

REBUTTAL TESTIMONY
OF
LARRY G. ARVIDSON

CASES 08-E-0887 & 08-G-0888

1 Q. Are you the same Larry G. Arvidson who submitted prefiled direct testimony and
2 supplemental testimony in this proceeding?

3 A. Yes, I am.
4

5 Q. What is the purpose of your rebuttal testimony?

6 A. My rebuttal testimony addresses the prepared testimony of the NYS DPS Staff
7 Gas Rates Panel.
8

9 Q. Please describe the issue that you would like to rebut.

10 A. The Gas Rates Panel (GRP) proposes to make a major modification to the
11 CHG&E gas department embedded cost of service (COS) studies to shift
12 significant cost responsibility from residential customers to commercial industrial
13 customers by abruptly abandoning the minimum intercept method of classifying
14 mains between customer-related and demand related.
15

16 Q. What was the effect of the GRP modification to the embedded COS studies?

17 A. The GRP classified distribution mains as 100% demand-related, which shifted
18 approximately \$13 million dollars (or about 20% of the total gas revenue
19 requirement) in revenue requirement responsibility from being allocated on

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1 number of customers (per the Company COS study re: Exhibit_(LGA-1),
2 Schedule C, Page 1 of 2 lines 15 & 16) to a total of \$23.5 million dollars being
3 allocated on class contribution to demand via the DMAINS allocator.
4

5 Q. Have you an exhibit which helps to evaluate the impact of the GRP modification?

6 A. Yes. Rebuttal Exhibit_(LGA-1), Schedule A compares selected elements (Rate
7 Base, Net Operating Income, Rates of Return and the ROR Indexes) from the
8 Company's 11/20/08 Revised Exhibit_(LGA-1R) Schedule B to Staff's
9 Exhibit_(GRP-6) Page 1 of 1.
10

11 Q. Could you please elaborate on what this exhibit shows?

12 A. Rebuttal Exhibit__(LGA-1) Schedule A shows that the GRP COS study (relative
13 to the Company study) reduces the amount of rate base allocated to residential
14 customers by approximately \$17 million dollars and increases the rate base of
15 the commercial-industrial customers by a like amount. By classifying all
16 distribution mains as 100% demand-related, Staff's COS study further reduces
17 the Net Operating Income produced in the COS from the commercial-industrial
18 customers by \$1.6 million, their ROR from 4.23% to 0.95%, and their COS index
19 from larger than the system average at 1.34 to much less than the system
20 average at 0.3.

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1 Q. Why do you find these results objectionable?

2 A. For several reasons: First, staff has never proffered such a treatment of
3 distribution mains in any of the CHG&E cases with which I have been involved
4 (since 90-G-0673). Central Hudson has used a consistent embedded COS
5 methodology over the years in order to establish a relatively stable foundation for
6 achieving cost-based rates; striving for rates that yield near (+/- 15%) the system
7 average ROR from all rate classes. That this goal is being approached is
8 evidenced by line 5 of the accompanying exhibit which shows the ROR projected
9 by the Company's COS to be near the system average for residential and
10 commercial-industrial customers (excluding the SC11). In contrast, Staff's
11 radical departure from past COS methodology projects a commercial-industrial
12 ROR 70% less than the system average (line 8) with a projected operating
13 income of only \$635 thousand on line 4 (vs. \$2.2 million projected by the
14 Company's COS). Given past history, it would take many rate cases to bring
15 commercial-industrial rates up enough to yield the system average ROR using
16 the GRP classification of distribution mains. It is undesirable to make radical
17 changes to COS methodology; and preferable to use a consistent methodology
18 from Case to Case requiring modest changes in rate design to bring all classes
19 to the System average ROR with minimal intra-/inter-class subsidization.

20

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1 Q. What reasons do you have for objecting to Staff's classification?

2 A. There are several:

3 1) It breaks a long established precedent for recognizing customer-related and
4 demand-related components to the cost of distribution mains (as described
5 above);

6 2) The GRP fails to support their testimony and their classification of distribution
7 mains:

8 "The purpose of this change is to more closely identify the minimum
9 customer costs for each service class. In the Panel's view, the result of
10 the revised study will more closely indicate costs associated with a basic
11 level of service, which is more representative of the costs saved when a
12 customer leaves the system."

13 3) Their response to CH-153 & CH-154 (Rebuttal Exhibit_(LGA-1), Schedules B &
14 C) seems to create a tautology.

15 4) Their response to CH-149 & CH-153 (Rebuttal Exhibit_(LGA-1), Schedules D &
16 B) seems to indicate a misunderstanding of what it costs to connect a customer
17 to the system;

18 5) It (wrongly) decreases customer-related charges and increases the demand-
19 related charges which result in large volume customers subsidizing smaller
20 volume customers within each class and among the classes.

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1 Q. Please elaborate on your second objection to the GRP classification of
2 distribution mains.

3 A. It is not at all clear how staff's change "...more closely identify the minimum
4 customer costs for each service class"; nor, how the revised study "...*more*
5 *closely* indicate(s) costs associated with a basic level of service, which is *more*
6 *representative* of the costs saved when a customer leaves the system."

7 We attempted clarification with interrogatories CH-153 & CH-154 (see
8 accompanying Rebuttal Exhibit_(LGA-1R) Schedules B&C but the GRP
9 responses seemed to be a tautology "It is the GRP's position that the result of
10 this allocation (did they mean "classification"?) *better* reflects minimum cost to
11 serve a customer."

12 It remains unclear how shifting roughly \$60 million in distribution mains gross
13 plant from being customer-related (Company classification) to yield a total over
14 \$100 million being allocated on demand more
15 "closely/representative/better...reflects costs saved when a customer leaves the
16 system." Mains are a sunk cost and the utility does not save the costs of sunk
17 investment when a customer leaves the system. On the other hand, from the
18 customer's perspective, when he or she leaves the system, he or she "saves"
19 both the customer-related charges as well as the demand-related charges. As a
20 result, the Panel's rationale is not correct. It should also be noted that if by

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1 “leaves the system” the panel intended “becomes a retail access customer,” the
2 GRP classification has no impact on the unbundled components (lines 56-59 of
3 Exhibit_(LGA-1), Schedule C, Page 2 of 2 & GRP response to CH-152, page 25
4 of the xls file). Therefore, the GRP demand-only classification of distribution
5 mains results in no changes to the MFCs produced by the COS model. The
6 GRP seems to understand this judging by their response to CH-154e (re:
7 Rebuttal Exhibit_(LGA-1), Schedule C).

8
9 Q. Please elaborate on your third objection to the GRP demand-only classification of
10 distribution mains.

11 A. The GRP responses to CH-153 & CH-154 (attached as Rebuttal Exhibit_(LGA-
12 1), Schedules B&C) seem to create a tautology when compared to their direct
13 testimony: Their response to CH-154c sends us to CH-150 (which refers to
14 marginal costs) and their response to CH-153 where they substitute “...better
15 reflects minimum cost to serve a customer” for “...more closely identify the
16 minimum customer costs for each service class” from their direct testimony.
17 However, the panel does not provide any demonstration that their method
18 identifies the minimum costs to serve, and confuses the concept of minimum
19 costs to serve a customer with the concept of minimum costs to a customer
20 class.

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1 The whole point of the minimum intercept method the Company has employed is
2 to determine the minimum costs to serve the typical customer, whereas the
3 Panel incorrectly dismisses that analysis without providing any other analysis.
4 Further, the GRP response to CH-154e states that costs saved by the Company
5 when a customer leaves the system would be the same under either
6 methodology. Therefore, not only has the Panel not provided any demonstration
7 for their proposition, they have conceded that they cannot demonstrate the
8 superiority of their proposal. It should be clear that the purpose of the minimum
9 intercept method the Company has used is to provide precisely what the GRP
10 did not; namely, a demonstration and quantification of the minimum costs to
11 connect all of the individual customers served by the distribution system.

12

13 Q. Please elaborate on your fourth objection to the GRP demand-only classification
14 of distribution mains.

15 A. In both the electric and gas embedded cost of service studies; the Company
16 identifies customer-related and demand-related components of the distribution
17 systems. The customer-related component reflects the minimum total cost to
18 hook every customer up to a Central Hudson delivery system. The demand-
19 related component reflects the cost related to the maximum requirements of the
20 customers: for gas customers this means the diameter of the mains: large

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1 demand-volume customers require bigger diameter pipes than small volume
2 customers; big diameter pipes cost more than small diameter pipes; commercial-
3 industrial customers (generally) require larger diameter pipes than residential
4 customers. Hence, in the Company's COS study, the investment related to
5 larger pipe sizes is allocated on demand.

6 In response to CH-149 and CH-153 (re: Exhibit_(LGA-1), Schedules D & B) the
7 GRP's position is that Central Hudson's investment in gas distribution mains is
8 related to the length of the mains and that the length of the mains is "not
9 indicative" of the number of customers. Intuitively, the GRP proposition does not
10 make sense, because the Company would require a greater total length of mains
11 as its number of customers increases and its system grows. The total
12 investment in mains will increase as a function of both diameter and length. The
13 causation for the size (i.e., diameter) of the mains is the instantaneous
14 requirements of the customers. Therefore, the minimum cost required to serve
15 individual customers is a function of the costs of the mains, and the cost of the
16 mains is a function of both their diameter and length.

17
18 Q. Please elaborate on your fifth objection to the GRP demand-only classification of
19 distribution mains.

20 A. Compared to the Company's gas department embedded COS study, the only

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1 difference resulting from the GRP's re-classified COS study is that customer-
2 related costs go way down and demand-related costs go way up. Since the
3 demand per customer of 10,000 commercial-industrial customers is
4 proportionately larger than the demand per customer of 65,000 residential
5 customers then the GRP disproportionately assigns more cost responsibility to
6 the commercial-industrial class and less to the residential class. Whenever the
7 customer charge is too small (relative to the COS), to achieve the system
8 average ROR, the demand/energy-related charges must be too large. In that
9 case, any small volume users will be subsidized by the larger volume users.

10

11 Q. Could you please summarize your recommendations?

12 A. Yes. We would urge that the Commissioners reject the GRP's gas COS
13 methodology and embrace the Company's methodology and approach to rate
14 design.

15

16 Q. Does this conclude your rebuttal testimony?

17 A. Yes.