Before the
Connecticut Department Of Public Utility Control

Application of the Connecticut Natural Gas Corporation For a Rate Increase

Docket No. 99-09-03 Phase II

Direct Testimony of Timothy Woolf

On Behalf of
The Connecticut Office of Consumer Counsel

On the Topic of
The Connecticut Natural Gas Company's
Proposed Performance-Based Ratemaking Mechanism

September 25, 2000

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1. INTRODUCTION AND QUALIFICATIONS

Q. What is your name, position and business address?

A. My name is Timothy Woolf. I am the Vice-President of Synapse Energy Economics, Inc, 22 Crescent Street, Cambridge, MA 02138.

Q. Please describe Synapse Energy Economics.

A. Synapse Energy Economics is a research and consulting firm specializing in electricity industry restructuring, regulation and planning. Synapse works for a variety of clients, with an emphasis on consumer advocates, regulatory commissions, and environmental advocates.

Q. Please describe your experience in the area of electric utility restructuring, regulation and planning.

A. My experience is summarized in my resume, which is attached as Exhibit TW-1. Electric power system planning and regulation have been a major focus of my professional activities for the past eighteen years. In my current position at Synapse, I investigate a variety of issues related to the restructuring of the electric industry; with a focus on performance-based ratemaking, market structure, stranded costs, customer aggregation, air quality, energy efficiency, environmental policies and many aspects of consumer protection.

Q. Please describe your professional experience before beginning your current position at Synapse Energy Economics.

A. Before joining Synapse Energy Economics, I was the Manager of the Electricity Program at Tellus Institute, a consulting firm in Boston, Massachusetts. In that capacity I managed a staff that provided research, testimony, reports and regulatory support to state energy offices, regulatory commissions, consumer advocates and environmental organizations in the US. Prior to working for Tellus Institute, I was employed as the Research Director of the Association for the Conservation of Energy in London, England. I have also worked as a Staff Economist at the Massachusetts Department of Public Utilities, and as a Policy Analyst at the Massachusetts Executive Office of Energy Resources. I hold a

Masters in Business Administration from Boston University, a Diploma in Economics from the London School of Economics, a BS in Mechanical Engineering and a BA in English from Tufts University.

Q. Please describe your recent experience with Performance-Based Ratemaking.

A. I was the editor and one of the authors of the NARUC report, "Performance-Based Regulation in a Restructured Electric Industry." I have also addressed PBR issues on behalf of the Delaware Public Service Commission Staff, the Mississippi Attorney General, the Kentucky Attorney General, and the Colorado Office of Energy Conservation. I have published articles on performance-based ratemaking in *Public Utilities Fortnightly* and *The Electricity Journal*. In addition, PBR is a variation of traditional electricity ratemaking, which has been an underlying aspect of much of my professional career.

Q. On whose behalf are you testifying in this case?

A. I am testifying on behalf of the Office of Consumer Counsel (OCC). My testimony is being filed in conjunction with the testimonies of Mr. Paul Chernick and Mr. Hugh Larkin, who are also witnesses for the OCC.

Q. Have you testified previously in this docket?

A. No, I have not.

Q. What is the purpose of your testimony.

A. The purpose of my testimony is to evaluate the overall design of the Connecticut Natural Gas Company's (CNG or the Company) proposed Incentive Rate Plan (IRP). Much of my evaluation is based on general regulatory and ratemaking policy in Connecticut and elsewhere. I begin with a discussion of the appropriateness of implementing any performance-based ratemaking (PBR) mechanism at this point in time in Connecticut. I also raise some important concerns about the general design of CNG's IRP proposal. Finally, I review the Company's proposed service quality plan.

Q. How is your testimony organized?

A. My testimony is organized as follows:

1. Introduction and Qualifications.
2. Summary of Conclusions and Recommendations.
3. The Timing of CNG's Incentive Rate Plan Proposal.
4. Demonstration of Customer Benefits.
5. The Appropriate Baseline for a PBR Mechanism.
6. CNG's Service Quality Plan Proposal.

2. SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Q. Please summarize your primary conclusions.

A. My primary conclusions are summarized as follows:

- This is not an appropriate time to fix customer rates through an IRP or PBR mechanism, because there are so many changes occurring in CNG's business environment that an accurate baseline revenue requirement cannot be determined.

- The Company's IRP proposal does not provide meaningful benefits to customers, because it does not provide customers with a significant portion of the savings of the merger with Energy East. The Company essentially claims that customers will benefit from the IRP proposal because they will be no worse off than they are today. However, this is the wrong definition of customer benefits. A PBR mechanism must provide demonstrated customer benefits relative to rates they would experience under traditional cost-of-service ratemaking. Under traditional ratemaking, customers would experience all, or at least a significant portion, of the savings from the merger with Energy East.

- The CNG IRP proposal is fundamentally flawed because it includes baseline rates that are not prospective and are certain to be too high. The baseline rates in the Company's IRP mechanism should not be based on

historical cost-of-service – they should instead incorporate the anticipated future savings from the merger with Energy East.

- CNG's service quality plan will not provide adequate protection to consumers because (a) it does not address the most appropriate service quality measures, (b) the benchmarks will not maintain historical performance levels, or achieve the improved performance levels associated with the merger, and (c) the penalties are too low to capture management attention.

Q. Please summarize you primary recommendations.

A. I recommend that the Department reject the Company's IRP proposal.

I also recommend that the Department reject the Company's proposed service quality plan. If the Company is allowed to implement any form of PBR mechanism, the service quality plan should be modified to account for the concerns raised herein. The new proposal should be based on a comprehensive assessment of potential service quality indicators. The new proposal should include goals that will clearly maintain the levels of service provided in the past, as well as goals based on promised service improvements due to the merger with Energy East. Finally, the new proposal should include meaningful penalties that are not subject to a cap.

3. THE TIMING OF CNG'S INCENTIVE RATE PLAN PROPOSAL

Q. Please briefly summarize the IRP mechanism that is being proposed by the Company in this docket.

A. CNG has proposed an IRP mechanism that includes the following components. Rates will be set based on the revenue requirements determined in Phase I of this docket. The Company states that these rates will be held constant during a four-year "stay-out" period. CNG proposes that the revenue requirements used in setting the baseline IRP rates will not incorporate any aspect of the proposed merger with Energy East. CNG proposes that the Purchased Gas Adjustment (PGA) clause will remain in place, at least for now. CNG proposes an earnings

sharing mechanism, to allow customers to share 50 percent of any merger savings that occur beyond a rate-of-return threshold of 11.8 percent. Finally, the Company proposes a service quality plan to prevent the deterioration of customer service in response to the price cap.

Q. Is this an appropriate time for CNG to be implementing a PBR mechanism?

A. No, it is not. This is an inappropriate time to fix customer rates through a PBR mechanism, because there are so many changes occurring in CNG's business environment that an accurate baseline revenue requirement cannot be determined. Three are three types of changes that have not been addressed by CNG in its IRP proposal. First, the gas industry in Connecticut and New England is undergoing significant changes as a result of increased competition. Second, the merger of Energy East and CNG will change the costs, risks and opportunities facing CNG. Third, CNG's recent rate case resulted in rates that we know will either change or be inappropriate for the inclusion in future rates. My colleague Mr. Larkin addresses the latter point in more detail.

Q. Has the Department established a precedent regarding the application of a PBR mechanism after a merger?

A. Yes. The Department has found that a PBR mechanism should not be implemented immediately after a merger, due to the difficulty of establishing appropriate customer rates. In it's review of the Southern Connecticut Gas Company (Southern) rates and charges, Phase II, the Department rejected that company's request for a PBR mechanism because of the changes caused by the merger. The Department noted:

> A principal concern of the Department lies with the timing of the proposal. Southern is currently in the process of merging with Energy East. As a result, there are likely to be significant changes in the Company's focus and the cost of its operations. Neither in this docket nor in the merger proceeding (Docket No. 99-07-20) has the Company quantified projected savings from the merger. Accordingly, the Department considers it premature to lock in rates for ratepayers for an extended period as proposed in the PBR/RPA. (Department Decision, Docket No. 99-04-18, Phase II, at 43.)

Q. Are there other Department Orders that caution against using PBR mechanisms in periods of great change.

A. Yes. In the recent investigation into PBR regulation for electric distribution companies, the Department concluded that "PBR should not be undertaken during periods of fundamental change to a utility's cost structure: hence it should not be undertaken in the near-term." (Department Decision, Docket No. 99-06-21, 2/2/2000, at 28). The Department specifically cautioned against the use of a PBR plan associated with the proposed merger between Northeast Utilities and Consolidated Edison, noting that:

> If approved, the proposed merger between CL&P's parent company, Northeast Utilities, and Consolidated Edison would further obscure CL&P's near-term cost structure. Effective PBR rests upon accurate portrayal of an EDC's costs. Such a portrait is difficult to achieve during a period of fundamental change. Undertaking PBR in the near-term for CL&P is inadvisable. (Department Decision, Docket No. 99-06-21, 2/2/2000, at 9).

This same rationale applies to PBR and mergers of gas companies. A merger can alter the costs, risks and opportunities that an electric or gas utility has experienced in the past, thereby making historical baselines irrelevant. Establishing an appropriate baseline price is one of the most important requirements for implementing a sound PBR mechanism.

Q. Has the Company provided evidence suggesting that a PBR mechanism should not be implemented at this time?

A. Yes, it has. Dr. Kenneth Gordon, testifying on behalf of the Company, describes the importance of establishing the correct baseline for any PBR mechanism. In emphasizing the overarching themes of his testimony, Dr. Gordon states that:

> there must be a good "fit" between the nature, opportunities, and risks of CNG's ongoing LDC's activities and the alternative regulatory plan that will govern these activities. Regulators must have a clear understanding of CNG's basic business roles prior to developing an alternative regulatory plan, as well as an understanding of the sorts of uncertainties, risks, and opportunities that CNG faces. (Gordon PFT, at 10.)

Yet immediately following this statement Dr. Gordon presents the very reason why a PBR mechanism would be inappropriate for CNG at this time, by noting that "(g)iven the important changes in the gas business in recent years, the risks and opportunities facing CNG will be quite different from those of the recent past." (Gordon PFT, at 10.) I agree with both of Dr. Gordon's points: a PBR mechanism must be tailored to a gas company's on-going and future business activities, and for CNG those activities will be "quite different" from those of the past. The obvious conclusion to be drawn from these two points, however, is that CNG's IRP proposal should not be implemented at this time. A proposal based on historical business activities, opportunities and risks will simply not provide a proper fit with future activities in this industry.

Q. What do you recommend to the Department, in light of the fact that this is an inappropriate time to implement a PBR mechanism for CNG?

A. I recommend that the Department treat CNG's IRP proposal the same way it treated PBR for electric utilities in its generic docket (Docket No. 99-06-21). The Company's request for a PBR should be denied because it is an inappropriate time.

4. DEMONSTRATION OF CUSTOMER BENEFITS

Q. If the Department were to allow a PBR mechanism at this time, should the mechanism be designed provide benefits to customers?

A. Yes, it should. One of the fundamental principles of performance-based ratemaking is that customers must experience distinct, quantifiable benefits relative to traditional cost-of-service ratemaking. The Department has acknowledged the importance of this principle in recent PBR decisions. In Phase II of the recent Southern rate case, the Department noted that Southern must demonstrate that its proposal provides "real benefits" to ratepayers. (Department Decision, Docket No. 99-04-18, Phase II, at 43.) In the recent investigation into PBR regulation for electric distribution companies, the Department found that "In principle, PBR plan design should strive to align the interests of ratepayers and shareholders." (Department Decision, Docket No. 99-06-21, 2/2/2000, at 28).

The Federal Energy Regulatory Commission (FERC) also acknowledges that customer benefits are a fundamental requirement of any PBR mechanism. In its Policy Statement on Incentive Regulation, FERC identifies five regulatory standards for implementing specific PBR mechanisms: they should (1) be prospective, (2) be voluntary, (3) be understandable, (4) result in quantified benefits to customers, and (5) maintain or enhance incentives to improve the quality of service. (FERC Policy Statement on Incentive Regulation, Docket No. PL92-1-000, October 30, 1992, at 3-4.) FERC emphasizes that the benefits to customers must be quantified, and cannot be based on speculation about the potential for savings.

Q. The Company witnesses claim that the CNG IRP proposal will provide benefits to customers. Do you agree?

A. No, I do not. The Company is using the wrong definition of customer benefits. CNG essentially argues that customers will enjoy benefits because they will be no worse off than they would be relative to the prices in place today. However, this is not the proper way to define the customer benefits associated with a PBR mechanism. The benefits to customers from a PBR mechanism should be measured relative to traditional cost-of-service ratemaking, not to the prices in place at the time of the PBR. Under traditional cost-of-service ratemaking, the merger savings would be passed on to customers through reduced rates, thereby making customers better off than they are today. The Company's proposed IRP is not designed to make customers better off than they are today, it is merely designed to ensure that they are no worse off.

Q. Please elaborate on the appropriate way to define customer benefits associated with a PBR mechanism?

A. With any PBR mechanism, customer benefits should be measured relative to the prices they would experience under traditional cost-of-service ratemaking. FERC emphasizes this point in its Policy Statement on Incentive Regulation:

> The Commission remains convinced that the benefits to consumers must be quantifiable even though the task is admittedly a difficult one... The cap must be designed to ensure that the incentive rate is no higher than it otherwise would have been under the projected

> traditional cost-of-service ratemaking. "Projected cost-of-service" simply means an annual estimate of the cost of service that the utility would otherwise expect to incur during the effective time period of its incentive rate proposal. If the utility proposed a five-year period, it would be required to include in its application with the Commission a comparison of expected incentive rates to the expected cost of service rates that it would otherwise propose to base it rates under traditional ratemaking. (FERC Policy Statement on Incentive Regulation, Docket No. PL92-1-000, October 30, 1992, at 12.)

FERC is quite clear that customer benefits of a PBR mechanism must be measured relative to traditional ratemaking, and must be demonstrated with a comparison of rates under the two future scenarios. The Company's definition of customer benefits – i.e., that customers will be no worse off relative to how they are today – clearly does not meet this fundamental standard.

Q. Please explain why the Company's definition of customer benefits is simply based on the premise that customers will be no worse off than they are today.

A. The Company claims that there will be four types of customer benefits resulting from its IRP proposal. First, prices will not increase, as a result of the four-year rate freeze. Second, customers will enjoy gas costs reductions due to merger synergies, as a result of the PGA. Third, customers may enjoy a portion of the merger benefits, as a result of the earnings sharing mechanism. Fourth, customers can be assured that service quality will not deteriorate, as a result of the service quality plan.

None of these so-called "benefits" provide any real advantage to customers, relative to what they would experience under traditional cost-of-service regulation. First, under traditional regulation gas prices should be reduced as a consequence of the merger savings – not merely held constant. Therefore, this so-called benefit is actually a disadvantage to customers. Second, the PGA would be operational under traditional ratemaking, so customers would enjoy gas costs reductions due to merger synergies anyway. Therefore, these gas cost savings cannot be cited as a customer benefit from the Company's IRP mechanism. Third, the Company's earning sharing mechanism is designed to provide customers with very little, if any, savings resulting from the merger. This point is addressed in

more detail by my colleague Mr. Chernick. Fourth, the service quality plan is designed to ensure that customer service does not deteriorate over time, but does not provide any benefit relative to traditional ratemaking practices. In fact, because of the benchmarks and penalties that the Company has proposed for its service quality plan, customers may actually be worse off under this plan than they have been historically. I elaborate on this point in Section 6 of my testimony.

In sum, the Company uses the wrong definition of customer benefits by arguing that customers will be no worse off than they are today. However, when viewed from the appropriate perspective of how customers would fare relative to traditional ratemaking, it becomes clear that customers will indeed be worse off. In order for customers to benefit from a PBR mechanism, it must incorporate the estimated savings from the merger with Energy East. This point is elaborated upon in the next section of my testimony.

Q. What do you recommend to the Department, in light of the fact that the Company's proposed IRP does not provide benefits to customers?

A. I recommend that the Department reject the Company's proposed IRP mechanism. The Department should clarify (a) that any PBR mechanism must provide meaningful benefits to ratepayers, (b) that those benefits must be measured relative to the rates and services provided under traditional ratemaking, and (c) that those benefits must be quantified and clearly documented by the utility.

5. THE APPROPRIATE BASELINE FOR A PBR MECHANISM

Q. Do you agree with the Company's proposal to use the rates from Phase I of this rate case for the setting the baseline rates in the IRP?

A. No. The baseline rates in the Company's IRP mechanism should not be based on historical cost-of-service – they must incorporate the anticipated savings from the merger with Energy East.

Q. Why is it so important that the baseline rates in the IRP be set properly?

A. One of the fundamental principles of designing a PBR is that the starting rates must be an accurate representation of the utility's cost of service during the period in which the PBR is in place. If a PBR mechanism does not adhere to this principle then the twin goals of providing better incentives to the utility and providing customer benefits will be thwarted.

The Department acknowledged this important principle in its investigation into PBR for electric distribution companies, where it noted that "(e)ffective PBR rests upon an accurate portrayal of an EDC's (electric distribution company's) costs." (Department Decision, Docket No. 99-06-21, 2/2/2000, at 9). In its findings and policy recommendations, the Department reiterated that "(a)n appropriate baseline revenue requirement is critical to the achievement of real cost savings." (Department Decision, Docket No. 99-06-21, 2/2/2000, at 28).

FERC also emphasizes the importance of setting the proper baseline for a PBR mechanism. In its Policy Statement on Incentive Regulation, FERC identifies two general principles that all PBR mechanisms must adhere to. The first general principle is that incentive regulation should encourage efficiency. The second general principle is that starting rates must be just and reasonable in the traditional cost of service sense. (FERC Policy Statement on Incentive Regulation, Docket No. PL92-1-000, October 30, 1992, at 3 and 8.) FERC elaborates upon this point by noting that "(i)ncentive ratemaking must be prospective. Utilities cannot assume that their existing rates will be the base on which the incentive mechanism will apply. The Commission must determine that the base rates, calculated on a cost-of-service basis, are just and reasonable at the inception of an incentive rate program." (FERC Policy Statement on Incentive Regulation, Docket No. PL92-1-000, October 30, 1992, at 10.)

Q. Has the Company acknowledged the importance of setting the proper baseline rate for a PBR?

A. Yes. In his direct testimony in this docket Dr. Gordon provides five basic overarching themes regarding PBR design. One of these themes pertains to the proper baseline to use.

> Finally, I would emphasize that the price-cap plan must begin from a reasonably accurate starting point. The starting point must provide the utility with a reasonable opportunity to recover its costs (including the cost of capital). Any price-cap plan must begin from a starting point that balances the interests of the utility and its customers. If the starting point is set too low, the price-cap mechanism, as structured in CNG's RPA, would provide little opportunity, if any, for the utility to actually earn its cost of capital... On the other hand, if the starting point is set too high, customers would have to pay too much over the term of the plan... (Gordon PFT, at 11.)

Q. Does the Company's proposed IRP mechanism include an appropriate baseline for setting rates?

A. No, it clearly does not. The proposed IRP is based on rates determined in Phase I of this proceeding – rates which are based on a historical test year. Hence, the proposed baseline is a reflection of the cost-of-service experience by CNG in the past. A properly-designed PBR mechanism should be prospective, in that it should reflect the anticipated cost-of-service during the period in which the PBR will be in effect. While it is difficult to forecast all the changes that are likely to occur to a utility's cost of doing business in the future, there is one significant change that CNG has explicitly decided to neglect – the changes due to its merger with Energy East. By not incorporating the anticipated merger savings in the baseline rates, the Company's IRP violates one of the most important principles in PBR design and thus is fundamentally flawed. The Company's proposal is inconsistent with the Department's standard that a PBR be based on an "accurate portrayal" of costs. It is inconsistent with the FERC standard that PBR baseline rates be prospective and be just and reasonable. And the Company's proposal is inconsistent with its own witness' assertion that a PBR must begin with a "reasonably accurate" starting point that "balances the interests of the utility and its customers." If the baseline doe not include any of the merger savings, then it

clearly does not balance the interests of the utility and its customers – it simply allows the utility to enjoy the savings of the merger. If the merger savings are not incorporated into the rates, then the rates will be too high by definition.

Q. What do you recommend to the Department, in light of the fact that the Company's IRP is fundamentally flawed?

A. I recommend that the Department reject the Company's proposed IRP mechanism. As discussed above, this is not an appropriate time to implement a PBR for CNG. Furthermore, a utility should only be allowed to implement a PBR if the baseline rates are prospective and provide a reasonably accurate portrayal of the cost-of-service that can be expected during the period in which the PBR will be in effect.

6. CNG'S SERVICE QUALITY PLAN PROPOSAL

Q. Please describe the main components of the Company's service quality plan (SQP).

A. The Company's proposal includes the following five service quality indicators, goals for those service quality indicators, and penalties in the event the company's performance does not meet the established goals.

Q. Please discuss the Company's proposed service quality indicators.

A. The Company has proposed five service quality indicators: call center performance, leak response time, service call response time, third party damage to CNG's facilities, and meter reading.

Q. Are these service quality indicators appropriate for this company?

A. It is difficult to determine whether these are the best service quality indicators, because CNG has provided very little analysis of the service quality issues facing the Company. In establishing a service quality plan, it is important to begin with an analysis of all of the relevant service quality issues that are important to the company, it customers, and its employees. In this way, a utility can identify those areas of service that either have deteriorated in recent years or might deteriorate in the future under a different ratemaking system. The Company has not yet performed such a study, and therefore it is difficult to determine whether the

Company has chosen the appropriate service quality indicators for its SQP. The absence of information enabling a comparison between the Company's historic performance and other companies' historic performance makes an evaluation of the company's choice of indicators and relative performance levels difficult.

Q. Are there other service quality indicators that the Company should consider for its SQP?

A. Yes. Natural gas utilities have incorporated a number of other indicators into service quality plans. Some indicators focus on customer service; for example, bills rendered in billing period, billing errors or time required to correct errors, customer problems resolved on first call, and consumer complaints to regulatory agencies. Some indicators focus on safety; for example, placement in top quartile of AGA annual safety performance report, worker safety compared with an OSHA benchmark, and lost time incidents per 100 employees. Some indicators focus on customer satisfaction; for example, customer survey responses, and customer satisfaction with company representatives' knowledge and site visits.

In its recent review of the Southern Company's rates and charges, the Department listed additional indicators that should be included in an SQP, including service quality indicators for "gas costs, uncollectibles, and uncollectible write-offs in comparison to industry, regional or index goals or ranges." (Department Decision, Docket 99-04-18, January 18, 2000, at 42.)

The Company has noted several of these other service quality indicators, but has not explained why they were not incorporated into the proposed SQP. (Bryant PFT, at 8; CNG response to GPS-021.) The Company simply notes that the issue was discussed with various members of CNG management, and a general consensus was reached about the measures proposed in the SQP. (Bryant PFT, at 8.)

Q. What do you recommend to the Department regarding the Company's proposed service quality indicators?

A. The Department should require the Company to provide an analysis supporting the choice of specific service quality indicators that are relevant for CNG. Such

an analysis would include comparison of the Company's past performance in many service quality areas with comparable utilities, as well as an evaluation of the most appropriate service quality indicators for the future. The Company's evaluation should address the service quality indicators listed above, and identify specific indicators to use in light of the Company's past performance and in light of the merger with Energy East.

Q. Please discuss the Company's proposed service quality goals.

A. Overall, the Company's proposal leaves the impression that the Company may not be willing to maintain the same level of service quality that it has offered in the past. For four of the five indicators, the proposed service quality goal is at or below the lowest performance of the last five years (service response time[1], third party damage, leak response time and actual meter reads). For call center response time, the goal is set for noticeably lower performance than that of the past four years.

This overall impression is particularly troubling in light of the fact that during merger proceedings Energy East and CTG Resources, parent company of CNG, claimed that the merger would result in improved and enhanced customer services following the merger. For example, the companies stated that CNG's customers would benefit from the best operational practices of NYSEG, an Energy East subsidiary. Despite the promises, the Department found insufficient evidence on the record regarding the companies' plans for implementing their best customer service practices. The Department was dissatisfied with the companies' failure to provide evidence supporting the conclusion that benefits would occur and with the lack of any quantification of customer service benefits to ratepayers. The Department requested a report that would identify and quantify realized and potential customer service benefits from the merger. (Department Decision, Docket No. 99-08-09, at 12-13.)

[1] In LFE 36 the Company explained that it has corrected the problem associated with the computer aided dispatch system that resulted in a lower percentage response for 1999.

Clearly, the customer benefits anticipated from the merger should be an important factor in determining the appropriate service quality indicators and goals for CNG. However, the Company has provided service quality goals that at best are designed to maintain past performance, and at worst could result in deterioration of past performance.

Q. Has the Company proposed an appropriate goal for call center performance?

A. This is not entirely clear. It appears as though the Company's performance in this area has been satisfactory, relative to other utilities. However, the proposed goal is slightly less stringent than CNG's experience of recent years.

Q. Has the Company proposed an appropriate goal for leak response time?

A. No. The Department has already indicated that the Company's current level of performance on leak response time is inadequate. In Phase I of this proceeding, the Department stated that it "is concerned about the percentage of responses that meet the guidelines [for gas odor complaint response time]; there must be improvement in this area." (Department Decision, Docket No. 99-09-03, May 25, 2000, at 50.) The Department's statement was in response to evidence that the Company met the Department's guideline 86% of the time during normal hours and 97% of the time during off hours. The Company's proposal in the SQP to establish targets of 83% during normal hours and 95% during off peak hours is not responsive to the Department's requirement that the Company improve its performance.

Q. Has the Company proposed an appropriate goal for service call response?

A. While the Company has increased its goal for this indicator from its original proposal, the goal may still be too low to prevent some deterioration in service. The Company has modified its original proposal for the percentage of utility service appointments met from 83% to 90%. (LFE 36, CNG response to OCC II-094.) This goal is more consistent with maintaining service call response; however there are three factors that indicate that the goal may still not prevent deterioration in the quality of service call response.

First, the company has explained that its lowest percentage level from the past five years, 89%, was due to problems with a new computer aided dispatch system, which have since been corrected (LFE 36). Besides the 89% rate in 1999, the next lowest response rate was five years earlier when the Company met 91% of its scheduled appointments. From 1996 through 1998 the Company met at least 92% of its scheduled appointments. Thus, the proposed service call response level of 90% may still be lower than reasonable based on the Company's historical performance.

Second, the Company establishes a goal for number of appointments scheduled within two and four hour windows (21,000 appointments) that is significantly below the company's performance in recent years. Reducing the minimum number of appointments that must be scheduled within two and four hour windows will mean that it is much more easy for the company to achieve the goal for percentage of appointments actually met, and could permit the Company's performance for this indicator to decrease from historic levels without penalty to CNG.

Third, the Company emphasizes that its practice of offering appointment within a 2 hour window is relatively uncommon. However, the proposed goal is for appointments scheduled and met within two and four-hour windows. Thus, it is difficult to determine how significant the two-hour appointments are in evaluating the Company's performance.

Q. Has the Company proposed an appropriate goal for damage to CNG facilities?

A. No. The Company proposes to establish the goal at a higher number of hits than the Company has experienced in any of the last five years. The Company asserts, without any supporting information, that its performance is "in line with the other two Connecticut gas companies." (CNG response to OCC II-090.) Even if that assertion is true, the Company has proposed a goal that would not maintain the Company's historic performance because the goal is higher than what has been experienced in the past five years.

Q. Has the Company proposed an appropriate goal for meter reading?

A. The Company has established its goal at the level of its lowest performance in the past five years, its performance of 1999. The Company argues that setting a goal at the lowest performance of five years would maintain CNG's past level of performance and would not result in penalties to the Company if its performance in the next five years is the same as the past five years (CNG response to OCC II-097.) However, the Company's performance on meter reading has shown a steadily deteriorating trend. In the past five years the percentage of actual meter reads has decreased steadily from a high of 91% in 1995 to a low of 86% in 1999. If the Company's historic performance reveals a trend of decreasing service quality for this indicator, setting the goal at the Company's lowest performance level indicates that the Company may not be committed to maintaining its historic level of service to customers.

Q. Please describe the Company's proposed penalties for failure to meet the service quality goals.

A. The Company has proposed that failure to meet any of the service quality goals would result in a maximum penalty of $50,000, or four basis points. If the Company were to be penalized for all five of the goals, the maximum penalty would be $250,000, or twenty basis points. (Supplemental Testimony of Robert Rude, at 10; and Bryant PFT 7; CNG response to OCC II-089.) In addition, CNG has proposed that prior to imposing a penalty, the Company could request a hearing to determine whether failure to achieve the established goal was actually within the Company's control. (Bryant PFT at 7.)

Q. Are the Company's proposed penalties adequate to prevent deterioration in quality of service?

A. No. The Company's proposal to cap penalties at four basis points for each indicator, with a total cap of twenty basis points, is unlikely to be sufficient to capture management attention and serve as a deterrent to reducing CNG costs at the expense of service quality. The penalty for each deviation from a service quality goal ($5,000 or $10,000) is quite small. For example, the meter reading goal is for 86% of meter reads to be actual, and the Company proposed to pay a

$5,000 penalty for each percent that the actual meter reading performance falls below 86%, up to a maximum of $50,000. This means that actual meter reads could drop to as low as 76% and the Company would incur a penalty of only four basis points. Clearly, this penalty is too low for such a large deterioration in customer service.

In addition, the Company's proposal to place an overall cap on the penalties for each service quality indicator may not protect customers from significant deterioration in service quality. Once the cap is reached, the Company would no longer face a financial disincentive within the SQP for further deterioration of service.

Furthermore, the Company's proposed penalties are generally lower than those used by other utilities in their service quality plans. For example, Central Maine Power Company, one of the subsidiaries of Energy East, has an Alternative Rate Plan that includes service quality standards with a maximum penalty of 42 basis points.

Q. What level of penalties would be appropriate for the Company's SQP?

A. The level of penalties must be high enough to capture the attention of management, and ensure that there is no net financial benefit to the Company if it simply allows service to deteriorate and accepts the penalties. The penalties proposed by the Company are so low that service could be significantly compromised within penalties of only five to ten basis points. This is clearly not enough to capture management attention and prevent the Company from accepting the penalties.

In general, if the penalties were doubled – so that each service indicator had a penalty of eight basis points and all the indicators combined had a penalty of 40 points – they would be within the range that management will clearly respond to. Furthermore, the proposed caps should be removed so that continued deterioration in service quality will result in increasing levels of penalties.

When considering the size of penalties and whether to use a cap, it is important to remember that the goal of the SQP is to prevent deterioration of service. If the SQP is working properly, then no penalties will be levied on the Company. If, on the other hand, the Company is frequently paying penalties and bumping up against a penalty cap, then the SQP is not working properly – it is not providing sufficient incentive for the Company to maintain customer service levels.

Q. Would the Company's ability to request a hearing prior to the imposition of a penalty be a useful component of the SQP?

A. No. The Company states that a hearing may be necessary "to determine if the failure to achieve the identified service level was actually within the Company's control." (Bryant PFT at 7.) This sort of proceeding would be administratively burdensome and should not be necessary if the Company has selected service quality indicators that are within the Company's control. As the Company has stated, performance indicators "should focus on specific business activities, so that specific action can be taken if performance falls below an acceptable level." (Bryant PFT at 3.)

Q. What do you recommend to the Department regarding the Company's proposed service quality plan?

A. I recommend that the Department reject the Company's proposed service quality plan. If the Company is allowed to implement any form of PBR mechanism, it should be required to propose a new SQP that accounts for the concerns I have raised above. The new proposal should be based on a comprehensive assessment of potential service quality indicators. This assessment should build upon the report that the Department required CNG to file on October 1, 2000 in response to its merger proposal. (Department Decision, Docket No. 99-08-09, at 12-13.) The new proposal should include goals that will clearly maintain the level of service quality provided in the past, as well as goals that will result in improvements in service quality associated with the merger with Energy East. Finally, the new proposal should include meaningful penalties that are not subject to a cap.

Q. Does this conclude your testimony at this time?

A. Yes, it does.

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PROFESSIONAL EXPERIENCE

Synapse Energy Economics Inc., Cambridge, MA. Vice President, 1997-present.
Conducting research, writing reports, and presenting expert testimony pertaining to consumer, environmental, and public policy implications of electricity industry regulation. Primary focus of work includes electricity industry restructuring and competition, electric power system planning, power plant performance and economics, performance-based ratemaking, market power, stranded costs, customer aggregation, information disclosure, air quality, energy efficiency, renewable resources, and many aspects of consumer and environmental protection.

Tellus Institute, Boston, MA. Senior Scientist, Manager of Electricity Program, 1992-1997.
Responsible for managing six-person staff that provided research, testimony, reports and regulatory support to consumer advocates, environmental organizations, regulatory commissions, and state energy offices throughout the US.

Association for the Conservation of Energy, London, England. Research Director, 1991-1992.
Researched and advocated legislative and regulatory policies for promoting integrated resource planning and energy efficiency in the competitive electric industries in the UK and Europe.

Massachusetts Department of Public Utilities, Boston, MA. Staff Economist, 1989-1990.
Responsible for regulating and setting rates of Massachusetts electric utilities. Drafted integrated resource planning regulations. Evaluated utility energy efficiency programs.

Massachusetts Office of Energy Resources, Boston, MA. Policy Analyst, 1987-1989.
Researched and advocated integrated resource planning regulations. Participated in demand-side management collaborative with electric utilities and other parties.

Energy Systems Research Group, Boston, MA. Research Associate, 1983-1987.
Performed critical evaluations of electric utility planning and economics, including production cost modeling and assessment of power plant costs and performance.

Union of Concerned Scientists and Massachusetts Public Interest Research Group,
Cambridge and Boston, MA. Energy Analyst, 1982-1983. Analyzed environmental and economic issues related to nuclear plants, renewable resources and energy efficiency.

EDUCATION

Masters, Business Administration. Boston University, Boston, MA, 1993.
Diploma, Economics. London School of Economics, London, England, 1991.
B.S., Mechanical Engineering. Tufts University, Medford, MA, 1982.
B.A., English. Tufts University, Medford, MA, 1982.

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