rate structure with unbundled components.

Exhibit (COSP-2)-Electric Department Embedded Study:

Schedule A - Electric Department Rate of Return Statement for the Historical

Year 2007;

Schedule B - Electric Department Rate of Return Statement for the Pro Forma Rate Year 7/2010-6/2011;

Schedule C - Electric Department Levelized Revenue Requirement for the Pro Forma Rate Year 7/2010-6/2011 with a targeted ROR to illustrate a potential rate structure with unbundled components.

Exhibit (COSP-3)-Electric Department Delivery-Only Hypothetical Embedded Study:

Page 1 of 2 - Electric Department Delivery-Only Hypothetical Rate of Return Statement

Page 2 of 2 – Summary of Assumptions

Q. What is the purpose of an embedded cost of service study?

A. The basic purpose is to determine the earned rate of return (ROR) on rate base by service class in order to evaluate the relationship between current rates being charged to each customer class and the costs incurred to serve each customer class. Basically, revenues less expenses divided by rate base yields the ROR, an estimate of net income received for each dollar invested to provide service.

Q. What is the difference between a historical COS and a pro forma COS?

A. A historical COS uses actual data as recorded on the Company's books for a particular calendar year, in this case 2007. A pro forma COS utilizes rate year forecasts for system loads, revenues, expenses, and rate base to develop an estimated ROR by service class. Together, the historical and pro forma studies allow for a comparison of realized to expected rates of return based on the current rate structure, which became effective as of July 1, 2009.

Q. What is the intent of the historical year COS studies?

A. To document actual realized rate base, revenues and expenses by rate class that are reconcilable to Central Hudson’s Annual Report to the State of New York Public Service Commission (PSC); and, to facilitate the unbundling of rates by reference to actual calendar year labor and expenses by PSC account and Central Hudson function number.

Q. What is the primary purpose of the rate year COS studies?

A. To provide a frame of reference and guidance for the design of cost-based delivery service rates that will produce relative ROR uniformity among the various rate classes and a fair rate of return on the Company’s investments.

Q. Please outline the methods used to prepare an embedded cost of service.

A. The basic procedure is to allocate rate base, expenses, and revenue among

the various service classes via a three step process of (1) functionalization, (2) classification of investment and expenses; then, (3) allocation of those “costs” among the service subclasses.

Q. Please explain what is meant by the term "functionalization".

A. Functionalization characterizes the analysis and re-grouping of the various plant investment and expenses according to the activity or "function" for which the cost was incurred rather than by the FERC/PSC account number to which it was booked. The conventional "functions" are production-related, transmission-related, distribution-related or customer-related (PTDC).

Q. How did you determine the function of a cost?

A. Company accounting records and data maintained for engineering purposes are the principal sources of information used in the functionalization process. Personnel from the Company's accounting and engineering areas also provided assistance in identifying the particular function or functions of specific investments.

Q. Would you please provide an example of a functionalized cost?

A. Costs recorded in the Electric Plant Account 353, Transmission Station Equipment, averaged about $83.5 million in 2007. Records as to the type and location of the equipment represented by this investment indicate that

about $1.3 million served a production function; $66.3 million served a power supply transmission function; $15.7 million - a distribution function and about $100,000 served a specific class of customers. As a result, the $1.3 million would be functionalized to production, the $66.3 million to transmission, the $15.7 million to distribution, and the $100,000 is specifically assigned to a specific class of customers.

Q. Please explain what is meant by the term "classification".

A. Classification refers to the process of separating the functionalized costs into amounts related to demand, energy or number of customers. Demand-related costs vary in proportion to the rate (in kW or Mcf) at which customers utilize electricity or natural gas. Energy-related costs vary in proportion to the total volume of the electricity or natural gas delivered. Customer-related costs vary in proportion to the number of customers served. A smaller, fourth category of costs, specifically-assigned, defines costs that can be attributed to a particular service class of customers.

Q. Regarding your example of the functionalization of Electric Account 353, how did you proceed to classify these costs?

A. Since virtually all of the equipment included in Account 353 must be sized to meet the expected maximum collective demand of all customers, the non-specific functional categories (production, power supply transmission and

distribution) were classified as demand-related investment. The remainder, about $100,000, was specifically assigned.

Q. Please explain what is meant by the term "allocation".

A. Allocation refers to the process of distributing the functionalized and classified costs among the service classes on the basis of service class contribution to peak[1] demand (in kW); or, class contribution to total volume of electricity delivered (i.e. energy in MWh); or, class contribution to total number of customers; or, by direct assignment to a specific rate class when appropriate.

Q. Continuing with your Account 353 example, how was the plant investment ultimately allocated?

A. Investments functionalized as “production” and "power supply transmission" were allocated to the various service classes on the basis of their respective contribution to the average of the summer and winter coincident peak demands. Investment functionalized as "distribution-related" was allocated per class contribution to the class non-coincident peak demand at the

1 Several types of ‘demand’ allocators are used: Summer/Winter Coincident Peak (CP) demand, Class NCP (non-coincident peak kW); Sigma NCPi (sum of individual customer’s peak demand).

substation level of service. Investments functionalized as “specific” were directly assigned to the rate classes of customers to be served by that investment.

Q. What major sources of information were used to develop the historical cost of service studies?

A. The "Electric Utility Cost Allocation Manual" dated January 1992 by the National Association of Regulatory Utility Commissioners was used as the basic reference on cost of service methodology. Company accounting and engineering records yielded additional information for the functionalization and classification of various costs. The Company's Annual Report to the PSC for the year ended December 31, 2007 was the principal source for Income Statement items and Operation & Maintenance expenses. The Company developed electric demand allocators from a comprehensive load research program. Finally, Company billing records yielded number of customers, kWh/Mcf sold/delivered and revenues by rate code and service class.

Q. What major sources of information were used to develop the rate year pro forma cost of service studies?

A. The Company’s Revenue Requirements Panel provided rate year income statements for both gas and electric, which included estimates for future rate

base, O&M, depreciation and amortization and other operating expenses. The Company's Forecasting & Rates Panel provided revenue, sales and customer forecasts. Details regarding future plant investments, depreciation reserve and taxes came from the Accounting department. Rate year demand allocators were developed by applying the ratio of historical kWh/customer/class: kW/customer/class to the forecast kWh/customer/class. Application of historical COS results to rate year data yields an expected ROR on rate base by customer class, given currently effective rates. A comparison of class ROR to the system average ROR will indicate which rates need to be adjusted in order to improve the system average ROR and/or reduce interclass subsidies.

Q. How many service classes and subclasses do your studies address?

A. The electric department COS studies address twelve subclasses: SC1-residential general/non-heating, SC1-residential heating, SC6-residential time-of-use, SC2-small general service non-demand metered, SC2-small general service secondary demand metered, SC2-small general service primary demand metered, SC3-large general primary, SC13-large general substation, SC13-large general transmission, SC5-area lighting, SC8-street lighting and SC9-traffic signals.

The gas department COS studies address nine subclasses: SC1-residential heating, SC1-residential non-heating, SC2-commercial/industrial heating,

SC2-commercial/industrial non-heating, SC8 & 9-interruptible, SC11dlm-firm distribution large mains, Interdepartmental (Central Hudson's own use of gas), SC11t-firm transmission and SC11d-firm distribution.

Q. With respect to the specific process, how did you classify production plant in the Electric COS studies?

A. Consistent with the decision in Case 00-E-1273, hydroelectric production plant was classified energy-related; combustion turbines were classified demand-related.

Q. How did you classify production plant in the Gas COS studies?

A. As in Cases 90-G-0673, 92-G-1056, 95-G-1034, 00-G-1274, 05-G-0935 and 08-G-0888, gas production plant was classified 100% demand-related since the Company's gas production investment is in propane peaking facilities utilized to meet anticipated winter peak demand.

Q. Have you made any significant changes to the manner in which the Company functionalized, classified or allocated items as compared to the approach filed by the Company in Cases 08-E-0887 and 08-G-0888?

A. Yes, consistent with the Commission’s Order in Case 08-E-0887, the allocation of procurement costs in the instant electric historic and pro forma COS studies has been changed. Previously, procurement costs were

allocated volumetrically on total energy deliveries. In the instant case, procurement costs have been allocated based on average number of billed customers in order to reflect an allocator that does not vary with volume, as prescribed by the Commission.

The gas historical and pro forma COS studies submitted in the instant case reflect gas mains costs allocated on the basis of 65% demand and 35% customer as prescribed by the Commission in the determination of rates in Case 08-G-0888. The studies also allocate the costs of the two downstream meters at West Point across the customer classes, including West Point, also as prescribed by the Commission in Case 08-G-0888. Additionally, the gas pre-allocator CSTMRS (total number of customers in the customer class divided by the total number of customers on the system) has been substituted for the pre-allocator CSTMRS2 (number of Metretek and Power Spring metered customers in the customer class divided by the total number of customers on the system having such demand meters). Finally, the development of the gas pro forma net plant by functional category in the new study reflects the functional detail underlying the net plant forecast developed by the Accounting Panel, consistent with the method utilized for the development of the electric pro forma net plant by functional category. This differs from the method utilized in Case 08-G-0888, wherein the gas pro forma net plant by functional category was developed by apportioning plant to functional category based on the historic COS plant balances.

Q. How are the costs of gas distribution mains less than six inches in diameter treated in the new studies?

A. Gas mains of less than six inches in diameter are allocated to customers other than the SC11dlm-firm distribution large mains class and the SC11t-firm transmission class.

Q. Please describe the distribution mains allocator utilized for the SC11dlm-firm distribution large mains class.

A. The distribution mains allocator utilized for this class has been adjusted to remove costs related to distribution mains less than 6-inches in diameter.

Q. Earlier in your testimony you made reference to unbundled functions and Case 00-M-0540. Please describe the requirements for unbundling and the results.

A. The Unbundling Track of Case 00-M-0504 required Central Hudson to file fully allocated embedded COS studies with unbundled rates based on those studies. In compliance, the Company filed such studies in Cases 05-E-0934, 05-G-0935, 08-E-0887 and 08-G-0888 that led to the implementation and continuation of the unbundled Merchant Function Charges (MFCs) that currently appear on customers' bills.

Q. Are the COS studies that you are sponsoring fully unbundled?

A. Yes. The electric and gas embedded COS studies prepared for this rate case identify the revenue requirements for bundled and unbundled components. Cost-based potential MFCs for customers taking commodity service from an Energy Services Company (ESCO) have been updated and are shown in Exhibit__(COSP-1) Schedule C for gas customers and Exhibit__(COSP-2) Schedule C for electric customers.

Q. How many cost components have you unbundled?

A. Four for the gas department and seven for the electric department.

Q. Could you please identify each of the unbundled components and explain the different number of unbundled functions for gas and electric?

A. The unbundled components common to both gas and electric departments include: procurement; credit & collections; bill printing, mailing and receipt services (BPRS); and, competitive energy services (CES). The unbundled components unique to the electric department include meter ownership, meter services and meter data services. The PSC has not yet mandated competitive metering for gas customers.

Q. How do these categories compare to the categories adopted by the Commission in its June 2009 rate order in Cases 08-E-0887 and 08-G-0888?

A. These categories are the same as those adopted by the Commission in its June 2009 rate order in Cases 08-E-0887 and 08-G-0888.

Q. Could you please identify the kinds of costs that are included in each of the unbundled component's revenue requirements?

A. Procurement includes shares of common plant, labor & expenses, including credit and collections costs related to commodity, for the acquisition of commodity for Central Hudson customers, allocated shares of call center costs and allocated shares of PSC accounts 905, 908 and Administrative & General O&M accounts 920 through 932 proportionate to full service credit & collections expenses.

The Credit & Collections (for delivery service) revenue requirement includes a share of account 904 (Uncollectible Accounts) proportionate to bad debt on delivery service as well as allocated shares of call center, credit and collections, bill complaints, and shares of 905, 908 & 920 through 932 proportionate to labor & expenses concerning delivery service credit & collections.

The BPRS revenue requirements and unbundled costs include labor and expenses attributable to the cash processing department, the annual charges of the vendor currently contracted by Central Hudson to print and mail bills plus allocated shares of call center costs and shares of expenses booked to

PSC accounts 905, 908 & 920 through 932.

CES includes the labor and expenses of any marketing efforts and advertising expenses related to sales promotions, plus an allocated share of call center costs and shares of expenses booked to PSC accounts 905, 908 & 920 through 932.

Regarding the unbundled components unique to the electric department: meter ownership reflects the service class average meter cost and average initial installation costs for non-demand meters but only the class average meter cost for demand metered customers; meter services reflect the class average avoidable maintenance expense per meter; and, meter data services reflect the class average meter reading cost.

Q. Please briefly describe the methods used to assign labor and expenses to each of the unbundled functions.

A. The analysis began with the compilation of year 2007 labor expenses (by internal area and function number) as recorded in each PSC account greater than or equal to 900.00; roughly 300 function numbers in the electric department and 200 in the gas department. Most areas within Central Hudson use 900 series accounts only for overhead-type functions (e.g., general office salaries); consequently, these labor expenses were temporarily functionalized as PTDC-related for later functionalization on labor sub-total across all functions. Several areas, however, use 900 series

accounts to record virtually all expenses. Labor and expenses in each of these areas were examined in detail and unbundled as appropriate.

Briefly, all labor and expenses booked to account 902, meter reading, were unbundled for the electric department but left bundled with customer accounts expenses for the gas department. Expenses booked to PSC account 904, Uncollectibles, were split proportionately between commodity-related bad debt and delivery service-related bad debt. Expenses booked to PSC account 903 by the call center were allocated to the various bundled and unbundled functions per surveys of call types from customers. Credit & collections costs booked to 903 were split like uncollectibles: to commodity-related procurement vs. delivery-service-related expenses. With the exception of bill printing and mailing vendor costs, most labor and expenses booked to PSC account 905 were functionalized per the unbundled subtotal of 902 & 903 labor. As previously mentioned, vendor charges for printing and mailing bills to customers were unbundled to the BPRS function together with labor and expenses from our cash processing department (from accts 903, 905, 908 and some A&G accounts). Marketing labor and expenses (within 908 & 912) were unbundled to CES together with advertising related to sales promotions (within PSC account 916) and shares of call center costs from several accounts.

Q. How would customers be able to avoid the unbundled costs and MFCs that you have described and shown in Schedule C of Exhibits (COSP-1) and (COSP-2)?

A. The complete array of unbundled costs could be avoided by customers who contract with an ESCO for commodity service, choose to have a single bill issued by the ESCO (an ESCO that agrees to assume all credit and collections costs); and, if an electric customer, contracts with a third party for all metering services.

Q. Are any current retail access/delivery service customers avoiding the full range of unbundled components?

A. No, not at this time. Currently, we have no retail access customers who have chosen to have a single bill issued by the ESCO. We do have customers who have chosen a single bill issued by Central Hudson and they receive a BPRS credit but the ESCO reimburses Central Hudson for that cost. Moreover, a customer would not be able to avoid the full range of unbundled components unless the billing ESCO assumed all uncollectibles, credit and collections responsibilities.

Q. Please briefly describe the results of the Gas Department COS studies.

A. Schedule A (the historical study) and Schedule B (the pro forma study) of Exhibit __ (COSP-1) summarize the rates of return for the system and for

service subclasses. Line 9 on each of the schedules details Rate Base by service class; Line 12 shows Total Operating Revenues; Line 18 shows Total Operating Expenses; Line 19 shows Operating Income (line 12 less line 18); and, Line 20 shows Rates of Return (line 19 divided by line 9).

The Index of Return, Line 21, indicates the relative degree of difference between the system total ROR and the ROR of each service class (100 signifies a ROR equal to the System ROR; 85 and 115 respectively indicate a ROR 15% less than and 15% greater than the System ROR).

The results from the historical gas COS study show the rates of return from four of the seven rate classes (excluding SC8&9 - interruptible and Interdepartmental) to be below the system average ROR.

The results shown in Exhibit __(COSP-1), Schedule B, the pro forma rate year gas COS study, reveal the system average ROR at 6.34%, below the 7.28% allowed for the rate year under the Order in Case 08-G-0888 issued and effective June 22, 2009, with four of seven classes also below the system average ROR.

Exhibit__(COSP-1) Schedule C Page 1 of 2 shows the approximate gas department revenue requirements by function to achieve a system average ROR of 7.58%, from each customer class. Exhibit__(COSP-1) Schedule C Page 2 of 2 develops (from Page 1) bundled delivery service rates (lines 53,

54 & 55) for each service class and potential credits for each of the unbundled components (lines 56-59). Finally, lines 60-63 develop delivery service rates with unbundled Merchant Function Charges (MFCs) for Administration (MFC_A) and Supply (MFC_B) for each rate class.

Q. What customers might be eligible to avoid MFC_A and MFC_B?

A. Any Retail Access customer of an ESCO that provided a single bill and assumed all credit and collection responsibilities would be eligible to avoid both MFC_A and MFC_B. A gas customer electing Retail Access service, with dual billing or single billing from Central Hudson, would be eligible to avoid only the Supply Charge, MFC_B (the Procurement and CES unbundled components; re: line 62).

Q. Please briefly describe the results of the Electric Department embedded COS (ECOS) studies.

A. Exhibit__(COSP-2) Schedule A (the historical year electric study) and Exhibit__(COSP-2) Schedule B (the pro forma study) similarly summarize the rates of return for the electric system and show the allocation of Rate Base, Revenues, Operating Expenses and resultant ROR by each customer rate classification.

Again, the Index of Return indicates the relative degree of difference between the system total ROR and the ROR of each service class (100

signifies a ROR equal to the System ROR; 85 and 115 respectively indicate a ROR 15% less than and 15% greater than the System ROR).

The results from the 2007 electric department COS study reveal indexes below 85 for the SC5 & SC8 lighting classes, SC1-Non-heat, and SC2-non-demand. All other classes had RORs above the 2007 system average ROR.

Exhibit__(COSP-2) Schedule B details the pro forma delivery service forecasted costs and expected revenues as allocated by the embedded electric cost of service study to the rate classes; and, the estimated rates of return by class. Schedule B shows the SC2 non-demand, SC13 substation, SC13 transmission and the SC5 lighting classes to be below a system index of 85, SC2 primary-demand is at the system index of 85, and all other classes are above an index of 85.

Exhibit__(COSP-2) Schedule C shows the revenue required to produce a targeted system average ROR of 7.58% from each service class (i.e. “levelized” revenue requirements), together with a potential rate structure for delivery service with potential credits for each of the unbundled components. The levelized bundled rates are shown in lines 60 through 62 and the unbundled credits potentially available to any retail access electric customer shown in lines 63 through 69.

Q. What might be the minimum Merchant Function Charge that a retail access electric customer might avoid?

A. An electric customer choosing an ESCO for commodity service with a two bill option or a single bill from Central Hudson would be eligible for MFC_B (reflecting the procurement credit shown on line 63 and the CES credit shown on line 69). The combined backout expressed in $/kWh is shown in line 73.

Q. What might be the maximum delivery MFC that a retail access electric customer could avoid?

A. An electric customer choosing an ESCO for commodity service that issued a single bill and assumed all credit and collections responsibilities for delivery service would be eligible to avoid both the Supply and the Administrative Merchant Function Charges (respectively MFC_B and MFC_A shown in Schedule C, page 2, lines 73 and 74).

Q. Are there any differences between the 2007 historical COS studies and the rate year studies?

A. Yes, the historical studies include rate base, revenues and expenses associated with commodity purchases of electricity and gas as well as delivery service rate base, revenues, and expenses. In contrast, the rate year studies contain neither fuel-related expenses nor expenses for the

purchase of electric or gas commodities.

Q. Has the Commission addressed these differences?

A. Yes. In its Order in Case 08-E-0887 the Commission required that the Company submit a delivery-only historic embedded cost of service study with its next electric rate filing. As a result, we have prepared such a study, which is summarized in Exhibit__(COSP-3). However, preparation of this study required that a number of gross simplifying assumptions be made regarding the identification and separation of revenues, certain expense items including federal and state income tax, and adjustments to rate base. As a result, we do not believe that the study accurately depicts historic results that may have been achieved if Central Hudson operated as a delivery-only company.

Q. Please discuss the preparation of a gas marginal cost of service study.

A. In its June 2009 Order, the Commission required that the Company file a gas marginal COS study with its next gas rate filing. The Commission also recognized that the Company might not have adequate time to complete such a study prior to its next filing. As Central Hudson has not previously been required to file a marginal COS study, such studies require a significant amount of time to prepare, and the Order requiring such a study was only issued June 22, 2009, we have not been able to complete a gas marginal COS study in time to include it with this filing, but believe that we could

submit such a study by December 1, 2009. Since the stated use for the study is in relation to the gas tail block rate design, this schedule should allow adequate time for consideration of the study in this case.

Q. Does this conclude your pre-filed direct testimony?

A. Yes.