

REBUTTAL TESTIMONY OF
MICHAEL L. MOSHER

CASES 09-E-0588 & 09-G-0589

1 Q. Are you the same Michael L. Mosher who filed direct testimony in these
2 cases?

3 A. Yes, I am.
4

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

6 A. The purpose of my rebuttal testimony is to respond to positions taken by the
7 Staff of the Department of Public Service in the testimony and exhibits filed
8 on November 17, 2009, and to address certain specific portions of those
9 positions. I will address the productivity/austerity positions of the Staff
10 Accounting Panel, the related positions of the Staff Policy Panel, the three-
11 year proposal of the Staff Policy Panel and the position of the Staff Gas
12 Rates Panel on the excess costs of removal for gas mains and services.
13

14 Q. Please state your understanding of the productivity/austerity positions of the
15 Staff Accounting Panel.

16 A. The Staff Accounting Panel has addressed productivity and austerity
17 explicitly or implicitly in several ways. First, even though the Panel
18 recognizes that the Company's actual number of employees exceeds the
19 number reflected in their position, the Panel proposes a cap on the number
20 of employees to be recognized for ratemaking purposes that is below the
21 actual number of employees currently employed and expected for the rate

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1 year. Second, it proposes to impute a 2% "productivity adjustment" applied
2 to a broad base that includes all labor, fringe benefits, payroll tax, and net
3 periodic pension and OPEB expenses. Third, it employs historic averages for
4 many expense items, in contrast with the historic period level of costs for the
5 12 months ending March 31, 2009. Fourth, it proposes to escalate many
6 elements of cost at a GPD inflator, as contrasted with known rates of
7 escalation and the GDP deflator employed by the Staff Accounting Panel is
8 significantly lower than the GDP forecast presented by the Staff Forecasting
9 Panel.

10
11 Q. Please state your understanding of the productivity/austerity positions of the
12 Staff Policy Panel.

13 A. The Staff Policy Panel refers to productivity and austerity explicitly or
14 implicitly in several portions of its testimony. First, at page 5, the Staff Policy
15 Panel provides its definition of the period for which austerity is required;
16 namely, the period until GDP reaches the highest value it had attained prior
17 to the fall of 2008, which the Policy panel predicts will not occur "until the end
18 of 2011 with employment recovering in early 2012." Second, the Staff Policy
19 Panel recommends to freeze executive salaries at 2009 levels from January
20 1 until July 1, 2011 and to freeze management salaries for the July 2010-
21 June 2011 rate year, in the event the Commission desires further austerity.

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1 Third, the "three-year rate plan" proposal of the Staff Policy panel would
2 exclude significant elements of the Company's costs and therefore constitute
3 a productivity/austerity proposal because, as the Panel stated at page 18 of
4 its testimony, the "Company would be required to manage the remaining
5 differences in its projected revenue requirement without incremental rate
6 relief."

7

8 Q. On July 24, 2006 the Commission modified and then approved a rate plan
9 ("2006 Plan") for Central Hudson that addressed the three-year period
10 ending June 30, 2009. Please describe the effects that the 2006 Plan had on
11 Central Hudson's financial results.

12 A. The Company was unable to recover its Commission-authorized revenues,
13 for both gas and electric delivery service, throughout the duration of the 2006
14 Plan with the exception of the first year, where financial results were
15 temporarily improved by a non-recurring item. During that time period, the
16 average annual residential use per customer was running nearly 5% and
17 10% below for electric and gas, respectively, the level of sales used to set
18 rates, on a weather-normalized basis. The deteriorating gas and electric
19 sales and resulting revenue shortfalls meant that Central Hudson was unable
20 to fully recover its authorized costs of providing electric and gas service
21 during the 2006 Plan, even as the Company was required to expend

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1 designated amounts for electric, gas and common plant additions, electric
2 transmission and distribution tree trimming programs, and was further
3 impacted by a number of other non-revenue matched expense items that
4 require deferral accounting treatment, including stray voltage testing and
5 MGP site remediation.

6

	Rate Year 1	Rate Year 2	Rate Year 3
Earned ROE(%)	7/1/06 – 6/30/07	7/1/07 – 6/30/08`	7/1/08 – 6/30/09
Electric	10.89	8.75	6.36
Gas	6.31	4.16	3.53
Allowed ROE	9.60	9.60	9.60

7

8 The unintended circumstances produced by the 2006 Plan imposed austerity
9 on Central Hudson two years before the economic upsets of the fall of 2008
10 and compelled the Company to look for efficiencies and implement all
11 available cost reductions, including reducing its overheads and temporarily
12 reducing its staffing.

13 The table below demonstrates significant cost reductions of over \$6.0 million
14 in total labor, pensions, Other Post Employment Benefit (OPEB) plans, and
15 fringe benefit costs the Company had originally forecasted for the current
16 rate year, compared to rate year three of the previous three-year rate plan.

17 While the pension and OPEB costs were ultimately updated during the

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1 course of the proceeding to recognize the severe downturn in the financial
2 markets, the comparison demonstrates the expense reductions resulting
3 from the Company's actions, excluding the market impacts, and all else
4 being equal.

(\$000)	Rate Year Ended June 2010	2006 Rate Plan	Rate Year Ending June 2010 vs. 2006 Plan
Total Labor	82,855	75,613	7,242
Pensions	14,314	18,392	(4,078)
OPEB's (net)	6,350	14,899	(8,549)
Fringe Benefits	10,311	10,955	(644)
TOTAL	113,830	119,859	(6,029)

5

6 As noted, the Company allowed its staffing levels to decrease temporarily,
7 from a high of 860 in December 2006 to a low of 823 in April 2008, averaging
8 about 840 for the term of the rate plan.

9 Under various sections of the Joint Proposal modified by the Commission in
10 the Order for the 2006 Plan, Central Hudson was required to make electric,
11 gas, and common plant capital expenditures totaling approximately \$208
12 million (exclusive of AFUDC) by the end of June 2009. In addition, the 2006
13 Plan also established a separate mandate to expend an additional \$15.75
14 million on gas cast iron/steel pipe replacement by the end of calendar 2009.
15 In addition, Central Hudson was required to expend \$6.723 million for
16 Electric Transmission ROW Maintenance, and by virtue of a change to the

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1 parties' Joint Proposal imposed by the Commission, Central Hudson was
2 also required to expend \$24.362 million for Distribution ROW Maintenance;
3 both over the three rate years of the previous rate plan. Despite the severe
4 sales shortfalls and resulting revenue deficiencies under the previous three-
5 year rate plan, the Company met all of these mandates, and its earned return
6 suffered significantly as a result.

7 I would also like to note that one of the reasons why the Company made the
8 required expenditures and only reluctantly allowed its staffing to decline
9 temporarily was that the 2006 Plan had several "incentives." There are
10 comprehensive sets of multi-part Customer Services Quality, Electric
11 Reliability, and Gas Safety performance targets and "incentives". Central
12 Hudson was required to meet these "incentives" (or suffer the
13 consequences) independent of the level of revenues or earnings. In addition,
14 there was a property tax incentive included in the 2006 Plan, which provided
15 for a 90/10 shared deferral on the differences (positive or negative) between
16 the rate allowances and actual property taxes between customers and the
17 Company, respectively.

18

19 Q. Were the productivity gains adopted by Central Hudson while it was
20 operating under the 2006 plan carried forward in the Company's subsequent
21 rate filing application in July 2008?

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1 A. Yes, they were. The Company based its forecast for the new rate year in the
2 most recent case on the premise that those efficiency gains were permanent
3 and would continue to benefit customers.

4
5 Q. Did the Commission agree?

6 A. Yes, it did. At page 9 of its Order of June 22, 2009, the Commission stated:

7 More specifically, because of constraints outside of its
8 control, the Company has, over the past three years,
9 successfully developed and implemented several
10 significant measures to restrain expenditures. While
11 some of these items may be viewed as temporary
12 austerity measures, others represent more permanent
13 solutions addressing the structural causes of certain
14 costs.

15
16
17 Q. Were the permanent cost reductions carried forward into the present cases?

18 A. Yes, they were. The Company's austerity filing of June 15, 2009 identified a
19 number of specific actions taken by the Company during the term of the
20 previous three-year rate plan to reduce expense and permanently reduce
21 the Company's cost structure. In addition to pension and OPEB plan
22 modifications, the Company implemented a cap on its contributions to retiree
23 health care, and also implemented greater cost sharing contributions for
24 active employees. The Company also reduced its use of outside services,
25 and consultants, and eliminated certain employee/retiree recognition events.
26 These structural cost reductions are properly considered as austerity

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1 measures, and are currently reflected in rates.

2

3 Q. Are there any other measures reflected in the Company's filing that can be
4 considered to be austerity measures?

5 A. Yes. As described in Mr. Haering's testimony, we based our rate year capital
6 expenditures forecast for "New Business" and "Load Growth" categories on
7 the premise that there will be a continuation of the lower levels of customer
8 and load growth experienced during the fall of 2008 and subsequently. As a
9 result, we have continued forward into the rate year in this case the "New
10 Business" austerity adjustment portion of our response to the Commission's
11 austerity order, with a capital expenditure forecast for the rate year that is
12 approximately \$15 million lower than was previously forecasted for the same
13 period in the recently concluded case. In addition, the commitment made by
14 Central Hudson in our austerity filing to freeze executive salaries in 2010 at
15 2009 levels reduces costs in the first half of the rate year in these cases.

16

17 Q. Do you agree with the Staff Accounting Panel's description of its treatment of
18 the costs of the SERP, the costs of IFRS implementation, and half of its
19 proposed 2% productivity adjustment as austerity-related grounds?

20 A. No, I do not. I believe that the intention of the Commission in its May 15,
21 2009 Austerity Notice was to call upon utilities to make sensible and mature

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1 judgments about costs that could reasonably be avoided. Accordingly, I
2 disagree with the Staff Accounting Panel's characterization of the SERP
3 costs, the costs of IFRS implementation and the Staff incremental
4 productivity adjustments are properly considered to be austerity-related.
5 As to SERP costs, no going-concern business can abruptly cancel a long-
6 standing benefit program, or shift the funding to shareholders or employees,
7 without consequence and the Staff Accounting Panel's statements to the
8 contrary are inconsistent with common human experience. I also note that
9 the Panel did not support its position in any fashion. I also disagree with the
10 Panel's assertion that the SERP is " an added benefit akin to a bonus" as the
11 Staff Accounting Panel states at page 26 of its testimony, as further
12 addressed by the Revenue Requirements Panel. IFRS are international
13 accounting standards that the SEC has decided to require public companies
14 in the U.S to employ for their financial statements. While the final timing for
15 implementation is not known at this moment, like all other public companies,
16 Central Hudson will be required to implement these new standards when the
17 SEC specifies. Avoiding the costs of IFRS planning, as the Staff Accounting
18 panel proposes, is short-sighted and therefore not properly considered as an
19 austerity measure. The Commission cannot expect utilities to plan
20 reasonably and efficiently for a federal regulatory requirement as important
21 as this proposed major accounting system change and, at the same time,

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1 treat it as insignificant by effectively withholding funding in the name of
2 austerity.

3 As to the incremental 1% productivity adjustment proposed by the Staff
4 Accounting Panel on austerity grounds, the Staff has not presented any basis
5 for believing that the incremental adjustment has a basis in reality. It simply
6 defies logic to believe that there are efficiencies that have not been identified
7 because of austerity, yet the Staff Accounting Panel bases its incremental
8 productivity position on the existence of austerity.

9 Q. Please address the two additional austerity measures proposed by the Staff
10 Policy Panel.

11 A. The executive and management salary freezes proposed by the Staff Policy
12 Panel *might* properly be considered as austerity adjustments if the utility had
13 excessive costs, but the Staff Policy Panel has presented no basis for
14 believing this is the case for Central Hudson. Central Hudson does not have
15 a top-heavy management; we have just 320 management employees,
16 including 13 executives. I note that the fact that the Company has so few
17 executives (and by implication management) employees is given by the Staff
18 Accounting Panel's reference to the Company's SERP as relevant to only
19 eighteen executives, seven of whom are retired.

20

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1 Q. Are there additional comments that you have regarding the Staff Policy
2 Panel's discussion of austerity?

3 A. Yes. On page 4 of its testimony, the Staff Policy Panel refers to my direct
4 testimony as follows:

5 Mr. Mosher concluded at page 9 that despite the current
6 economic slowdown, "given the severe financial
7 conditions and circumstances the Company operated
8 under the terms of the recently expired rate plan, which
9 required a number of specific cost-cutting actions, all of
10 which have already been captured permanently for the
11 benefit of customers in the recent Rate Order, there are
12 few, if any, additional opportunities to reduce non-labor
13 O&M expense without jeopardizing the Company's
14 ability to serve."

15
16 I would like to invite a review of page 9 of my testimony. My testimony does
17 not say "despite the current economic slowdown." In reality, the point of my
18 testimony was quite different than conveyed by the Staff Policy Panel. My
19 point is that by the time that the economic slowdown hit the general
20 population, Central Hudson had already internalized many cost-cutting
21 changes to its operations because of the "self imposed austerity" that it was
22 forced to operate under because of the 2006 Plan. Central Hudson's
23 austerity actions were not "despite" the economic slowdown, they were in
24 advance of the economic slowdown. Central Hudson is unlike other utilities
25 in that it had already undertaken hard decisions to cut its costs, as the
26 Commission recognized in its June 22, 2009 order, as I stated previously.
27 Therefore, I believe that the Staff Policy Panel's attempt to disparage the

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1 Company as being indifferent to the economic slowdown is incorrect and
2 misplaced.

3 Third, the Staff position that an additional 1% labor productivity, or 2% total
4 productivity adjustment is required, can be viewed as compounded
5 productivity, given the Staff Accounting Panel's position for a hard ceiling on
6 staffing, and to limit a majority of increases to the inflation rate.

7 Fourth, the Staff filing in other areas, particularly with respect to the
8 forecasted customer and sales growth, is disjoint from the Staff Policy
9 Panel's claim for additional austerity. The Staff Forecast Panel's forecast of
10 customer and sales growth suggests that the recession is over and that pre-
11 recession growth rates will return, fueling the additional revenue growth
12 projected by the Staff Forecasting Panel.

13

14 Q. Did the Company take any specific actions in developing its filing to address
15 economic conditions?

16 A. Yes, we did, although one can find little, if any, recognition of them in Staff's
17 presentation. The Company's decision to reflect an allowed ROE of 10.00%
18 in its filing, in light of expert testimony supporting a range of cost of equity
19 capital from 11.00% to 11.50%, is consistent with the Commission's decision
20 from the prior case's allowed 10.00% when austerity was considered due to
21 the economic conditions. As previously addressed, the Company's five year

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1 capital expenditures presented in its filing reflect assumptions for lower levels
2 of new business and load growth expenditures. Additionally, the Company
3 adopted the Commission's methodology for forecasting certain cost
4 elements, such as treating fringe benefits, transportation fuel, and advertising
5 as inflationary expense items.

6

7 Q. Given the actions taken by the Company to implement major portions of the
8 Commission's June 22, 2009 rate case decision in its new filing, how does
9 the Company's filing compare to the Commission's Order?

10 A. Perhaps the best way to illustrate is through the following, high-level income
11 statement comparison.

12

13

ELECTRIC	Commission	Company
(\$Millions)	Authorized	Filing
	<u>08-E-0887</u>	<u>09-E-0588</u>
Delivery Revenues	257.2	269.5
Total Operating Revenues	264.5	278.1
Total O&M Expense	136.0	143.8
Total Other Deductions	57.2	59.8
Total NYS & FIT Taxes	22.2	21.9
Total Operating Deductions	215.4	225.5
Net Operating Income	49.1	52.6
Rate Base	674.5	694.1
ROE	10.00%	10.00%

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GAS (\$Millions)	Commission Authorized <u>08-G-0888</u>	Company Filing <u>09-G-0589</u>
Delivery Revenues	66.7	69.8
Total Operating Revenues	70.0	73.4
Total O&M Expense	33.7	35.8
Total Other Deductions	15.5	15.8
Total NYS & FIT Taxes	7.5	7.3
Total Operating Deductions	56.7	58.9
Net Operating Income	13.3	14.5
Rate Base	183.2	190.0
ROE	10.00%	10.00%

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Q. How does the Staff position compare?

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1 A. While Staff has essentially accepted the Company's plan to add about \$85
2 million in new capital, Staff cuts back on the allowed return on equity from
3 that just approved by the Commission. Despite the continuing development
4 of the Company's infrastructure for the benefit of ratepayers, and the
5 assumed growth in the number of customers forecast by Staff, Staff attempts
6 to suppress the expense allowances through attempting to base significant
7 expense elements of costs on a backwards-looking three-year average (that
8 reflects extreme cost-cutting by the Company) and also applying an
9 unrealistic inflation-capped rate of escalation. The conclusions that may be
10 drawn are that Staff is seeking at all costs to eliminate the rate increase,
11 through various adjustments to sales, expense, rate base, and return.
12 Despite the extreme financial pressures the Company was operating under
13 during the term of the three-year rate plan, Staff is proposing to use costs
14 from that time period to forecast rate year costs and to hold total O&M
15 expense escalation to a level below inflation, even when presented with
16 factual information (concerning, for example, insurance, and stray voltage
17 testing) that demonstrate that the prices that Central Hudson must pay for
18 services it acquires from competitive markets are much higher than inflation.
19

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1 Q. Given the \$84 million of incremental capital that the Company is committing
2 to the public service and the increasing costs in areas like property taxes and
3 uncollectibles, how is it feasible for there to be zero rate increases?

4 A. It is not feasible in any realistic fashion. The Staff filing would have the
5 Company commit this capital, and only recognize an additional \$900,000 in
6 net operating income.

7

8 Q. Did the Company's filing seek to establish rates for a three-year period?

9 A. No. The Company's filing of July 31, 2009, consisting of testimony, exhibits,
10 and tariff changes, addressed only the rate year beginning July 1, 2010. As
11 part of its filing, the Company provided certain additional information for two
12 additional year time periods subsequent to the rate year in order to be
13 responsive to the Commission's Test Year Policy Statement. However, the
14 Company did not request and is not seeking to set rates for a multi-year
15 period.

16

17 Q. Please describe in more detail some of the problems with Staff's staged filing
18 proposal for multi-year rates.

19 A. The Staff filing would seek to limit rate increases for the two subsequent rate
20 year periods based on what Staff believes are the four primary electric cost
21 drivers: sales, labor, carrying charges (return and depreciation) on net plant

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1 additions, and property taxes, and for gas service, the same four plus two
2 additional cost drivers: gas leak repairs, and excess cost of removal. The
3 Staff multi –year staged filing proposal essentially decides now what the
4 Company’s cost drivers will be, and seeks to limit any increases to these
5 items, simply because they have been cost drivers in the past. This is not
6 logical or even constructive because it is irrational to limit increases to only
7 these costs, and excluding even inflationary increases on other costs, without
8 knowing what other costs or cost drivers might be. Moreover, as I have
9 previously noted, the drivers for the present rate increase application are not
10 the categories that Staff has identified, but mandates and externally imposed
11 costs (MGP site remediation, property taxes, etc), rate base growth and
12 related depreciation, higher debt costs, lower sales, and modest increases in
13 O&M expenses, most notably uncollectibles. The Staff multi –year staged
14 filing proposal, if adopted, would certainly provide ratepayers with benefits,
15 with downward-only reconciliations on net plant targets and T&D ROW
16 maintenance, but would also expose the Company to uncompensated cost
17 impacts and financial/operating risks. Additionally, the Policy Panel’s
18 adoption of the Electric Infrastructure Panel’s recommendation that capital
19 expenditures in the staged flings cannot exceed the level of capital
20 expenditures as originally forecasted in early 2009 for those two subsequent
21 time periods that extend into mid-2013, and subject to downward only

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1 reconciliations, is a proposal to immunize ratepayers from the consequences
2 of prudently incurred costs that may be incurred. The Staff Infrastructure
3 Panel, after extensively reviewing and analyzing all of the Company's capital
4 expenditures and net plant additions in the instant case as well as the
5 previous case, have essentially accepted all of the projects proposed by the
6 Company and not identified material capital project exclusions. The Staff
7 Infrastructure Panel also recognizes the Company should spend at the levels
8 it deems appropriate to provide safe and adequate service. However, their
9 proposals seek to place a cap now on the funding for these capital
10 expenditures, with downward-only reconciliations. Similarly, the Policy
11 Panel's adoption of the Rate of Return Panel's return on common equity of
12 9.60% and recommended stay-out premium of 12 basis points is plainly
13 insufficient to compensate the Company for the financial and business risks
14 over the next three years. An 'allowed' return on equity of 9.60%, 40 basis
15 points below what is currently authorized, is not a sufficient demonstration of
16 the regulatory support that will allow the Company to maintain its A-/A3
17 ratings by S&P and Moody's. The rebuttal testimony of Company witness
18 Robert Rosenberg will further address Staff's ROE and stayout premium
19 recommendations.

20

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1 Q. In the three-year proposal of the Staff Policy panel, the Panel claims that its
2 proposal would allow the Company to recover about 100% of a forecast
3 incremental electric revenue requirement and 76% of the incremental gas
4 revenue requirement in year 2, and 90% of the incremental electric revenue
5 requirement and 46% of the incremental gas revenue requirement in year 3.
6 Please comment on these statements by the Staff Policy Panel.

7

8 A. First, I observe that the Staff has not been able to identify any revenue
9 requirement for year 1, and did not provide any testimony or exhibits in
10 support of any subsequent rate year periods in the face of obvious revenue
11 requirements as compared to the Commission's recent rate order, which I
12 would illustrate by pointing out that the level of Company capital program is
13 relatively constant at about \$84 million across the entire mid-2009 through
14 mid-2013 period. Therefore, I believe that any statements by the Staff Policy
15 Panel concerning revenue requirements should be viewed with skepticism.
16 Second, the concept that the Commission would impose a "plan" that would
17 intentionally block any portion of legitimate utility revenue requirement is, I
18 believe, contrary to the "just and reasonable" standard that I have been
19 advised is contained in (section 65 of) the Public Service Law. The
20 suggestion that the Commission adopt a system to intentionally exclude any

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1 potential legitimate utility costs to serve is a major flaw in the Staff Policy
2 Panel proposal.

3 The impact of the Staff Policy Panel's proposal upon the Company can be
4 seen through some simple examples. Let us take the Staff position, as I
5 have summarized it above, and exclude 10% of the electric expenses
6 (corresponding to the Policy Panel's statement that its third year electric
7 proposal would recover 90% of the Company's costs). This would reduce
8 the indicated ROE from the 9.72% nominally allowed by the Policy Panel to
9 7.22%, or roughly 250 basis points below the allowed return. A similar, but
10 much more drastic impact would be created for gas operations, with the end
11 result that the Company would again not be able to achieve its allowed
12 return.

13

14 Q. The Staff Policy Panel seemingly would hold the "incentives" it recommends
15 constant for the three years in its three-year proposal. Is this a reasonable
16 level of "incentives" for Central Hudson?

17 A. I do not believe so. The Staff is proposing a significant ramping-up of the
18 Company's exposure to electric and gas penalties, which are referred to
19 euphemistically as "negative revenue adjustments, or NRA." While Staff is
20 proposing to maintain the SAIFI and CAIDI electric reliability measurement
21 metrics, Staff is proposing an incremental 5 basis points of NRA on each

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1 metric to offset their proposed elimination of two previous electric reliability
2 mechanisms.

3 While the increased exposure is troubling enough, in and of itself, there are
4 additional surrounding circumstances that make it even more so. First, Staff
5 is proposing to not fund the current four-year distribution line clearance
6 program that the Company and its consultant have developed. This means
7 as Mr. DuBois has described, that the benefits from the work done already
8 will be lost and that the Company's exposure the SAIDI and CAIFI penalties
9 will be increased even if the level of those "metrics" were to be held constant.

10 Second, the Company would be placed into another "Catch 22" situation
11 because, on the one hand, it would face a limited level of funding for tree
12 trimming and on the other hand it would face an "NRA" for failure to meet the
13 electric reliability metrics. The Commission has already foresworn that
14 Companies should not be placed into this position.

15 While the electric reliability is problem enough, Staff proposes to compound it
16 with a similar "Catch 22" concerning gas metrics. Here, the principal problem
17 is gas leak repair. Staff continues to seek to impose upon the Company the
18 obligation to repair any and all gas leaks found as may be necessary to meet
19 a specified leak backlog target, but not to provide the funding for the number
20 of leaks that will actually be required to be repaired to meet the backlog
21 target. A second problem is damages. On the one hand, Staff is seeking to

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1 reduce the level of damages, but on the other it is proposing to require
2 expanded Company activities to repair and replace leak-prone pipe and
3 services. No analysis supports the positions of the Gas Safety Panel in
4 these regards.

5

6 Q. Please explain the impact of the Staff position on the costs of excess cost of
7 removal for gas mains and services upon the Company.

8 A. The Staff would ensure that the Company is unable to fully recover its capital
9 removal costs for gas mains and services. The proposed Staff rate
10 allowance associated with excess costs of removal, which are the expense
11 costs above what is provided for, or allowed to be recovered through
12 depreciation, is based on Staff's recommended five year average of removal
13 costs, which are based on a historic time period when the Company's
14 removal expenditures can be demonstrated to be much less than the
15 expenditure levels forecasted and required, under a capital expenditure
16 performance mechanism proposed by Staff's Gas Safety Panel, in the rate
17 year period. While Staff would prefer to complicate the issue with
18 depreciation study jargon and unsubstantiated concerns over book to
19 theoretical reserve imbalances, it is much simpler than that. Plainly stated,
20 the Company's full costs of removal are to be recovered either through
21 depreciation or expense, and the Staff filing seeks to cap both cost recovery

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1 elements at a level that is insufficient to fully recover these costs. This forced
2 stranding of shareholder money is one of the matters before the Commission
3 in a petition for rehearing filed by the Company following the Commission's
4 order in June in Case 08-G-0888 and will be more fully addressed in the
5 rebuttal testimony of the Accounting Panel.

6

7 Q. Please explain the impact of the Staff position on the stray voltage testing

8 A. As more fully addressed by Company witness DuBois, Staff is seeking to
9 establish a rate allowances for stray voltage testing based on a historical
10 three year average, which is again, a time period that does not recognize the
11 Commission's change to the electric safety standards instituted in December
12 2008, which expanded the testing scope. While Staff indicates they would
13 entertain an update based on the Company's actual costs, Staff seeks to
14 inflate that amount by the GDP inflation rate when presented with known
15 contractor pricing that exceeds inflation on various elements of the work
16 scope, which would result in inadequate funding to perform the work.

17

18 Q. Please explain the Staff position on D&O insurance and the impacts on the
19 Company.

20 A. The Staff filing also seeks to again disallow half of the Company's costs of
21 Directors and Officers (D&O) insurance coverage, on the basis that the

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1 Company did not produce any empirical study that showed ratepayers were
2 the beneficiary of such costs. This is not the standard under which utilities
3 operate and is a challenge to the regulatory compact that customers pay for
4 the prudently incurred costs of providing service. Since Central Hudson
5 cannot avoid these costs, the costs will continue to be incurred and result in
6 another missed opportunity for the Company to achieve its allowed return.
7 These previous illustrations are just simple examples of the regulatory biases
8 that are built into the Staff filing, which are intended to minimize or eliminate
9 legitimate rate increases and prevent the Company from any real opportunity
10 to earn its allowed return.

11

12 Q. Will the costs the Company was required to spend to replace leak-prone pipe
13 through 2009 be increased in subsequent periods?

14 A. Under the current rate order Central Hudson is required to spend a minimum
15 of \$6.1 million in 2010, a 16% increase in spending as compared to the
16 average under the prior, three-year rate plan. As noted in the Staff Gas
17 Safety Panel testimony on page 16 the required spending level would be
18 further increased to \$6.7 million for 2011, which is a 27.6% increase from the
19 annual levels for 2007-2009 and the Staff Gas Safety Panel would also
20 subject the Company to a Negative Rate Allowance were it not to make
21 those expenditures.

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1 As was recognized in the Staff Gas Safety Panel testimony page 13, for the
2 three-year period 2007- 2009 the Company was required to spend a total of
3 \$15.75 million replacing leak-prone pipe. This equates to an average of
4 \$5.25 million per year, but the actual expenditures were greater in 2009 as
5 compared to the prior two years. The actual costs of removal for the three-
6 year period are shown in our Exhibit ____ (AP-1R), along with calculations
7 applying the 60% net cost of removal to illustrate the remaining costs that
8 would be recovered through expense under the 2006 three-year rate plan. It
9 should be noted that the now-expired three-year rate plan did permit the
10 company to recover its actual expenses, unlike the position recommended by
11 the Staff Gas Safety Panel in the present case. It should also be noted that
12 the three-year average for the costs charged to expense under the three-
13 year rate plan is significantly above the expense allowance being proposed
14 by Staff in the present case (\$821,000 vs. \$430,000).

15

16 Q. Does this conclude your rebuttal testimony?

17 A. Yes, it does.