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COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

JUN 14 2017

PUBLIC SERVICE  
COMMISSION

In the Matter of:

APPLICATION OF NOLIN RURAL ELECTRIC )  
COOPERATIVE CORP. FOR A GENERAL RATE ) Case No.  
INCREASE ) 2016-00367

**ATTORNEY GENERAL’S POST-HEARING BRIEF**

Comes now the intervenor, the Attorney General of the Commonwealth of Kentucky, by and through his Office of Rate Intervention, and hereby tenders his post-hearing brief in the above-styled matter.

**A. Nolin Should Not be Allowed to Double Recover Pre-Pay Program Costs**

In Case No. 2011-00141, the Commission approved Nolin Rural Electric Cooperative Corp. [“Nolin”]’s request to implement a three-year pilot optional pre-pay metering tariff.<sup>1</sup> Customers choosing to participate in the pre-pay program did not have to pay a deposit, late charges, or disconnect or reconnect fees.<sup>2</sup> Furthermore, as noted in the final order in that case, the service fee charge of \$5.10 per month (or \$0.17 daily) to program participants covered the cost of “. . . necessary metering equipment and computer software.”<sup>3</sup> At the time that Nolin’s application for a pre-pay metering tariff was approved, the Company was using an AMR metering system.<sup>4</sup> In response to PSC 2-5 (a) in Case No. 2011-00141, Nolin provided a cost justification for the service fee charge pre-pay customers would have to pay. Significantly, that cost justification was based *solely* upon the costs of the pre-pay meter itself (\$300 per customer), and the software necessary for its operation (\$66.67 per customer).

<sup>1</sup> Case No. 2011-00141, Final Order dated June 20, 2011, p. 10-11. During the test year in the instant case, Nolin had 1,376 customers on pre-pay service (Case No. 2016-00376, Response to PSC 1-18, p. 2).

<sup>2</sup> Id. at p. 2.

<sup>3</sup> Case No. 2011-00141, Final Order p. 3.

<sup>4</sup> Id. at p. 4.

In Case No. 2014-00436, the Commission approved Nolin's CPCN application for installation of AMI meters across its entire system. The new metering system was fully-deployed as of July 18, 2016, at an expense of \$6,007,447.<sup>5</sup> Nolin's application in that case stated that the project would enable Nolin to provide remote connects/disconnects and optional pre-pay metering capabilities to all its customers,<sup>6</sup> all of which would be remotely initiated and monitored from Nolin's central office.<sup>7</sup> Nolin's new AMI system provides the Company with the capability of offering pre-pay service to most of its customers without having to install any additional devices or software at the customer's location. The records in Case Nos. 2011-00141 and 2014-00436 are void of any evidence indicating that Nolin would incur any additional costs related in any manner to overhead or labor associated with the pre-pay program.

Whereas the Commission's approval of the pre-pay program service charge in Case No. 2011-00141 was premised upon the need to recover costs associated with metering and software, Nolin in the instant case asserts for the first time that it should be allowed to continue that service charge based solely upon the *entirely new* claimed costs of: (a) "Overhead;" and (b) "Labor."<sup>8</sup> These items of claimed expense were never mentioned in Case No. 2011-00141, when Nolin initiated its pilot program utilizing a limited number of pre-pay meters that were less sophisticated than the type of AMI meters Nolin has now deployed system-wide. Moreover, nowhere in Nolin's response to Commission PHDR item no. 26 did the company provide a definition for these claimed expenses. Nolin has thus failed

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<sup>5</sup> Response to PSC 4-23.

<sup>6</sup> Case No. 2014-00436 Application, Exhibit 1, pp. 1, 3; Exhibit 4 p. 1; and Final Order dated Feb. 13, 2014, p. 4.

<sup>7</sup> Id., Exhibit 2, pp. 1, 3.

<sup>8</sup> Nolin's response to Commission post-hearing data request ["PHDR"] item no. 26, Case No. 2016-00367.

to provide any justification for including these items of claimed expense in costs charged to pre-pay customers.

Furthermore, the term “Overhead,” when juxtaposed with Nolin’s calculations presented in response to the Commission’s data request, appears to merely refer to an *arbitrary* amount (55%) of *averaged* hourly cost of labor. No explanation is provided to support the claimed 55% figure. Additionally, Nolin has provided no evidence that the “Overhead” to which it refers represents any costs different than those incurred during installation of the initial pre-pay meters and supporting infrastructure. In fact, any costs for “Overhead” associated with administering the pre-pay program through means of Nolin’s new AMI meters are already embedded in base rates. Moreover, there is no record evidence indicating what costs “Overhead” represents, or why “Overhead” would represent a reasonable determination of the pre-pay program’s costs.

Additionally, the term “Labor” to which Nolin refers is an expense which Nolin has clearly already captured in base rates, through the salaries, benefits and retirement provided to its staff. The record is void of any evidence that Nolin, once it installed its AMI meters, had to hire more staff to administer the pre-pay program.

Given that the pilot program authorized in Case No. 2011-00141 made no provision for “Overhead” and “Labor” to operate that less sophisticated and now-retired system, it is simply not credible that the Company incurs any such costs using today’s more advanced metering system. Any recovery for these items of claimed expense would constitute an impermissible double recovery. Accordingly, the Commission should deny Nolin’s last-minute attempt to enhance its revenues.

## **B. The Commission Should Reduce Nolin's Proposed Fees for Connections, Disconnections and Reconnections**

In response to Commission PHDR item no. 11, Nolin stated that it intends to reduce its fees charged for connections, disconnections and reconnections from the current \$20 to \$17.00. This is a reduction of *only 15%* from the current fees. In the same response, Nolin sets forth a cost justification which, just as was the case for the pre-pay program, cites "Labor" and "Overhead" as the only cost components.

As discussed *supra*, Nolin's application in Case No. 2014-00436 stated that its AMI meters would enable the Company to provide connects/disconnects to its customers,<sup>9</sup> all of which would be conducted remotely from Nolin's central office,<sup>10</sup> without the need for a truck roll and manual service call at the customer's location. The records in both Case No. 2014-00436 and the instant case are completely void of any evidence indicating that Nolin would incur any additional costs related in any manner to "Labor" or "Overhead" associated with connections, disconnections and reconnections. Moreover, Nolin assured this Commission in Case No. 2014-00436 that costs related to connections, disconnections and reconnections would be reduced significantly if the Commission approved its CPCN.<sup>11</sup> Nolin should be held to its commitment to pass cost savings resulting from the AMI meter conversion along to its customers.

Furthermore, the term "Overhead," when juxtaposed with Nolin's calculations presented in response to Commission PHDR no. 11, appears to merely refer to an *arbitrary* amount (55%) of *averaged* hourly cost of labor. No explanation is provided to support the

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<sup>9</sup> Case No. 2014-00436 Application, Exhibit 1, pp. 1, 3; Exhibit 4 p. 1; and Final Order dated Feb. 13, 2014, p. 4.

<sup>10</sup> *Id.*, Exhibit 2, pp. 1, 3.

<sup>11</sup> See Attorney General's Hearing Exhibits 2 and 3, Case No. 2016-00367.

claimed 55% figure. In fact, any costs for “Overhead” associated with the conducting of connections, disconnections and reconnections are already embedded in base rates. Moreover, there is no record evidence indicating what costs “Overhead” represents, or why “Overhead” would represent a reasonable determination of costs associated with connections, disconnections and reconnections.

Additionally, the term “Labor” to which Nolin refers in that same response is an expense which Nolin has already captured in base rates, through the salaries, benefits and retirement provided to its staff. The record is void of any evidence that Nolin, once it installed its AMI meters, had to hire more staff to conduct connections, disconnections and reconnections. If the Commission were to approve these items of claimed expense, it would constitute an impermissible double recovery.

Nolin has previously assured this Commission and its ratepayers that the new AMI system would greatly reduce costs associated with connections, disconnections and reconnections. The Company should be held true to its word.

### **C. Nolin’s Residential Customer Charge Should be Set at a Rate that Incentivizes Customer Conservation**

Nolin’s proposal to increase its residential customer charge from the current \$9.04 per month to \$20.00 per month, an increase of 121.2%, is based solely on the cost of service study that Nolin witness James Adkins prepared.

However, the Attorney General believes that Nolin’s proposal would recover too much of the overall revenue increase through the customer charge. From an economic perspective, the notion that fixed costs must be recovered through fixed charges is misguided. Regulation should serve as surrogate for competition to the furthest extent possible. Pricing

policy for regulated public utilities should mirror those of competitive firms to the greatest extent practical. *All* costs are *variable* in the long run, not fixed. In competitive, efficient pricing structures high levels of upfront, or sunk, fixed costs are recovered volumetrically based on usage. Upfront expenses for customer-related distribution costs are most commonly associated with the creation of the distribution system, such as secondary transformers and poles. These costs are incurred regardless of the number of customers that join the system, and should not necessarily be reflected in the customer charge, especially under the incorrect argument that fixed costs must be collected through fixed charges.

In competitive markets, prices are equal to marginal costs, which capture cost variability. Although many utilities' short-run costs are fixed in nature, the rates they charge should be based on long-run costs, which are variable in nature. Not only does this pricing mechanism adhere to widely-recognized and long-held economic principles, but it also addresses *fairness* and *equity*. By recovering short-run fixed costs as long-run variable charges, those who use more electricity receive more benefits and thus pay more than those who receive fewer benefits. In regard to electricity, consumption (i.e., kWh usage) is the best and most direct indicator of benefits received.

The process of recovering largely fixed costs in the short-run with a pricing structure that recovers those costs on a volumetric basis is not unique. Indeed, most manufacturing, agriculture, and transportation industries are comprised of cost structure predominated with "fixed" costs. Invariably, Mr. Adkins' contention that fixed costs need to be recovered through fixed charges is incorrect, especially since all costs are variable in the long-run. When costs that vary in the long-term are reflected in volumetric charges, their recovery correlates more with conservation measures than if the costs had been recovered through a fixed charge.

A pricing structure that is largely fixed, such that customers' effective prices do not properly vary with consumption and such as Mr. Adkins proposes, promotes the inefficient utilization of resources. Pricing structures weighted heavily on fixed charges are more inferior from a conservation and efficiency standpoint than pricing structure that require consumers to incur more cost with additional consumption.

For thirty years, this Commission has recognized that energy conservation as a ratemaking standard "is intended to minimize the 'wasteful' consumption of electricity and to prevent consumption of scarce resources."<sup>12</sup> In Case No. 2012-00222,<sup>13</sup> LG&E requested an increase in the customer charge based solely on its cost of service.<sup>14</sup> In its order in that case, the Commission noted that in reviewing that increase, it was faced with ratepayer complaints stating that a higher customer charge would disincentivize them from making energy efficiency expenditures, and that their bills would rise even though they reduce their energy usage.<sup>15</sup> The Commission in that case noted:

Determining the proper balance between cost of service, energy efficiency incentives for the utility, and energy efficiency incentives for the customer is challenging and requires a close examination of the facts and circumstances of each case. . . . [W]ith the potential for huge increases in the costs of generation and transmission as a result of aging infrastructure, low natural gas prices and stricter environmental requirements, we will strive to avoid taking actions that might disincen energy efficiency.<sup>16</sup>

An excessively high fixed charge, such as that Mr. Adkins proposes, undermines future incentives for efficiency and is also unfair to customers who have already invested in those

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<sup>12</sup> Administrative Case 203, *The Determinations with Respect to the Ratemaking Standards Identified in Section III (d)(1)-(6) of the Public Utility Regulatory Policies Act of 1978*, p. 7 (Ky. PSC Feb.28, 1982).

<sup>13</sup> *In Re Application of Louisville Gas and Electric Company for an Adjustment of Its Electric and Gas Rates, A Certificate of Public Convenience and Necessity, Approval of Ownership of Gas Service Lines and Risers, and a Gas Line Surcharge*.

<sup>14</sup> *Id.*, Final Order dated Dec. 20, 2012, p. 12.

<sup>15</sup> *Id.*, p. 13.

<sup>16</sup> *Id.*, pp. 14-15.

resources, but who would now see a diminished return on their investment. Thus a smaller increase in the customer charge than that Nolin proposes is consistent with this Commission's longstanding policy to "avoid taking actions that might disincent energy efficiency."

Additionally, a smaller increase in the customer charge will preserve a greater degree of customer control over their electric bills; in contrast to a bill composed of a higher fixed charge that customers cannot avoid no matter what investments or behavioral changes they may make to reduce usage. The reduced ability to control and therefore lower one's utility bill is particularly harmful for low-income customers who have limited financial resources to meet their basic needs.

Nolin owes a fiduciary duty to its member-owners. However, the Company's proposed residential customer charge rate of \$20 per month is focused *solely* on reducing the Company's overall risk, does not take the needs of its member-owners into consideration, and thus fails to satisfy that duty. Instead, it would be more appropriate for Nolin to recover short-run fixed costs through the volumetric charge, which has the effect of sending proper pricing signals to customers to conserve and utilize resources efficiently.

As pointed out during cross-examination of Nolin CEO Mr. Miller,<sup>17</sup> the average of all Kentucky coop customer charges as depicted in Nolin Hearing Exhibit 1 is \$13.21.<sup>18</sup> The Attorney General believes this figure, representing a 46% increase, strikes a much more reasonable balance between reducing Nolin's risk, and sending proper long-term price signals to incentivize customer conservation. Finally, such an increase would also comport with the principle of gradualism, which Nolin's proposal clearly fails to satisfy.

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<sup>17</sup> Video transcript at 2:56:32.

<sup>18</sup> Excluding Owen RECC's \$20.00 customer charge as an outlier, because that coop utilizes a straight-fixed variable rate design.



Respectfully submitted,

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*Certificate of Service and Filing*

Counsel certifies that an original and ten photocopies of the foregoing were served and filed by hand delivery to Dr. Talina R. Mathews, Executive Director, Public Service Commission, 211 Sower Boulevard, Frankfort, Kentucky 40601; counsel further states that true and accurate copies of the foregoing were mailed via First Class U.S. Mail, postage pre-paid, to:

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this 14<sup>th</sup> day of June, 2017



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Assistant Attorney General