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May 26, 2009

**By Hand**

Hon. Jaclyn Brillling  
Secretary  
New York State  
Public Service Commission  
Three Empire State Plaza  
Albany, New York 12223

**Re: Case 08-E-0539 -- Con Edison Electric Rates**

Dear Secretary Brillling:

In its Order Setting Electric Rates, issued April 24, 2009 in the referenced proceeding ("2009 Rate Order"), the Commission reduced by \$60 million the Company's electric revenue requirement for the twelve months ending March 31, 2010 (the "Rate Year"), by imputing \$60 million of "austerity" cost reductions. The Commission also directed Con Edison to file within 30 days its plan to achieve such costs reductions, and report quarterly thereafter its progress in achieving those cost reductions. (2009 Rate Order, Ordering Clause 8).

The Company is submitting, under separate cover, a petition for rehearing of the Commission's austerity imputation. The Company's petition demonstrates that the Commission's unprecedented action is not only unlawful in several respects, it is unwarranted, unjustified and not in the public interest. Subject to the Commission's determination of the rehearing request, the Company is submitting a list of austerity measures that it is implementing in compliance with the Commission's directive. This compliance filing, however, should not be construed to indicate agreement or acceptance of the Commission order. The Company's rehearing petition explains why the Commission erred in assuming that its austerity imputation could be implemented in a manner that did not pose risks for customers, in the form of unintended service impacts and higher long-term costs, and for investors, in the form of lower returns and greater business risks of utility investments. There are always consequences to deferring infrastructure investments or maintenance, even when the targeted projects do not directly impact safety or reliability of service, not the least of which are loss of jobs by contractor and/or Company employees. When cost levels are already mitigated to the minimal reduced levels, reducing expenditures is clearly counterproductive.

As described in greater detail below, the measures to be implemented include reductions in management compensation and other employee benefits, corporate-wide cost reduction initiatives and reductions in expenditures for capital projects and O&M programs.

1. Labor Costs, Including Compensation and Other Employee Benefits (\$6.5 million)

The first category of austerity measures includes reductions in base salaries of executives and senior to mid-level management personnel, as well as employee benefit reductions applicable to all management employees. Salaries of Company executives named in the Company's Proxy Statement will be reduced by 5 percent; other senior executives by 3 percent, other officers by 2 percent; upper (Band 4) management employees by 1 percent; and mid-level (Band 3) management employees by 0.5%. In addition, the Company will reduce by 50 percent the (a) Thrift Savings (401K) Plan matching program, under which the Company matches half of employee contributions, up to 6 percent of their salaries, and (b) Discount Stock Purchase Plan, under which the Company contributes 10 percent of the cost of Company stock purchased by employees on a monthly basis. Except for the salary reductions applicable to executives, these measures will be in effect from July 1, 2009 to June 30, 2010. The duration of the salary reductions applicable to executives will be revisited in 2010. Finally, the Company has delayed by 60 days its hiring of 60 new associates under its Gold Program, the Company's leadership development and technical skills training program for recent college graduates, and has canceled its 2009 Summer Intern Program. In total, these measures are expected to achieve about \$6.5 million in cost reductions in the Rate Year (\$8.0 million on an annualized basis) applicable to electric service. The expected costs reductions associated with each of these austerity measures are listed below.

It should be noted that the Company is implementing salary reductions because the Commission identified executive and management compensation as a prime source for austerity cost reductions, at least in part in apparent reliance on misinformation with respect to austerity measures for executive compensation implemented by other utilities. However, as demonstrated on the record in this proceeding, Con Edison's executive and management compensation is already at or below the median of peer groups. Importantly, the revenue requirement established in the 2009 Rate Order already excludes a major portion of annual salary increases for executives and management employees.

|   | <u>Rate Year</u><br>(\$ million) |
|---|----------------------------------|
| a. Reduce base salaries for executives                      | 0.2                              |
| b. Reduce base salary for upper and mid-level management    | 0.3*                             |
| c. Reduce (50%) Thrift Savings Plan (401K) matching program | 3.8*                             |
| d. Delay (60 days) start of 2009 Gold Program               | 0.6                              |
| e. Cancel 2009 Summer Intern Program                        | 1.1                              |
| f. Reduce (50%) Discount Stock Purchase Plan                | <u>0.5*</u><br>6.5               |

2. Corporate-Wide Cost Reduction Initiatives (\$7.4 million)

The Company expects to achieve approximately \$7.4 million of cost reductions in the Rate Year (\$9.7 million on an annualized basis) applicable to electric service through corporate-wide initiatives. These initiatives include restrictions on business travel and attendance at professional conferences, reductions in transportation and communication costs, suspension of some memberships in industry associations, reductions in consulting services, suspension of the Company's Leadership and Career Development Program for senior management, reduction of costs associated with employee seminars, conferences and service recognition events, and reduction in vested vacation and employee health costs to be achieved by continued use of overtime work to delay some new hires. The expected costs reductions associated with each of these austerity measures are listed below.

These measures are not expected to directly affect the near-term provision of safe and reliable service. They will, however, necessarily have adverse impacts in the form of lower service quality. For example, reduced employee education and professional development will result in a less proficient workforce and reduced participation by the Company in industry associations will, among other things, diminish the Company's ability to influence policies that benefit customers and to exchange best practices with peer utilities. Moreover, in light of the doubling of the 1 percent productivity imputed by the Commission in the 2009 Rate Order, which will require the Company to more aggressively manage costs, further cost reductions without impacting the Company's operations will be particularly challenging, especially in areas such as transportation (e.g., vehicles) and communications (e.g., mobile phones), which are underfunded in the Rate Year due to the Commission's disallowance of Rate Year general equipment costs. If nothing else, the Company will be forced to reduce its focus on desirable, but truly discretionary, programs such as the Company's solar pilot program, which the Company believes to be a promising element of the future energy profile of its service territory.

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\*Effective July 1, 2009 to June 30, 2010.

|   | <u>Rate Year</u><br>(\$ million) |
|---|----------------------------------|
| a. Reduce (75%) travel costs  | 0.8*                             |
| b. Reduce professional conference costs                                   | 0.2*                             |
| c. Reduce transportation costs  | 0.2                              |
| d. Reduce communication costs   | 0.1                              |
| e. Suspend Leadership and Career Development Program                      | 0.2*                             |
| f. Reduce (25%) corporate dues in industry associations                   | 0.6*                             |
| g. Reduce costs for employee meetings, conferences and recognition events | 0.5                              |
| h. Reduce consulting services   | 1.6*                             |
| i. Reduce vacation and health costs associated with new hires             | <u>3.2</u>                       |
|   | 7.4                              |

3. Reduction in Expenditures for Capital Projects and O&M Programs (\$33.0 million)

The final category of austerity measures includes reduction in expenditures for capital projects and O&M programs. These measures include approximately \$3.2 million in reduced expenditures for 2009 R&D programs, such as the development and demonstration of an advanced two-way network remote monitoring system; approximately \$2.4 million in cost reductions for facility improvements, primarily resulting from a delay in starting renovations of the Company's headquarters to install a sprinkler system in compliance with Local Law 26; approximately \$9 million representing carrying charges associated with capital expenditure reductions of approximately \$139 million in 2009 (exclusive of capital cost reductions associated with project deferments as a result of lower demand);\*\* and approximately \$18.4 million in reduced O&M program costs in 2009. The capital projects and O&M programs identified for cost reductions in 2009, and the targeted amounts of cost reductions, are shown on Attachment A and Attachment B, respectively.

The targeted reductions are, for the most part, associated with multi-year and low-priority projects and programs, and are relatively modest on an individual project or program basis. For example, capital projects targeted for delay include replacement of paper-insulated lead cable, various Information Technology projects and low-priority underground enhancements. Operation and maintenance programs targeted for reductions include substation equipment testing and repairs and customer operations programs, including customer educational advertising. Actual reductions in project and program costs in these identified projects and programs and/or in other capital projects and O&M programs will be determined based on a continued monitoring of operational needs and priorities, and will be reported in the Company's

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\*Effective July 1, 2009 to June 30, 2010.

\*\* The Company understands the 2009 Rate Order to say that, unlike capital cost reductions due to lower demand, the capital costs reductions associated with austerity will not be subject to the downward-only reconciliation applicable to capital expenditures.

quarterly reports. The expected costs reductions associated with each of these austerity measures are listed below.

While the Company made every effort to apply cost reductions to capital projects and O&M programs in a manner that will minimize their adverse impact on provision of safe and reliable service, the revenue requirement set by the 2009 Rate Order already reflects minimum levels for capital and O&M expenditures, and cuts below such levels can have adverse impacts. For example, the Company's current expectation is that the targeted O&M program reductions will result primarily from program scheduling adjustments without increasing the near-term level of expenditures to "catch up" with the deferred expenditures. However, costs could increase in the long run should such deferrals result in increased failures of equipment. Similarly, compressing the schedule for upgrading facilities to comply with local laws could result in greater future costs to address unforeseen contingencies. A more immediate impact will be the loss of several hundred contract and/or Company employee jobs.


|   | <u>Rate Year</u><br>(\$ million) |
|---|----------------------------------|
| a. Reduce R&D Programs                        | 3.2                              |
| b. Reduce facilities expenditures             | 2.4                              |
| c. Reduce capital expenditures                | 9.0                              |
| d. Other operating cost-reduction initiatives | <u>18.4</u>                      |
|   | 33.0                             |

4. Unidentified Cost Reductions (\$13.1 million)

The measures enumerated above are expected to result in \$46.9 million in Rate Year cost reductions applicable to electric service. With respect to the remaining \$13.1 million in unidentified cost reductions, the Company expects that a portion of these additional cost reductions will be identified when the Company develops its 2010 capital and O&M budgets, which will cover the last three months of the Rate Year. The Company will provide the Commission as part of its quarterly reports the reductions expected to be realized during the first three months of 2010 (which are the last three months of the Rate Year) when the 2010 budgets are finalized. Should the Company identify cost reduction opportunities that would require regulatory approval prior to implementation, the Company will seek such approval in a timely manner. As to the remaining portion of the unidentified cost reductions, the Company will continue to search for further cost-reduction opportunities, but its ability to do so is far from certain, given that, as a practical matter, the Company cannot implement

all of its austerity measures before July 2009, leaving roughly nine months of the Rate Year to achieve austerity reductions applicable to all twelve months of the Rate Year, in addition to the cost reduction measures that are needed to achieve the 2 percent productivity imputed by the Commission.

Very truly yours,

A handwritten signature in cursive script, reading "Edward J. Rasmussen". The signature is written in dark ink and is positioned to the right of the typed name "Edward J. Rasmussen".

C: Parties to Case 08-E-0539

**Electric Rate Case Austerity Measures - 2009 Capital**

| \$ Millions<br>DESCRIPTION  | 2009<br>Impact |
|---|----------------|
| Low Priority Underground Enhancements (See Attachment A Page 2 of 2 - "A")        | 30,300         |
| IT Projects (See Attachment A Page 2 of 2 - "B")                                  | 22,800         |
| Facilities  | 10,800         |
| Transformer and Equipment Purchases   | 14,000         |
| Additional feeders, switches  | 8,900          |
| Feeder M51  | 6,700          |
| Emergent Transmission Reliability   | 6,500          |
| Lower Priority Overhead Enhancements (See Attachment A Page 2 of 2 - "C")         | 6,300          |
| Continuance (63rd Street - Bus Work) - Defer                                      | 5,000          |
| Paper Insulated Lead Cable (PILC)   | 5,000          |
| Transformer Installations   | 3,000          |
| Replace 345kV Circuit Breaker Other Than ATB - Defer                              | 3,000          |
| Pumping Plant Improvements  | 3,000          |
| Outage Scheduling System  | 2,000          |
| EMS for Electric/Steam Operation  | 2,000          |
| HiPot (Fall)  | 2,000          |
| Re-Conductor Dunwoodie – Sprain Brook Transmission Corridor                       | 1,500          |
| Substation Automation Target Information System                                   | 1,000          |
| Security Enhancement  | 1,000          |
| Substation Loss Contingency   | 1,000          |
| Roof Repairs  | 854            |
| U7 Steam Heat Traps/Heat Condensate Recovery - Defer                              | 600            |
| Upgrade Unit 70 boiler casing/insulation  | 846            |
| Additional G&T Devices  | 500            |
| Diesel/Blackstart Restoration (Upgrade Light and Power for Feeder Pressurization) | 200            |
| <b>TOTAL - AUSTERITY</b>  | <b>138,800</b> |

**Electric Rate Case Austerity Measures - 2009 Capital**

| \$ Millions<br>DESCRIPTION                           | 2009<br>Impact |
|--|----------------|
| <b>"A" - Lower Priority Underground Enhancements</b> | <b>\$ 30.3</b> |
| Underground Secondary Cable Replacements             | 16.1           |
| Service Box Cover Replacements                       | 4.0            |
| Street Light Reliability                             | 3.0            |
| Vented Manhole Replacements                          | 3.2            |
| Coastal Storm Mitigation                             | 2.0            |
| ATS Installation USS Reliability XW                  | 1.0            |
| Targeted Primary DBC Replacement                     | 0.5            |
| Sectionalizing Switches                              | 0.5            |
| <b>"B" - IT Projects</b>                             | <b>\$ 22.8</b> |
| Work Management System                               | 12.1           |
| Mapping System Upgrades                              | 6.0            |
| Control Center Upgrades                              | 2.0            |
| Meter Shop ADAMS                                     | 1.3            |
| Distribution Engineering Workstation (DEW)           | 0.5            |
| Grid Optimization                                    | 0.5            |
| 4KV Load Shedding                                    | 0.5            |
| <b>"C" Lower Priority Overhead Enhancements</b>      | <b>\$ 6.3</b>  |
| Osmose   | 1.5            |
| Autoloop Reliability                                 | 3.5            |
| Rear Lot Pole Elimination                            | 1.0            |
| Additional 13KV Feeder Sectionalizing                | 0.3            |



**Electric Rate Case Austerity Measures - 2009 O&M Attachment B**

| \$ Thousands<br>DESCRIPTION                            | 2009<br>Impact |
|--|----------------|
| Transformer vault cleaning and repairs                 | 1,600          |
| Tree Trimming  | 1,600          |
| Unit substation maintenance                            | 700            |
| Maintenance associated with capital                    | 300            |
| Distribution equipment inspections                     | 600            |
| East River Unit #6 Generator Rewind and Other          | 2,625          |
| Substation facilities maintenance                      | 1,500          |
| Substation equipment testing and repairs               | 3,200          |
| Central Engineering - reduction in outside studies     | 200            |
| <b>Systems and Transmission Operations programs:</b>   |                |
| - Planning Studies                                     | 100            |
| - Conductor Cart Training                              | 50             |
| - Live Line Method Procedures                          | 100            |
| - Van Nest Facilities Costs                            | 250            |
| - Targeted transmission cable and equipment repairs    | 1,160          |
| - Coating Refurbishment                                | 250            |
| - Manhole Inspections                                  | 250            |
| - Medium Pressure Manhole Refurbishment                | 75             |
| - PFT Patrols  | 300            |
| - Tower Painting                                       | 40             |
| - Security Improvements                                | 40             |
| - Improve Overhead Transmission Restoration Capability | 700            |
| - Install Bird Discouragers                            | 200            |
| - Corrosion Work Orders                                | 42             |
| Customer Operations programs                           | 2,050          |
| Other Programs   | 1,087          |
| <b>TOTAL - AUSTERITY (A)</b>                           | <b>19,019</b>  |

**(A)** - The total amount reflected here for Austerity includes \$600 thousand allocated to gas and steam operations.