BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

In the Matter of

Central Hudson Gas & Electric Corporation

Cases 08-E-0887 & 08-G-0888

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Prepared Direct Testimony of:

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MICHAEL M. TWERGO

Q. Please state your name and business address.
A. My name is Michael M. Twergo and my business address is Three Empire State Plaza, Albany, New York 12223.
Q. What is your occupation?
A. I am a Utility Supervisor with the staff of the Office of Electric, Gas and Water, New York State Department of Public Service.
Q. Please summarize your education and professional experience.
A. In December 1981, I graduated from Rensselaer Polytechnic Institute with a Bachelor of Science degree in Electrical Engineering. Since joining the Department of Public Service in April 1982, I have held progressive engineering positions within the Office of Electric, Gas and Water and its predecessors. My responsibilities include the management, supervision and performance of technical analyses and investigations of a variety of filings submitted by New York

electric utilities inclusive of Central Hudson Gas and Electric Corporation (Central Hudson or the Company). These analyses have related to construction contracts, small power contracts, property transfers, capital expenditures, electric system modeling, revenue forecasting, embedded and marginal cost of service studies, interclass revenue allocation, intraclass rate design, commodity portfolio management, and the design and operation of various rate mechanisms.

Q. Have you previously testified before the New York State Public Service Commission?

A. Yes, I have testified before the New York Public Service Commission in numerous proceedings.

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

A. The purpose of my testimony is to present Staff's recommendations addressing Central Hudson's proposed:

- Electric Revenue Decoupling Mechanism,

- Retail Access Lost Revenue Recovery Mechanism, and
- Energy Cost Adjustment Mechanism.

Q. Are you sponsoring any exhibits?

A. Yes. I am sponsoring two exhibits: Exhibit___ (MMT-1) and Exhibit___ (MMT-2).

Electric Revenue Decoupling Mechanism

Q. What is a revenue decoupling mechanism?

A. As the Commission states in its ORDER REQUIRING PROPOSALS FOR REVENUE DECOUPLING MECHANISMS (RDM Order) in Cases 03-E-0640 and 06-G-0746, issued April 20, 2007, a revenue decoupling mechanism (RDM) is a ratemaking approach designed to eliminate or substantially reduce the linkage between sales and utility revenues and/or profits. It functions by comparing actual versus authorized total revenues or revenues per customer and either crediting or collecting any differences from customers in a subsequent period.

Q. Why is an RDM necessary?

A. An RDM is necessary because utilities' existing rate designs are, in most cases, not "optimal" in that they do not collect fixed costs through fixed charges and variable costs through variable charges. To the degree that utility fixed delivery costs are recovered from customers on a volumetric basis, there remains a net lost revenue and profit effect that may discourage utilities from actively promoting energy conservation and behind-the-meter renewable technologies and other forms of distributed generation. An RDM removes this disincentive.

Q. Has the Commission addressed the need for each utility to file an RDM?

A. Yes. In the RDM Order the Commission directed the utilities to file proposals, in ongoing and new rate cases, for true-up based RDMs. The filings were to include proposals for limiting

customer bill impacts and price volatility, to the extent practical. Specifically, on page 16 of the RDM Order the Commission ordered that RDMs should incorporate the following:

"1. The mechanism should be designed to true-up forecast and actual delivery service revenues for a given time period;

2. The mechanism should be designed to prevent gaming by the utility (e.g., shifting customers to different classes);

3. The recovery of any net lost revenues component of the mechanism should not, in and of itself, produce inter-class revenue re-allocations between customer classes, and that such re-allocations should only be made purposefully after considering a current fully-allocated cost of service study; and,

4. All remaining design and implementation issues should be addressed in individual rate proceedings."

In addition, the Commission also identified a number of design and implementation issues that should be considered when developing an effective RDM. Specifically, whether the RDM needs to be applied to all or only some customer classes and whether allowed revenues should be calculated on a per customer basis or a total delivery revenue per class basis.

Q. Has Central Hudson complied with the Commission's Order to file an RDM proposal in the instant electric rate case?

A. Yes. The Company's Electric Forecasting Panel, beginning on page 55 of its direct testimony, is proposing the implementation of an RDM to become effective with the commencement of the rate year.

Q. Please elaborate.

A. The Company's proposed RDM design is based on a unit or usage per customer (UPC) model. The RDM would be applicable to SC1 (residential), SC2

(small & medium C&I), SC3 (large C&I, primary), SC13 (large C&I, substation & transmission) and SC14 (standby service). SC5 and SC8 (street lighting), and SC9 (traffic signals) are proposed to be exempt. RDM refund/recovery factors are proposed to be calculated monthly and included in bills with meter-read dates after the effective date of the factors.

Q. Do you recommend that the Commission approve Central Hudson's RDM proposal?

A. No. My review of the Company's proposal revealed several shortcomings of the proposed RDM mechanics. In summary, these are:

- The UPC RDM model over-compensates or over-penalizes the utility for variances from the rate year customer forecast;
- The UPC RDM model charges ratepayers for "lost revenue" for efficient customer additions;
- The proposed methodology permits the over or under recovery of revenues associated with

Merchant Function Charges (MFC);

- Application of an RDM to certain classes has the potential for creating detrimental bill impacts; and
- The proposed frequency of the RDM refund/recovery billing factors could introduce unnecessary volatility to the delivery portion of customer bills.

Q. Please elaborate on your first observation that the UPC RDM model over-compensates or over-penalizes the utility for variances from the rate year customer forecast.

A. A UPC RDM model allows the utility to retain the average per customer forecast delivery revenues for customers incremental to the rate year forecast. A simple example would be to assume that a service class was forecast to have 100 customers, collectively using 70,000 kWh in a month, yielding an average UPC of 700 kWh. If the utility were to gain customers that also

averaged 700 kWh each for the month, all else equal, the RDM adjustment would be zero and the utility would retain those customers' delivery revenues. Similarly, if the utility were to lose customers that averaged 700 kWh each for the month, all else equal, the RDM adjustment would also be zero and the utility would lose those customers' delivery revenues. In either case, however, the retained (or lost) revenues would exceed the incremental (or avoided) revenue requirement.

This occurs because average revenues recover costs that do not vary with the number of customers or sales. A review of the testimony of the Company's Revenue Requirement Panel reveals numerous costs that are forecast independent of the number of customers or sales.

The Company's Electric Forecasting Panel testifies on page 65 that increased customer levels entail increased costs. The Panel

continues that additional customers require additional plant investment for connection to the system, resulting in increased depreciation expense. This is true to varying degrees.

New construction by customers necessitating system expansion does require additional capital investment. Central Hudson rightfully minimizes these costs, as Company Witness Mosher states in his direct testimony on pages 18 and 19, by consistently enforcing its existing tariff so as to place cost responsibility on developers or others who wish to connect under conditions that exceed the existing line extension parameters. Significantly less investment is required to serve new customers moving to locations that previously received utility service. The incremental revenue requirement associated with new customers is less than the revenues retained by the utility under the UPC RDM model.

Q. Please explain your second observation that the

UPC RDM model assesses ratepayers for “lost revenue” for efficient customer additions.

A. Previously, I explained that if the average UPC of incremental customers was equal to the forecast UPC, there would be no RDM adjustment and the utility would retain the additional delivery revenues. If however the premises of the incremental customers were energy efficient and consumed, on average, less than the UPC forecast level, in addition to retaining those customers’ full delivery revenues, the UPC RDM model would, all else equal, indicate that the utility experienced a revenue shortfall collectible from ratepayers within the same service class. The revenues retained and collected by the utility under the UPC RDM model would exceed the incremental revenue requirement and bill impacts would result from the RDM surcharge.

Q. Please describe your third observation that the

Company's proposed RDM methodology permits the over or under recovery of revenues associated with Merchant Function Charges.

A. As the Company confirmed in response to Staff interrogatory DPS-439 [Exhibit___(MMT-1), Schedule 1], the proposed electric RDM methodology does not reconcile MFC-related revenues for retail access customers associated with differences in the sales volumes compared to forecast. So, for example, if a retail access customer increased (or decreased) their kWh consumption, all else being equal, the MFC revenues gained (or lost) associated with such a change in usage would not be captured by the Company's proposed RDM.

Q. Please expand upon your fourth observation that application of an RDM to certain classes has the potential for creating detrimental bill impacts.

A. As mentioned previously, Central Hudson proposes that its electric RDM be applicable to the SC13

– Substation and SC13 – Transmission large C&I service subclasses. These two subclasses are each forecast to have seven customers during the rate year. Given the limited number of customers in each of these subclasses combined with the differences in their billing demands, application of an RDM to these classes may result in severe bill impacts for the remaining customers within these two subclasses if one or more customers materially curtails their usage or leaves the system entirely.

Q. Please describe your fifth observation that the proposed frequency of the RDM refund/recovery billing factors could introduce unnecessary volatility to the delivery portion of customer bills.

A. Central Hudson proposes that RDM refund/recovery factors be determined on a calendar month basis by service class and applied to each month’s delivery bill; the average of two months’ RDM

factors will be applied to bimonthly bills. If the RDM refund/recovery factors are calculated and applied on each bill it is possible that the factors for a given service class will vary substantially each month or perhaps change from a refund to a charge, thus introducing volatility to delivery rates that could be avoided or minimized by modifying the RDM refund/recovery mechanism.

Q. What do you recommend to address the shortcomings of Central Hudson's proposed RDM?

A. I recommend that a delivery revenue per class RDM be employed by Central Hudson, similar to the electric RDMs approved for Consolidated Edison Company of New York and Orange & Rockland Utilities.

Q. Please describe your proposed RDM.

A. Under my proposal, RDM targets will be computed for each class or subclass for each month of the rate year as the sum of the forecast revenues

associated with the customer charge, base rate delivery energy charge (if any), base rate delivery demand charge (if any), base rate delivery reactive demand charge (if any) and Merchant Function Charges for that class or subclass. Each month, actual revenues from those same rate elements will be computed and compared with the RDM targets to determine the excess or shortfall of revenue.

Q. How will the refund or collection be accomplished?

A. Total monthly revenue excesses or shortfalls for each class or subclass will be aggregated over the 12-month rate year to yield the total rate year per class or subclass revenue excess or shortfall. This revenue will either be refunded to or collected from customers, in the respective causative class or subclass, on a per kWh (for non-demand metered classes) or per kW (for demand metered classes) over the following

twelve month period upon submittal of a newly-created Statement of RDM Adjustment filed with the Commission prior to the factors becoming effective. The unamortized monthly balances will accrue carrying charges at the other customer capital rate.

In the event that the algebraic sum, for all classes or subclasses, of the cumulative monthly excesses or shortfalls (exclusive of carrying charges) exceed $4 million prior to the end of the rate year, the per class or subclass revenue excess or shortfall will immediately begin to be either refunded to or collected from customers in the respective causative class or subclass. The refund or collection will occur over a twelve month period upon submittal of a Statement of RDM Adjustment filed with the Commission prior to the factors becoming effective. To prevent unnecessary bill volatility, RDM disbursement and/or collection

factors may only be changed once in any given six-month period. I selected a $4 million threshold to initiate an RDM adjustment based on the product of the $3 million threshold approved by the Commission for Orange & Rockland Utilities, Inc. in its ORDER ESTABLISHING ELECTRIC RATE PLAN FOR ORANGE AND ROCKLAND UTILITIES, INC. in Case 07-E-0949, issued July 23, 2008, and the ratio of the two utilities' delivery revenues.

Q. Which classes do you propose be subject to the RDM?

A. I propose that the RDM be applicable to SC1 (residential), SC2 (small & medium C&I), SC3 (large C&I, primary), and SC14 (standby service). SC5 and SC8 (street lighting), SC9 (traffic signals), and SC13 (large C&I, substation & transmission) are proposed to be exempt.

Q. Why do you propose that SC5, SC8 and SC9 be

exempt from the RDM?

A. As explained in the direct testimony of Central Hudson's Electric Forecasting Panel, beginning on page 57, the rate structure for SC5 and SC8 is based on fixture type and the rate structure for SC9 is based on signal face.

Q. Why do you propose that SC13 - Substation and SC13 – Transmission be exempt from the RDM?

A. The Company's response to Staff interrogatories DPS-135, [Exhibit___(MMT-1), Schedule 2] and DPS-136, [Exhibit___(MMT-1), Schedule 3] shows the proposed rate year monthly billing demands for each customer within SC13 – Substation and SC13 – Transmission, respectively. Exhibit___(MMT-2), Schedule 1 and Schedule 2, respectively, reproduces this data as well as the calculated average annual billing demand for each customer and the total annual average billing demand for the subclass. Due to the limited number of customers in each of these

classes combined with the differences in their billing demands, I am concerned that application of an RDM to these classes may result in severe bill impacts if one or more customers materially curtailed their usage or left the system entirely. Also, as noted in the Company's response to Staff interrogatory DPS-446 [Exhibit___(MMT-1), Schedule 4], there are no identified Energy Efficiency Portfolio Standard programs for these two subclasses which promote energy efficiency, thus further reducing the need for an RDM. As a result, I am proposing that these two subclasses be exempt from the RDM.

Q. Do you propose that the RDM continue beyond the rate year?

A. Yes. Absent a new rate case filing by Central Hudson that would allow new RDM targets to be in place beyond the conclusion of the rate year, I propose that the RDM continue and the monthly

RDM targets repeat, thus continuing to support the Commission's energy efficiency goal.

Q. Please summarize your RDM proposal.

A. I propose a delivery revenue per class/subclass RDM which will reconcile actual revenues to forecast revenues associated with the customer charge, base rate delivery energy charge, demand charge, reactive demand charge and Merchant Function Charges for each class/subclass for each month.

Total monthly revenue excesses or shortfalls for each class/subclass will be aggregated over the 12-month rate year to yield the total per class/subclass revenue excess or shortfall. This revenue will either be refunded to or collected from customers, in the respective causative class/subclass, on a per kWh or per kW basis over the following twelve month period.

If the sum for all classes/subclasses, of

the cumulative monthly excesses or shortfalls exceed $4 million prior to the end of the rate year, the per class/subclass revenue excess or shortfall will immediately begin to be either refunded to or collected from customers, in the respective causative class or subclass. The refund or collection will occur over a twelve month period. However, RDM disbursement and/or collection factors may only be changed once in any given six-month period.

The RDM will be applicable to only SC1, SC2, SC3, and SC14.

Retail Access Lost Revenues

Q. How are lost revenues associated with Central Hudson's retail access program currently recovered from ratepayers?

A. Pursuant to the procedure contained in the Commission's ORDER ESTABLISHING RATE PLAN in Cases 05-E-0934 and 05-G-0935, issued July 24, 2006, fifty percent of the forecast lost revenue

is recovered by adding a separate component to the MFC Supply Charge on a MFC group-specific basis. The remaining fifty percent of forecast net lost revenues is recovered through the MFC group-specific Transition Adjustment. At the end of each rate year, a reconciliation is performed between the actual retail access-related lost revenue and the amount of retail access-related lost revenue recovered from ratepayers.

Q. Do you recommend that the current methodology employed by Central Hudson to recover retail access lost revenues from customers continue during the rate year?

A. No. In order to avoid unintended interaction with the RDM, potentially resulting in over or under recovery of MFC-related revenue, and to simplify rates, I recommend that Central Hudson’s current retail access lost revenue mechanism be eliminated. In its place, I

recommend that a forecast of lost MFC revenues associated with the Company's retail access program be incorporated into base delivery rates.

The revenue per class RDM, as I propose above, will reconcile the forecast retail access-related lost revenues incorporated into base delivery rates with the level actually experienced. Incorporating a forecast of lost MFC-related revenue into base delivery rates, all else equal, will minimize future RDM adjustments because the majority of lost revenues will be recovered through base rates while only variations from that amount will be refunded or recovered through the RDM.

Q. How do you propose to reconcile forecast lost MFC-related revenue incorporated into base delivery rates with actual retail access-related lost revenue for classes and subclasses not subject to an RDM?

A. I recommend that at the conclusion of the rate year and each subsequent 12-month period the difference between the actual retail access-related lost revenue and the amount of retail access lost revenue recovered from customers through base delivery rates be calculated on a class/subclass specific basis. Over or under recoveries should be refunded or recovered, over a maximum time period of 12-months, through a newly-created class/subclass-specific Retail Access Reconciliation Adjustment.

Actual retail access-related lost revenue is as defined in Section VI.H.8 of Attachment 1 to the Commission's ORDER ESTABLISHING RATE PLAN in Cases 05-E-0934 and 05-G-0935, issued July 24, 2006. Specifically, the actual net lost revenue for each class/subclass is equal to the actual retail access kWh participation level of customers taking service from ESCOs participating in Central Hudson's Purchase of

Receivables (POR) Program multiplied by MFC_{Supply}, plus the actual retail access kWh participation level of customers taking service from ESCOs not participating in Central Hudson's POR Program multiplied by the sum of $MFC_{Administration}$ and MFC_{Supply}.

Q. Are your proposals regarding recovery of retail access lost revenue consistent with current Commission policy?

A. Yes. In its ORDER DETERMINING FUTURE OF RETAIL ACCESS PROGRAMS in Case 07-M-0458, issued October 27, 2008, the Commission stated on page 16 that "... utilities are authorized to recover [retail access] lost revenues, although it is noted that as part of rate proceedings parties may recommend changes or alternatives to the mechanism to collect retail access related lost revenues."

Energy Cost Adjustment Mechanism

Q. Have you reviewed Central Hudson's proposal

regarding its Energy Cost Adjustment Mechanism.

A. Yes. The Energy Cost Adjustment Mechanism (ECAM) is addressed by Central Hudson's Electric Forecasting Panel beginning on page 49 of its direct testimony.

Q. Do you recommend changes be made to the ECAM?

A. Yes. I recommend that the methodology used to flow through Purchased Power Adjustment (PPA) benefits to customers be modified to more equitably distribute those benefits.

Q. What benefits are flowed through to customers by means of the PPA factor?

A. According to Central Hudson's Electric Forecasting Panel direct testimony on page 51, the net benefits from the Company's Nine Mile Point Unit No. 2 (NMP2) power purchase contract are flowed through to customers by means of the PPA factor.

Q. How are the NMP2 net benefits that are flowed through the PPA allocated to the classes and

subclasses?

A. According to the Company's response to Staff interrogatory DPS-146 (Exhibit___(MMT-1, Schedule 5), the NMP2 net benefits flowed through the PPA are allocated to the classes and subclasses in proportion to delivery kWh sales.

Q. Is this current methodology used to allocate NMP2 net benefits amongst classes and subclasses equitable?

A. Not entirely. The current methodology only allocates NMP2 net benefits in proportion to energy whereas NMP2 capital costs were allocated to classes based on energy and demand.

Q. Please elaborate.

A. Central Hudson's below market price contract for the purchase of energy and capacity from NMP2 is a consequence of the utility selling its nine percent share of the plant to Constellation Energy. During the approximate 13-year operating period that Central Hudson owned its

share of the plant (August 1988 – November 2001), capital costs were incorporated in rate base and classified between demand and energy. This resulted in an allocation of NMP2 capital costs to the classes 25 percent in proportion to demand and 75 percent in proportion to kWh sales in the utility's 1989 and 1991 rate cases (Central Hudson response to Staff interrogatory DSP-498 [Exhibit___(MMT-1), Schedule 6]). In the 1992 and 1996 rate cases, NMP2 capital costs were allocated to classes 38 percent in proportion to demand and 62 percent in proportion to kWh sales (Central Hudson response to Staff interrogatory DSP-148 [Exhibit___(MMT-1), Schedule 7]).

Hence, the capital costs associated with ownership of NMP2 were recovered from ratepayers in a manner somewhat different from the manner in which contract benefits are currently allocated to ratepayers.

Q. How do you propose that NMP2 contract net benefits flowed through the PPA factor be allocated to the classes and subclasses?

A. I recommend that NMP2 benefits be allocated 31 percent in proportion to pro forma embedded cost of service study class/subclass average summer & winter coincident peak demand factors and 69 percent in proportion to class/subclass kWh sales. The classification of benefits as 31 percent demand-related and 69 percent energy-related represents an average of the two demand & energy cost classifications employed by Central Hudson to allocate NMP2 capital costs to the classes during the time it had an ownership interest in the plant.

Q. Does this conclude your testimony at this time?

A. Yes.