

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matters of:

ELECTRONIC APPLICATION OF KENTUCKY)
UTILITIES COMPANY FOR AN ADJUSTMENT) CASE No.
OF ITS ELECTRIC RATES AND FOR CERTIFICATES) 2016-00370
OF PUBLIC CONVENIENCE AND NECESSITY)

-and-

ELECTRONIC APPLICATION OF LOUISVILLE)
GAS AND ELECTRIC COMPANY FOR AN) CASE No.
ADJUSTMENT OF ITS ELECTRIC AND GAS) 2016-00371
RATES AND FOR CERTIFICATES OF PUBLIC)
CONVENIENCE AND NECESSITY)

JOINT BRIEF OF ATTORNEY GENERAL, SIERRA CLUB, METROPOLITAN HOUSING COALITION, ASSOCIATION OF COMMUNITY MINISTRIES, COMMUNITY ACTION COUNCIL FOR LEXINGTON-FAYETTE, BOURBON, HARRISON COUNTIES, INC., LOUISVILLE / JEFFERSON COUNTY METRO GOVERNMENT, and LEXINGTON-FAYETTE URBAN COUNTY GOVERNMENT, REGARDING RESIDENTIAL CUSTOMER CHARGE FOR ELECTRIC SERVICE

Come now the Attorney General of the Commonwealth of Kentucky; Sierra Club, Alice Howell, Carl Vogel, and Amy Waters (collectively hereinafter “Sierra Club”); Metropolitan Housing Coalition (“MHC”); Association Of Community Ministries (“ACM”); Community Action Council For Lexington-Fayette, Bourbon, Harrison Counties, Inc. (“CAC”); Louisville / Jefferson County Metro Government (“Louisville Metro”); and Lexington-Fayette Urban County Government (“LFUCG”)—collectively hereinafter the “Joint Briefing Intervenors”—each by counsel, and hereby tender the following brief limited solely to the issue of the residential customer charge for electric

service as set forth in the unanimous Stipulation and Recommendation (“Stipulation”) pending before the Commission in these two cases.¹

For the following reasons, the Joint Briefing Intervenors urge the Commission to approve the Stipulation’s proposed two-step increase in the residential customers charge for electrical service, from the current \$10.75 per month to \$11.50 (effective July 1, 2017), and subsequently to \$12.25 (effective July 1, 2018).²

A. All of the Many Parties (including the Companies), with Their Diverse Perspectives, Support the Customer Charge Proposed in the Stipulation

The Commission granted intervention to fourteen (14) separate parties in the two cases. On the issue of residential rate design, following the pre-filed written direct testimony submitted by witnesses for Kentucky Utilities and Louisville Gas & Electric Co. (jointly hereinafter “KU-LG&E” or “the Companies”),³ expert witnesses testifying on behalf of the Attorney General and Sierra Club also tendered pre-filed written direct testimony on the issue.⁴ The Attorney General’s and Sierra Club’s respective experts each independently determined that the KU-LG&E experts’ analysis and conclusions vis-à-vis residential cost of service, cost causation, and intra-class subsidization were erroneous, and that their recommendations to more than double the customer charge were thus unfounded as a

¹ The Stipulation was filed into the record of both cases on April 19, 2017.

² Stipulation § 4.3, p. 11.

³ See Direct Testimony of William Seelye (Managing Partner of the Prime Group, LLC) on behalf of KU-LG&E, at pp. 9-23 (Nov. 23, 2016); see also Direct Testimony of Robert M. Conroy (Vice President of State Regulation and Rates) at pp. 9-16 (Nov. 23, 2016) (invoking the Direct Testimony and cost of service study of Mr. Seelye in support the Companies’ initially proposed residential rate design).

⁴ See Direct Testimony of Glenn Watkins (President and Senior Economist with Technical Associates, Inc.) on behalf of the Attorney General, at pp. 50-67 (Mar. 3, 2017); Direct Testimony of Jonathan Wallach (Vice President of Resource Insight, Inc.) on behalf of Sierra Club, at pp. 4-16 (Mar. 3, 2017), in Case No. 2016-00371.

technical matter.⁵ These experts' conclusions that the Companies' customer charge proposal was inconsistent with principles of cost causation was accompanied by other, more policy-based reasons addressed in their testimony that additionally militate against raising the fixed charge. Furthermore, witnesses on behalf of MHC, CAC, ACM and Louisville Metro advocated from strongly-substantiated positions against the originally proposed increase in the residential customer charge for electric service, citing the adverse impact the proposal would have on the utility customers they represent.⁶ The records in these cases thus reflect and support the Joint Briefing Intervenors' unified and forceful opposition—from both technical and policy standpoints—to the originally-proposed increase in the residential customer charge for electric service.

Subsequently, all of the Joint Briefing Intervenors entered into negotiations with KU-LG&E, most of which were held over the course of three days, and involved multiple offers and counter-offers of proposed settlement regarding multiple issues, including rate design. The Commission should take careful note of the fact that the Joint Briefing Intervenors and the Companies, who have many separate and divergent interests among them, were nonetheless able to reach unanimous agreement on the Stipulation's terms regarding the residential customer charge for electric service.

⁵ KU-LG&E originally proposed to increase the residential customer charge for electric service to \$22.00 per month.

⁶ Also, as the Commission is aware, hundreds of Kentuckians further articulated opposition to an increased customer charge by submitting written comments or speaking at the public meetings in these dockets.

B. The Settlement's Proposed Customer Charge, while a Product of Fair Negotiation, Is Well Supported by the Record

The Stipulation's proposed two-step increase to the residential customer charge for electric service to \$11.50 and later to \$12.25, while resulting from the parties' broader settlement negotiations and fair compromises in these proceedings, is supported by substantial evidence. Several witnesses calculated what amount would reflect, as a technical matter, the true and properly defined minimum cost to connect and serve a residential customer; their figures ranged from amounts well *below* the Stipulation's proposed term—\$4.15 per month as calculated by the Attorney General's expert witness⁷ and \$8.01 per month as calculated by Sierra Club's expert witness⁸—to a \$23.93 per month figure offered by a KU-LG&E witness.⁹ Meanwhile, hundreds of passionate written and spoken comments from numerous KU-LG&E customers, filed into the records of both cases, urged the Commission to not grant any increase at all to the residential monthly charge.

The Stipulation's terms and conditions taken as a whole are fair, just and reasonable, as is the proposed residential rate design evaluated on its own. Moreover, the Stipulation's rates afford the Companies an opportunity to earn a fair rate of return, to fairly and adequately cover costs as a whole, provide customers proper pricing signals, and are based on a well-vetted record with testimony and discovery provided by experts in their respective roles and fields. The give-and-take between so many different parties with diverse positions crystalized into an outcome that, significantly, is both grounded in the record and positive for the Companies, the intervenors, and KU-LG&E consumers at large.

⁷ Direct Testimony of Glenn Watkins, Case No. 2016-00371, p. 60.

⁸ Direct Testimony of Jonathan Wallach, Case No. 2016-00371, p. 9.

⁹ Direct Testimony of Robert Conroy, Case No. 2016-00370, p. 10.

C. The Stipulation's Recommended Increase in the Residential Customer Charge Is Substantial and Needs No Modifications

With a combined request of over \$200 million dollars annually between these two cases, it can be difficult to retain a proper perspective on the significance of even the smallest changes in residential customer charges. For instance, the \$0.75 increase per year in the residential customer charge provides the Companies with an additional \$8 million each year of revenue that is neither dictated by, nor at risk due to, volumetric usage. Additionally, this sum would *double* with rates effective July 1, 2018. This represents a significant benefit to the Companies.

Moreover, the two-step increase is also substantial in relative terms. For instance, as compared to the current monthly residential charge, the stipulated increases represent a 7% increase with rates effective July 1, 2017, which doubles to a 14% increase with rates effective July 1, 2018. These amounts are *highly* noteworthy as compared to the overall increase to the residential class proposed in the Stipulation of 3.5% for KU customers and 6.7% for LG&E customers.

Furthermore, when the Stipulation's proposal regarding the residential customer charge is juxtaposed with residential customer charge levels over the last five years, the unmistakable conclusion is that the Commission need not modify the Stipulation's recommendation in any manner. Compared to the \$8.50 charge that was in effect prior to the conclusion of the rate cases in 2013, the increase from \$8.50 to the current \$10.75 alone represented an increase of 26%. But when compared to the increase proposed to take effect July 1, 2018, this represents a relative increase of 44% in the residential customer charge over a period of slightly more than five years. This means that in just over five years' time,

the Companies have increased the amount of revenues that are not subject to volumetric risk by more the \$40 million per year.

The Joint Briefing Intervenors were cognizant of these facts when they recommended no increase in the residential customer charge, as was the public when they turned out in droves to public meetings held by the Commission across the Commonwealth. Nevertheless, the increases as proposed in the Stipulation are fair, just and reasonable, and are (unlike the initial utility request) consistent with the principles of gradualism,¹⁰ rate stability and rate continuity,¹¹ while providing significant revenue to the Companies. In considering the above facts, any concern that the customer charge for residential customers is not keeping pace with the overall increases to revenue requirements is simply unfounded.¹²

D. Rate Design Considerations

Prior to reaching the agreement embodied in the Stipulation, the parties utilized various methodologies based in both policy and economics in order to calculate varying amounts of customer charges. In considering the Stipulation's unanimously agreed-on customer charge, the Commission should bear in mind that the parties' experts presented differing views as to what level of customer charge reflects "cost causation." As such, the stipulated position should not be viewed as a departure from the "proper" customer charge,

¹⁰ Final Order, Case No. 2012-00222, 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*, p. 12.

¹¹ James C. Bonbright, Albert L. Danielson & David R. Kamerschen, *Principles of Public Utility Rates*, p. 383 (Second Edition, 1988).

¹² Although the Commission occasionally increases customer charges in step with any volumetric or overall increase to revenue requirements, this is done almost exclusively in instances where there is no cost of service study and in Alternative Rate Filings. Those processes are normally devoid of detailed analysis or testimony and normally rely on Commission staff reports as justification for requests. Conversely, this record is complete with facts, analysis and testimony providing ample justification and evidence regarding rate design, and thus no consideration should be given to equal increases in customer and volumetric charges.

but rather as a negotiated agreement between positions supported by competing theories of cost causation.¹³

While one expert may believe a certain methodology to be more sound than others, another expert may reach the opposite conclusion. For example, the Companies relied in part upon principles set forth in NARUC's *Electric Utility Cost Allocation Manual* to develop their embedded cost of service study, which they in turn utilized to develop their proposed residential customer charge. However, Mr. Watkins relied in part upon a different NARUC publication, *Charging For Distribution Services: Issues in Rate Design*, to support his assertion that the customer charge should be based upon the marginal costs of adding and servicing customers.¹⁴ The fact that two experts reached contrasting conclusions while relying in part on different publications from the same authority tends to show that there is no single objectively correct and superior customer charge methodology. The Executive Summary in the report cited by Mr. Watkins is insightful in this regard:

Utilities and commissions should be cautious before adopting a particular method on the basis of what may be a superficial appeal. More important, however, is the concern that a costing method, once adopted, becomes the predominant and unchallenged determinant of rate design.¹⁵ (emphasis added)

Ultimately, the main point of contention between the Companies and the intervenors' experts who provided testimony regarding rate design is that the Companies maintain that costs for secondary transformers, poles, wires and some additional overhead

¹³ The Stipulation represents a compromise among the parties. As such, the degree to which each party may or may not have deviated from their respective testimony positions has no bearing on reasonableness.

¹⁴ Watkins direct testimony, Case No. 2016-00371, p. 40.

¹⁵ Watkins direct testimony, Case No. 2016-00371, pp. 41-42 (citing *Charging For Distribution Services: Issues in Rate Design*, p. 67).

should be included in the customer charge itself. More specifically, the Companies maintain that costs classified as customer-related for *revenue allocation* purposes must be classified as customer-related for purposes of *rate design*. However, the intervenors, and specifically the Attorney General's witness Mr. Watkins and the Sierra Club witness Mr. Wallach, maintain that instead, the customer charge should be based solely on the marginal cost of adding and servicing customers, which includes the cost of meters, meter-reading, billing, and customer service. This method, which Mr. Watkins advocates using, treated the costs of poles, wires, and transformers (which represent most of the delta between the methodologies) as demand-related.¹⁶ In fact, the NARUC cost allocation manual to which the Companies cite as support for the methodology they used to calculate the customer charge does not mention the usage of its allocations or classification for rate design purposes, but rather for purposes of cost of service calculations.

Rather, as Mr. Watkins pointed out in his direct testimony, the well-known treatise *Principles of Public Utility Rates* by Mr. James C. Bonbright states:

. . . if the hypothetical cost of a minimum-sized distribution system is properly excluded from the demand-related costs for the reason just given, while it is also denied a place among the customer costs for the reason stated previously, to which cost function does it then belong? The only defensible answer, in our opinion, is that it belongs to none of them. Instead, it should be recognized as a strictly unallocable portion of total costs. And this is the disposition that it would probably receive in an estimate of long-run marginal costs. But fully-distributed cost analysts dare not avail themselves of this solution, since they are the prisoners of their own assumption that "the sum of the parts equals the whole." They are therefore under impelling pressure to fudge their cost apportionments by using the category of customers costs as a dumping

¹⁶ Watkins direct testimony, Case No. 2016-00371, p. 60.

ground for costs that they cannot plausibly impute to any of their other cost categories.¹⁷ (emphasis added)

The inclusion of secondary transformers, poles and wires in the customer charge actually leads to small-volume customers (those that use less than the average monthly kWh) subsidizing large-volume users.¹⁸ This is contrary to the Companies' assertion that under the current customer charge, large-volume users are subsidizing small-volume customers.¹⁹

The Commission should avoid rigid adherence to a single methodology, as no one perfect methodology or conclusion exists. A rigid adherence would risk missing the trees for the forest, as all of these processes should serve only as a reference in the creation of rates. Nevertheless, both of these divergent viewpoints were provided and supported in the records of these cases. Although the parties in these cases disagreed on methodology and thus reached divergent initial recommendations for the customer charge—with the Attorney General's and Sierra Club's experts each determining that the current customer charge is already too high, as a technical matter, and the Companies' expert contending that it is too low—the Stipulation's more modest proposed two-step increase is nonetheless supported by substantial evidence in the record.

E. Rate Design of an Investor-Owned Electric Utility Cannot Be Compared to an Electric Distribution Cooperative nor a Gas Distribution Company

During the hearing on approval of the Stipulation, the Companies' expert witness, Mr. Seelye, was asked many questions by the Commission, Commission staff, and counsel

¹⁷ Bonbright, *supra*, p. 492.

¹⁸ Wallach direct testimony, Case No. 2016-00371, p. 10; Watkins direct testimony, Case No. 2016-00371, pp. 58-59.

¹⁹ Conroy Direct Testimony Case No. 2016-00371, p. 15.

for several intervenors concerning the rate design. One area of examination specifically related to whether residential rate design (i.e., the customer charge/volumetric charge) of an investor-owned utility (“IOU”) can be compared to an electric distribution cooperative or a gas distribution company. Mr. Seelye ultimately made clear, however, that there are many factors that differentiate an IOU from an electric distribution or gas distribution company, such that one cannot use that comparison as apples-to-apples evidence to establish what the customer charge should be for an IOU.

First, in looking at the difference between an IOU and an electric distribution cooperative, Mr. Seelye concluded by saying that one cannot compare them directly “because they have two different cost structures.”²⁰ Because cooperatives are in general much smaller and economies of scale differ, then according to Mr. Seelye, the cooperative would have higher overhead relative to the cost.²¹ Further, the cooperatives may not have the purchasing power that an IOU would have.²² Because the vertically integrated IOU is involved in the additional cost of producing energy while the distribution cooperative is not, the customer charge/volumetric charge ratio cannot be compared favorably.

In fact, the Commission has recently made it clear that comparing the distribution cooperative with an IOU cannot be performed in order to judge the fairness of the IOU’s customer charge:

The Commission concludes that, for an electric cooperative that is strictly a distribution utility, there is merit to the argument that there is a need for a means to guard against the revenue erosion that often occurs due to the decrease in sales volumes that accompanies poor regional economics, changes and weather patterns in the implementation or

²⁰ Seelye hearing testimony, May 9, 2017, transcript p. 160 at line 13.

²¹ *Id.*, p.160 at line 3.

²² *Id.*, p.160 at line 5.

expansion of demand-side management and energy-efficiency programs.²³

Likewise, according to Mr. Seelye, the analysis is the same for a gas distribution company. A gas distribution company does not produce the gas; it is merely a distribution company of the commodity like the electric distribution cooperative. Mr. Seelye also indicated that there are “greater infrastructure costs for the gas than there is for the electric.”²⁴ Additionally, gas usage over the past few years has dropped precipitously, but not electric use.²⁵ Therefore, use of a gas company’s customer charge/volumetric charge as a basis to establish the amount of a customer charge for electric IOU’s like LG&E and KU is flawed.

Thus, in determining the fairness of the customer charge for KU-LG&E, one should not compare a distribution cooperative nor a gas distribution company with an investor-owned electric utility that produces its own commodity (electricity). To the extent the Commission wishes to benchmark the proposed residential customer charge against that of another in-state utility, we note that the Stipulation’s proposed final customer charge of \$12.25 exceeds Duke Energy Kentucky’s \$4.50 customer charge, and Kentucky Power Company’s \$11.00 charge.²⁶

F. Fixed Costs Do Not Necessarily Require Recovery Through Fixed Charges

The Commission should have no qualms about whether KU-LG&E would be under-recovering customer-related “fixed” costs through the fixed customer charge proposed in the Stipulation.

²³ *In Re Farmers Electric Cooperative*, Case No. 2016-00365, Order dated May 12, 2017, p. 13.

²⁴ Seelye hearing testimony, May 9, 2017, transcript p. 131, lines 11-13.

²⁵ *Id.* at p. 133, lines 8-11, and p. 134 at lines 12-16.

²⁶ See Sierra Club Hearing Exhibits -1 and -2, respectively.

As a threshold matter, the premise espoused by some that fixed costs should be recovered through fixed charges is misguided as a matter of economics.²⁷ Regulation should serve as surrogate for competition to the furthest extent possible.²⁸ “As such,” Mr. Watkins explains, “pricing policy for a regulated public utility should mirror those of competitive firms to the greatest extent practical.”²⁹ As it is well-known that all costs are variable in the long run,³⁰ in competitive, efficient, pricing structures high levels of up front, or sunk, fixed costs are recovered volumetrically based on usage.³¹ 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, thus they are included in a zero-intercept study in the creation of a fully embedded cost of service study for the purposes of allocating revenues. These costs should not necessarily be reflected in the customer charge, especially under the incorrect argument that fixed costs must be collected through fixed charges.³²

As Mr. Watkins testified, in competitive markets prices are equal to marginal costs; “as such, under efficient pricing principles, marginal costs capture the variability of costs, and prices are variable because prices equal these costs.”³³ Regulation of utility monopolies is intended to act as a surrogate for competitive markets, and therefore, although many of the Companies’ short-run costs are fixed in nature, the prices they charge should be based

²⁷ See, e.g., Watkins direct testimony, Case No. 2016-00371, p.52.

²⁸ Bonbright, et al., *supra*, p. 141.

²⁹ Watkins direct testimony, Case No. 2016-00371, p. 52 (*citing* Bonbright, et al., *supra*, p. 141).

³⁰ *Id.*, p. 53.

³¹ Watkins direct testimony, Case No. 2016-00371, p. 53

³² The Companies have attempted to put forth that assumption since at least 2012, *see* Conroy direct testimony, Case No. 2012-00222, p. 48, and it was just as unsupported by rate-making principles then as it is now.

³³ Watkins direct testimony, Case No. 2016-00371, p. 53.

on long-run costs, which are variable in nature.³⁴ Not only does this pricing mechanism adhere to widely-recognized and long-held economic principles, but it also addresses fairness and equity, though on a secondary basis. 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.³⁵

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. For instance, “[m]ost manufacturing, agriculture, and transportation industries are comprised of cost structure predominated with “fixed” costs.”³⁶ Invariably, the Companies’ 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.³⁷ Rather, the Companies’ position regarding fixed cost recovery seems to be nothing more than attempt to reduce any risk they have regarding the variability of volumes between rate cases.

Of course, by recovering more revenue through the customer charge, the Companies are less concerned about the volume of the product they are in the business of providing: electricity. Increased customer charges reduce the Companies’ risk, which has already been

³⁴ *Id.* at 55.

³⁵ *Id.*

³⁶ *Id.* at 54.

³⁷ See Bonbright, *supra*, p. 491 (noting that the use of a zero-intercept method in determining certain customer-related costs to be included in the customer charge overlooks weak correlation between cost causation of factors and certain customer-related costs). Bonbright further notes that costs associated with the system envisioned by either the zero-intercept or other minimum-sized methods are unallocable and probably best reflected as long-run marginal costs, and thus best recovered volumetrically.

greatly mitigated through recovery of lost sales volumes from the DSM tariff (plus a return to shareholders), surcharges for fuel and environmental compliance costs, and the use of a fully-forecasted test year. As Mr. Watkins notes:

A pricing structure that is largely fixed, such that customers' effective prices do not properly vary with consumption, promotes the inefficient utilization of resources. Pricing structures that are weighted heavily on fixed charges are much more inferior from a conservation and efficiency standpoint than pricing structure that require consumers to incur more cost with additional consumption.³⁸

Rather than promoting rates that reduce the risk of the Companies, it is more appropriate to recover short-run fixed costs through variable rates, which has the effect of sending proper pricing signals to customers to conserve and utilize resources efficiently.³⁹ The proposed customer charge in the Stipulation strikes a reasonable balance between risk reduction for the Companies, and proper long-term price signals for customers, as discussed further in the following section.

G. Long-Standing Commission Policy Dictates that Rates Should Promote Conservation

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.”⁴⁰

In Case No. 2012-00222,⁴¹ LG&E requested an increase in the customer charge based solely on its cost of service.⁴² In its order in that case, the Commission noted that in reviewing that increase, it:

³⁸ Watkins direct testimony, Case No. 2016-371, p. 57.

³⁹ *Id.*, pp. 53-57.

⁴⁰ 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).

. . . is faced with a different argument, one raised by consumers whose e-mails, letters, and public hearing comments contend that a higher customer charge will disincentivize them to make energy efficiency expenditures. They argue that their bills will rise even though they reduce their energy usage.⁴³

The Commission then analyzed the impact of the proposed increase in the residential customer charge for electric service from the then-existing \$8.50 to the rate recommended in the stipulation to that case of \$10.75. In finding that the proposed increase would not disincentivize customers from using energy efficiency measures to reduce their bills, the Commission stated:

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 disincent energy efficiency.⁴⁴

The Joint Briefing Parties believe the Stipulation’s two-step increase in the residential customer charge for electric service will not disincentivize conservation and urge the Commission to approve the proposed increase without any modification. The record shows that a higher customer charge, such as that originally proposed by the Companies, would, in the words of Mr. Wallach, “dampen price signals and discourage economically efficiency conservation and investments in distributed generation by residential customers.”⁴⁵ Likewise, Mr. Watkins’ testimony observes that “a rate structure that is heavily based on a

⁴¹ *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.*

⁴² *Id.*, Final Order dated Dec. 20, 2012, p. 12.

⁴³ *Id.*, p. 13.

⁴⁴ *Id.*, pp. 14-15.

⁴⁵ Wallach Direct Testimony, Case No. 2016-0370, p. 11.

fixed monthly customer charge sends an even stronger price signal to consumers to use more energy.”⁴⁶ Mr. Watkins further noted:

one of the most important and effective tools that this, or any, regulatory Commission has to promote conservation is by developing rates that send proper pricing signals to conserve and utilize resources efficiently. A pricing structure that is largely fixed, such that customers’ effective prices do not properly vary with consumption, promotes the inefficient utilization of resources.⁴⁷

Additionally, Cathy Hinko, testifying on behalf of the MHC, observed that the Companies’ own demand-side management programs are premised on the notion that customers will tend to invest in energy efficiency to reduce their bills, but that a very high customer charge “surely would undercut the incentive since so much of the bill would be in an inelastic meter charge.”⁴⁸ Not only does an excessively high fixed charge, such as that originally proposed by the Companies, undermine future incentives for efficiency and distributed solar, it is also unfair to customers who have already invested in those resources, but who would now see a diminished return on their investment.⁴⁹

Mr. Wallach quantified the extent to which a lower energy charge, as a result of an increased customer charge, will dampen price signals for conservation. His analysis relies on a comprehensive review of the literature on the elasticity of residential customers’ demand in response to changes in electricity prices. He concluded that a 10 percent reduction in the energy price, which would have resulted from the Companies’ initial customer charge and revenue proposals, would result in a 3 percent increase in energy

⁴⁶ Watkins direct testimony, Case No. 2016-0370, p. 57.

⁴⁷ *Id.* p. 58.

⁴⁸ Direct Testimony of Cathy Hinko, on behalf of MHC, Case No. 2016-0371, at p. 20, lines 4-6.

⁴⁹ Hinko direct testimony, p. 19 (discussing a solar system installed on affordable housing and noting that “saving due to per Kwh lower cost would negatively impact to the amount of time to recover cost of installation and maintenance.”).

consumption over several years.⁵⁰ Such an increase in consumption would “undo about fifteen years of savings from the [Companies’] Residential Incentives [energy efficiency] program.”⁵¹

As such, the record in these cases demonstrates that a smaller increase in the customer charge than the Companies initially proposed is consistent with this Commission’s longstanding policy to “avoid taking actions that might disincent energy efficiency.” The agreed-upon \$1.50 increase in the customer charge over two years will largely preserve the energy efficiency incentives in the Companies’ current residential rate structure and is therefore just and reasonable.

The agreed-upon increase in the customer charge will also preserve a greater degree of customer control over their electric bills, in contrast to a bill that is made up in significant part of a fixed charge that customers cannot avoid no matter what investments or behavioral changes they may make to reduce their usage.⁵² 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.⁵³

In sum, the negotiated customer charge for residential electric service is not only consistent with record evidence regarding the cost properly included in the customer charge, but also comports with public policies in favor of incentivizing conservation.

⁵⁰ Wallach direct testimony, Case No. 2016-0370, pp. 14-15.

⁵¹ *Id.*, p. 15, lines 10-16.

⁵² See Direct Testimony of Malcolm Ratchford, filed on behalf of CAC, Case No. 2016-0370, p. 13, lines 3-6 (“ . . . because the basic service charge is a flat-rate charge for all customers not based upon usage, a smaller percentage of the bill can be controlled by energy usage and conservation. Customers have less incentive to conserve to lower their bills.”).

⁵³ *Id.*

H. The Proposed Customer Charge Preserves Rate Affordability for Low-Income Customers

Affordability of electric service for vulnerable customers is another important consideration for the Commission in determining whether the proposed residential customer charge is fair, just and reasonable. At current rates, many low-income customers struggle to afford utilities as evidenced by a higher demand for assistance than assistance agencies can meet⁵⁴ and high disconnection rates in high poverty areas.⁵⁵ Organizations that specifically advocate for low-income customers—MHC, ACM, and CAC — unanimously opposed the Companies’ original customer charge increase, which they asserted would harm their constituencies by raising bills for low-usage customers disproportionately.⁵⁶ In addition, Louisville/Jefferson County Metro Government filed testimony by City Councilmen Kevin Kramer and Bill Hollander, who both expressed concern about the disproportionate impact of a large customer charge increase on vulnerable, low-income residents.⁵⁷

In evaluating the impact of customer service charges on low-income customers, it is important to recognize that these customers are a diverse population with a variety of characteristics that affect their utility usage rates. Income levels, family and household sizes vary.⁵⁸ Some low-income customers are disabled or elderly living on fixed incomes, some are among the working poor.⁵⁹ Some of these customers are able to access third party

⁵⁴ Ratchford Direct Testimony, Case No. 2016 -00370 at 13 -14; Cummings Direct Testimony, Case No. 2016-00371 at 6.

⁵⁵ Cummings Direct Testimony, Case No. 2016-00371 at 12 – 14.

⁵⁶ See Hinko Direct Testimony, Case No. 2016-0371; Ratchford Direct Testimony, Case No. 2016-0370, Direct Testimony of Marlon Cummings on Behalf of Association of Community Ministries, Case No. 2016-0371.

⁵⁷ See Direct Testimony of Kevin Kramer on behalf of Louisville/Jefferson County Metro Government, Case No. 2016-0371; Direct Testimony of Bill Hollander on behalf of Louisville/Jefferson County Metro Government, Case No. 2016-0371.

⁵⁸ Cummings Direct Testimony, Case No. 2016-00371 at 6 - 7.

⁵⁹ Cummings Direct Testimony, Case No. 2016-00371 at 6 - 7.

financial assistance when bills get too high and some are not.⁶⁰ Housing characteristics, such as single or multifamily, the size, age, condition and level of weatherization also play a role. All of these factors can affect whether a low-income customer has higher or lower than average usage.

Some data in the record shows varying levels of higher than average usage among some segments of the low-income population.⁶¹ However, the record also includes data showing that customers in areas with the highest poverty rates in Jefferson County, the largest county in the LG&E territory, had lower than average usage in 2015 and 2016.⁶²

Regardless of whether a low-income customer has higher or lower than average usage, the customer will benefit more from the proposed two-step increase in the residential customer charge, as opposed to a higher increase, as it allows for a greater percentage of the bill to be capable of reduction through conservation measures. Both witnesses for CAC and ACM, agencies which have significant experience in assisting utility customers in need, emphasized the importance of their clients' having the ability to reduce utility costs by lowering usage.⁶³ Further, the stipulated increase will support the efforts of the Companies,

⁶⁰ Ratchford Direct Testimony, Case No. 2016 -00370 at 13 -14; Cummings Direct Testimony, Case No. 2016-00371 at 6.

⁶¹ Case No 2016 00371, Attachment to LG&E Response to First Request for Information of ACM No 3 (a); Case No. 2016-00370, Attachments to CAC Response to KU DR 1, and KU Response to CAC Initial Request for Information No. 8.

⁶² See Cummings Direct Testimony, Case No. 2016-00371 at 8 -9, for the ten Jefferson County Zip Codes with the highest individual poverty rates; also in Case No. 2016 – 00371 see LG&E Response to ACM First Request for Information No. 4(a) which shows the average Use kWh per Residential Electric Customer Accounts. In 2015, the average usages in these ten zip codes ranged from 709 kWh to 896 kWh; in 2016, the average usages in these ten zip codes ranged from 672 kWh to 902 kWh; all of these usages are lower than the residential average usage of 957kWh in the LG&E territory used by LG&E Witness Robert Conroy as a point of comparison in his Rebuttal Testimony at 15 (Case No. 2016-00371).

⁶³ Ratchford Direct Testimony at 13; Cummings Direct Testimony at 9.

CAC and ACM to promote energy efficiency, weatherization and awareness of energy efficiency opportunities among low-income constituents.⁶⁴

Thus, the proposed \$1.50 increase in the customer charge contained in the Stipulation is not only reasonable in light of record evidence on cost causation and conservation incentives, but also because it mitigates disproportionate increases in electric bills for those customers who conserve electricity in an effort to keep their bills within their household's limited means.

CONCLUSION

WHEREFORE, as the Joint Briefing Intervenors believe the stipulated residential electric customer charge is supported by substantial evidence, and is fair, just and reasonable, they urge the Commission to approve the residential electric customer charge as set forth in the Stipulation.

Respectfully submitted,

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⁶⁴ Direct Testimony of Robert M. Conroy, Case No. 2016-00371 at 60 – 62; Cummings Direct Testimony, Case No. 2016-00371 at 4 – 5; Ratchford Direct Testimony, Case No. 2016-00370 at 5 – 6.

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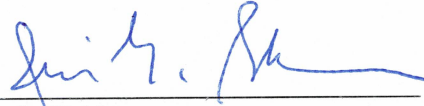
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Certificate of Service and Filing

Counsel certifies that the foregoing is a true and accurate copy of the same document being filed in paper medium with the Commission within two business days; that the electronic filing has been transmitted to the Commission on May 31, 2017; that there are currently no parties that the Commission has excused from participation by electronic means in this proceeding.



Assistant Attorney General

This 31st day of May, 2017.