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Austin Energy Cost of Service and Rate Review

December 15, 2015

Current Schedule Highlights

- December 14, 2015—Electric Utility Commission briefing on Revenue Requirement and Cost of Service
- December 15, 2015—City Council Work Session briefing
- January 11, 2016—Special called EUC meeting (tentative)
- January 25, 2016—EUC briefing on rate design recommendations
- January 28, 2016—Utility Oversight Committee briefing on rate design recommendations
- End January, 2016—Begin proceedings before Impartial Hearings Examiner
- April 22, 2016—Impartial Hearings Examiner recommendations report released
- April & May 2016—hold three Council Work Sessions
- June 2016—hold two Council public hearings
- June 23, 2016—final Council decision meeting

Steps in Cost of Service and Rate Setting

- Revenue Requirement
- Cost Allocation
- Rate Design

Austin Energy's Objectives

- Transparent process
- Fairness for all customers
- Focus on affordability
- Adhere to applicable State and local laws and policies
- Sustain long-term financial health of the utility

Guiding Policies and Principles

- Affordability Goals:
  - 2 percent per year
  - Competitiveness
- Austin Energy Strategic Plan
- City of Austin Climate Protection Plan (2007) and Austin Energy Resource Generation Plan to 2025
- Financial Policies of the City of Austin and 2012 Rate Ordinance

Austin Energy's Evolving Financial Challenge: Restoring Financial Health

- 2012 Rate Review: first Cost of Service study in 17 years
  - Declining reserves
  - Imbalances among customer classes
  - Rate structure not aligned with strategic posture of Austin Energy
- Settlement of appeal to Public Utility Commission:
  - $66 million annual rate increase
  - Sustained realignment of rates and programs
- Significant progress in restoring financial health of Austin Energy

Austin Energy's Evolving Financial Challenge: " the Business Model"

- Changes in our community:
  - Urbanization
  - Share of multi-family properties
- Changes in the electric industry:
  - Distributed generation/solar expansion
  - Energy efficiency
  - Building codes
  - Load management
  - Emergence of electric vehicles
- Community goals:
  - 30 years of energy efficiency leadership
  - Austin Climate Protection Plan
  - Austin Energy Resource Generation Plan to 2025

Austin Energy's Evolving Financial Challenge: Long-run Revenue Stability

"Our public is on a path to use less energy, but demand for public infrastructure to deliver reliable service and support modernized systems is unabated."

- Average residential customer usage is declining over time
- Customer growth continues
- Need for infrastructure remains strong

How do we fund the infrastructure?

Austin Energy's Evolving Financial Challenge: Long-run Revenue Stability

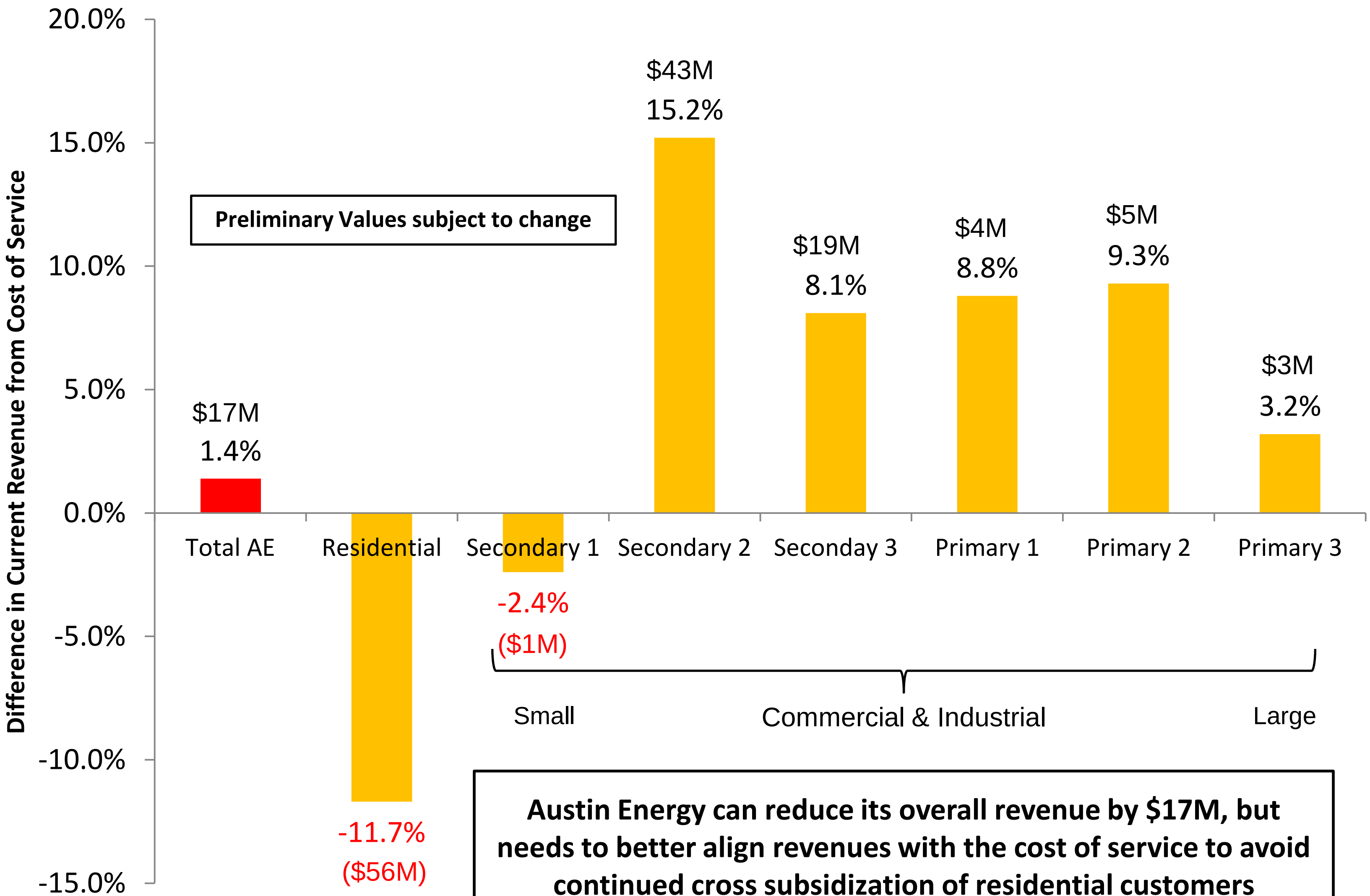
- Residential infrastructure cost recovery is on an unsustainable path
  - Infrastructure costs are "fixed costs"
  - Residential rate design (tiered structure with low fixed charges) depends on hot weather and high residential energy users to recover infrastructure costs
    - Inconsistent with community goals and the business model evolution
  - Insufficient recovery of fixed costs is unsustainable
- Commercial infrastructure cost recovery at risk in future:
  - Demand charges more successful at recovering fixed costs
  - Electric industry transformation may create greater future risks (e.g., building codes, energy efficiency and distributed generation)

Cost of Service:
Preliminary Conclusions

Cost of Service Summary

- Base Revenue Requirements reduction of approximately $17 million (2.7 percent of base revenue)
  - Equal to approximately 1.4 percent of total revenue
  - Additional reductions in Regulatory Charge and Power Supply Adjustment anticipated
- Commercial and industrial rates above competitiveness goal
  - Reductions for second year in a row will help restore competitiveness
- Customer class allocation imbalances improved, but continue:
  - Progress since 2009 in aligning revenues with Cost of Service
  - Commercial and industrial customers continue to subsidize the residential class

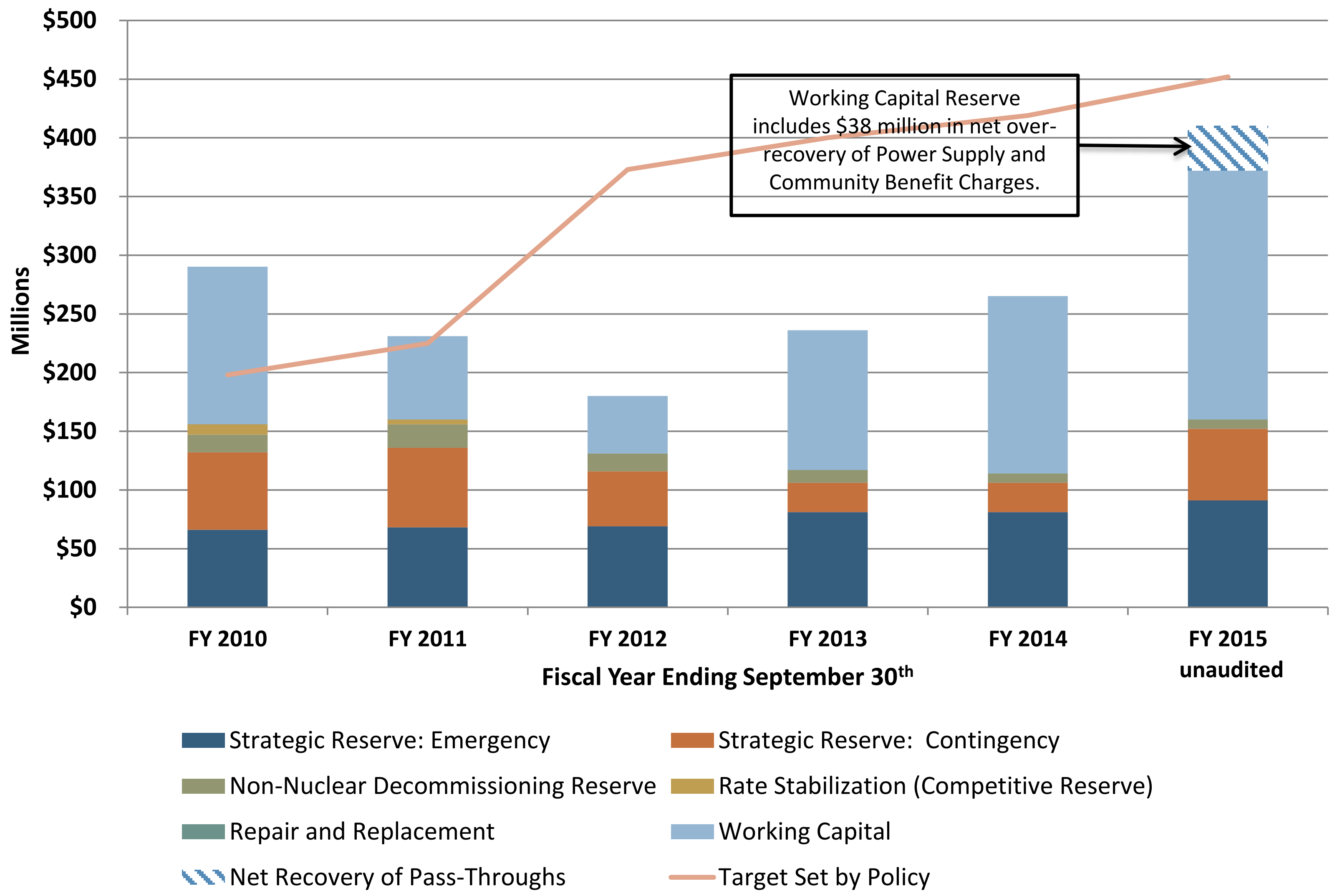
Revenues are Not Aligned with Cost of Service



Austin Energy can reduce its overall revenue by $17M, but needs to better align revenues with the cost of service to avoid continued cross subsidization of residential customers

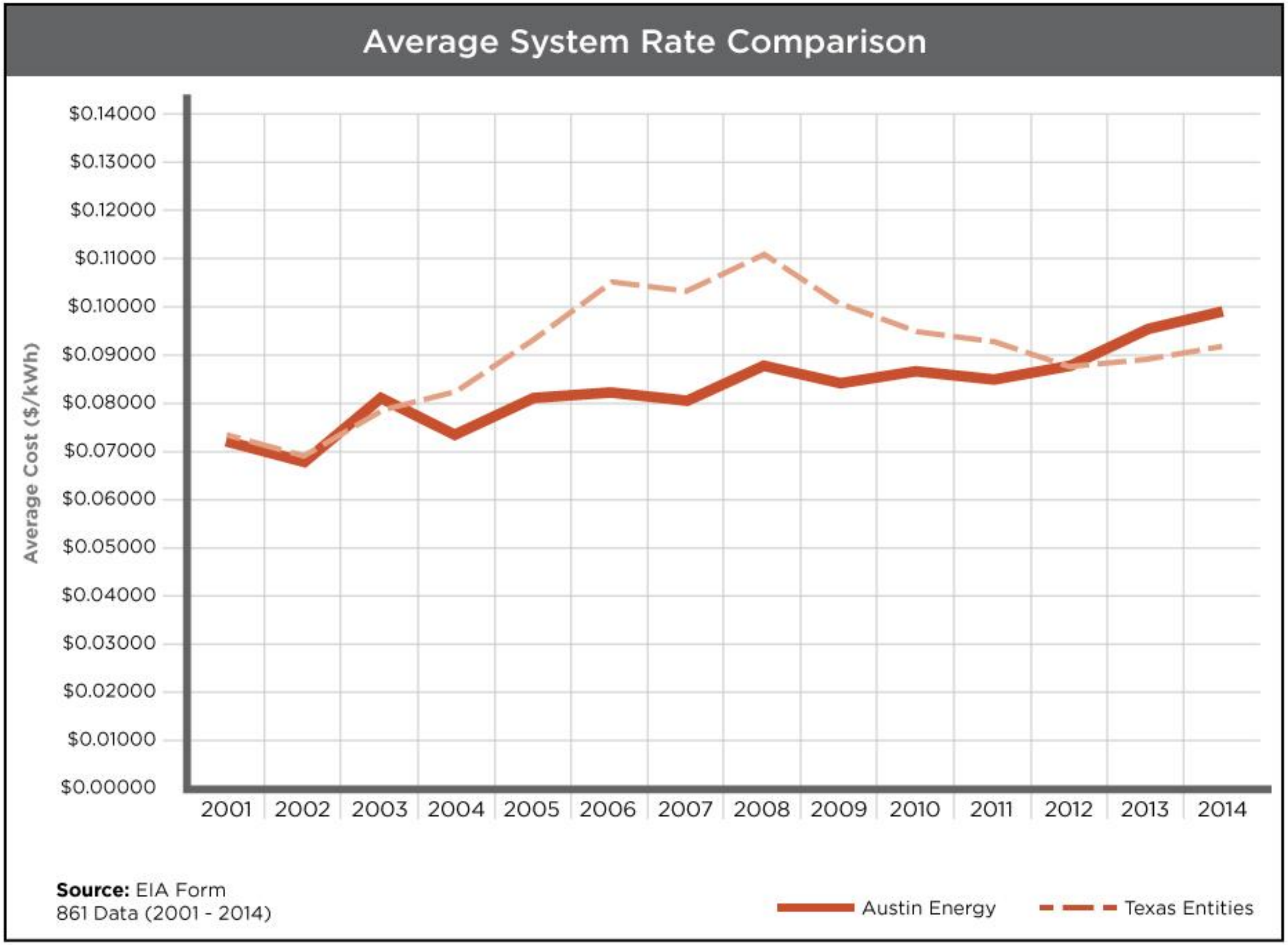
Current Financial Picture

Cash and Reserves Improving

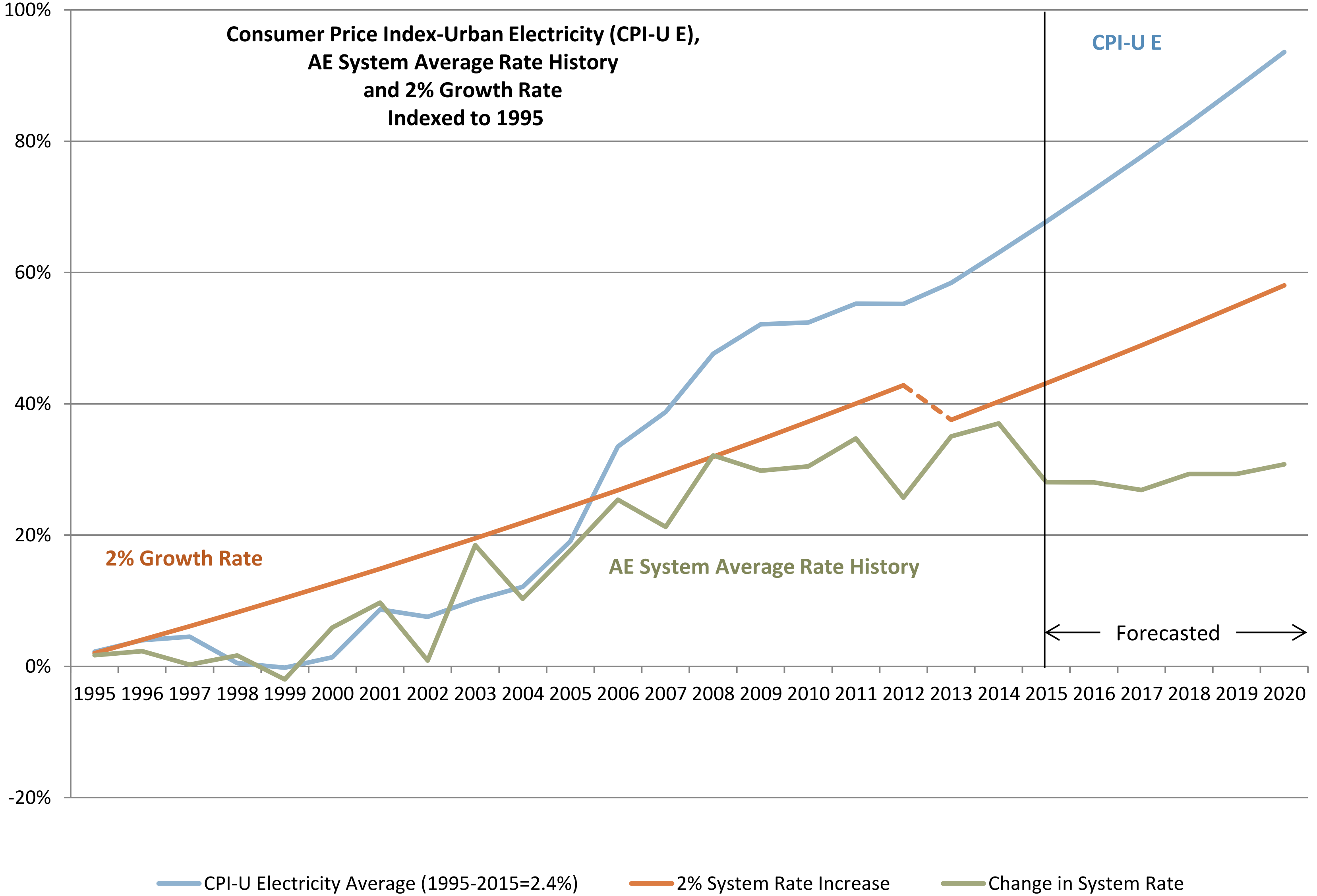


Competitiveness

Rates Fail to Meet Competitiveness Goal



Compliance with Annual Affordability Metric



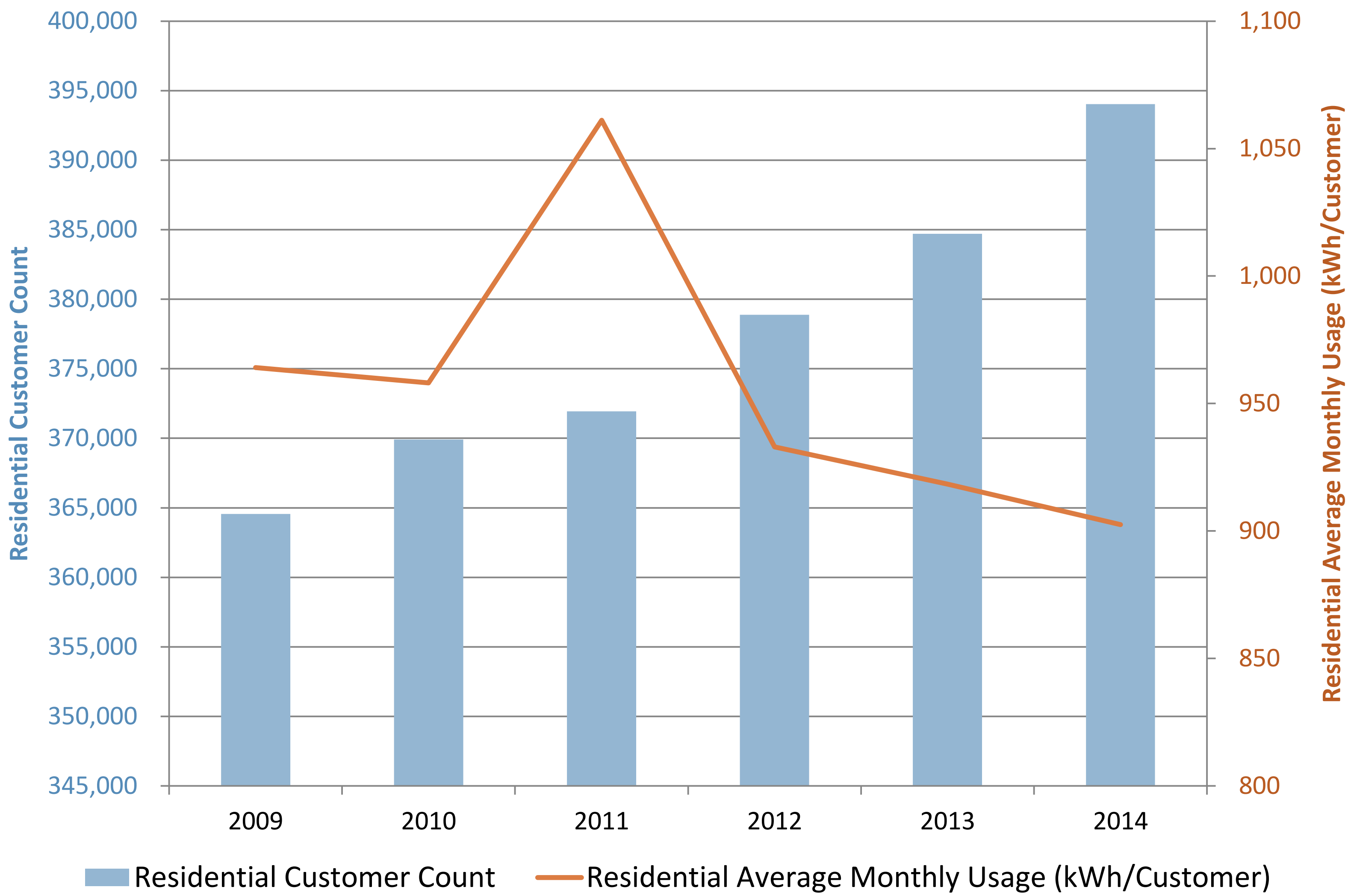
Cost of Service Results

Progress in Aligning with Cost of Service

	Test Year 2009 (As Approved by Council)		Test Year 2014 (Preliminary values subject to change)	
	Revenue Excess (Deficiency)	Change needed to meet Cost of Service	Revenue Excess (Deficiency)	Over/ (Under) Cost of Service
Residential	($78.0)	-20.6%	($55.6)	-11.7%
SEC 1	($9.5)	-25.9%	($0.8)	-2.4%
SEC 2 / SEC 3 (Combined for comparative purposes)	($8.4)	-1.9%	$62.0	11.9%
PRIM 1	$0.9	2.8%	$4.1	8.8%
PRIM 2	($5.3)	-11.2%	$4.8	9.3%
PRIM 3 & 4	($5.3)	-9.3%	$2.8	3.2%
All others	$0.3	1.8%	($0.6)	-3.0%
AE System	**($105.4)**	**-10.3%**	**$16.8**	**1.4%**

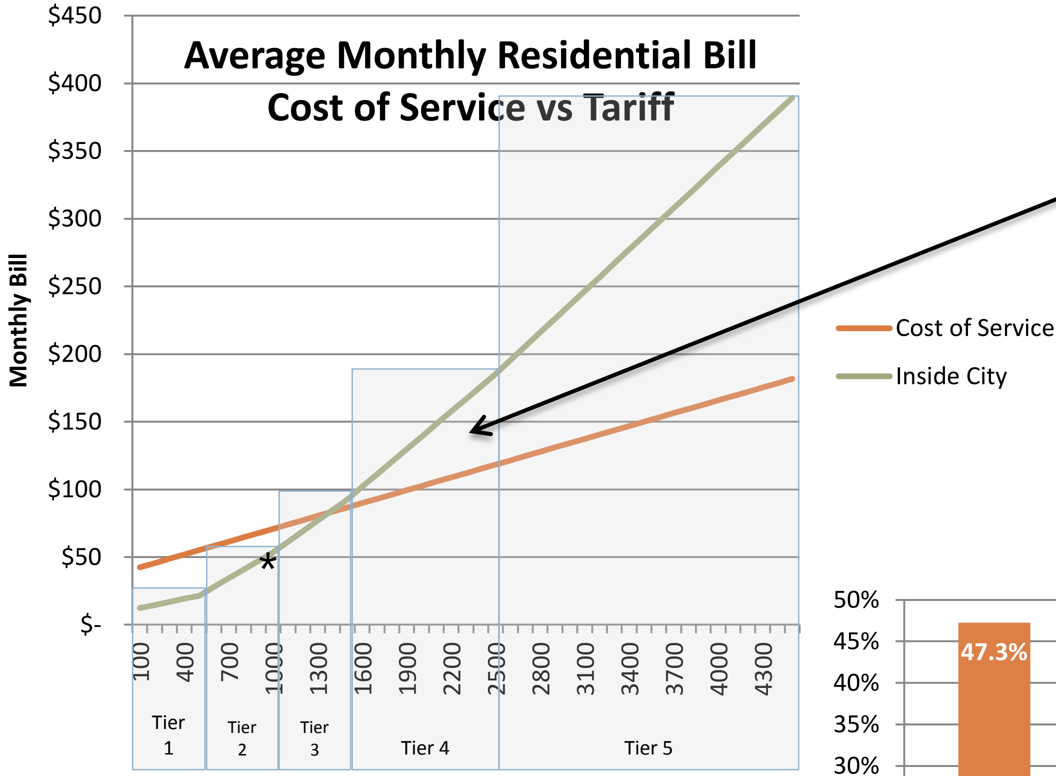
Revenue Sustainability Challenge

While Residential Customer Count Steadily Increasing, Average Residential Use Declining

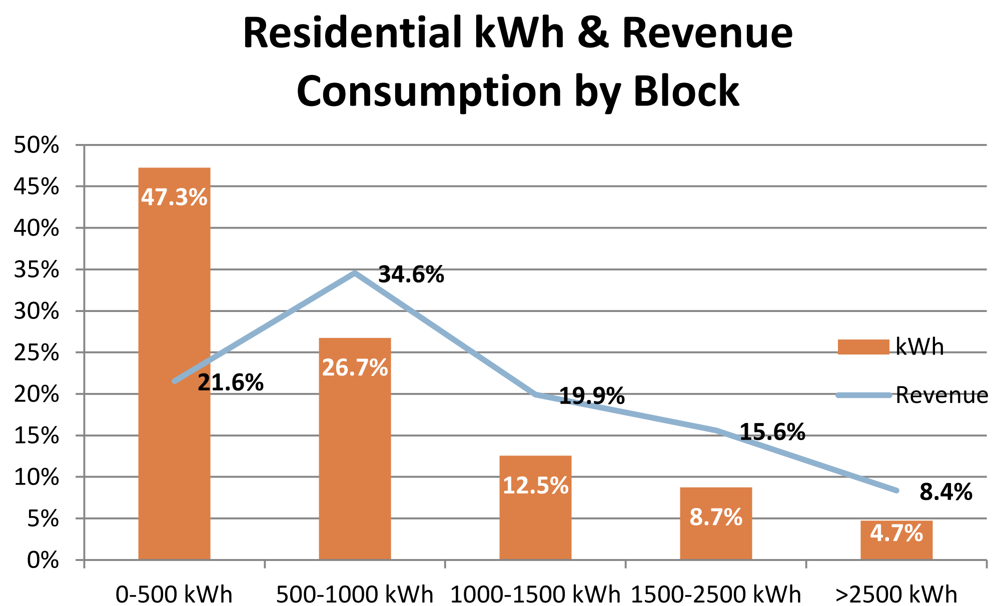


Source: EIA 861 data reported on a calendar year basis for 2009 through 2014.

Nearly 80 Percent of Residential Electricity is Sold Below the Cost of Service



Residential rates do not meet the cost of service until 1,400 kWh. In fiscal year 2014, the average residential customer used 919 kWh* per month.



Only 13 percent of residential electricity is delivered in the 4th and 5th tiers but contribute 24 percent of revenue

Note: Annual consumption of 903 kWh as reported by EIA is based on 2014 calendar year while the 919 kWh is based on City of Austin's fiscal year 2014.

Next Steps

- Rate Design Recommendations: brief EUC and Utility Oversight Committee of Council in January
- Cost of Service and Rates Report: released mid-January
- EUC input sessions for public comment (to be scheduled)
- Formal review process begins: end January