AUSTIN ENERGY'S	**§**	**BEFORE THE CITY OF AUSTIN**
	§	
2022 BASE RATE REVIEW	**§**	**IMPARTIAL HEARING EXAMINER**

AUSTIN ENERGY'S RESPONSE TO THE IMPARTIAL HEARING EXAMINER'S FINAL RECOMMENDATION

September 26, 2022

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AUSTIN ENERGY'S RESPONSE TO THE IMPARTIAL HEARING EXAMINER'S FINAL RECOMMENDATION

Executive Summary

- The IHE's Recommendation issued on September 9, 2022 agreed with Austin Energy's proposals on all major issues except for residential rate design. The IHE's Recommendation was based on a thorough and unbiased review of all participants' positions and the record evidence, and confirms that AE's proposed base rate increase is warranted and necessary, and that AE has met its burden of proof in seeking an increased revenue requirement and revised base rate design.

- Although AE agrees with and supports the majority of the IHE's Recommendation, AE respectfully requests City Council reject the IHE's position on the following five issues:
    1. General Fund Transfer
    2. Distribution-Demand-Related Costs
    3. Primary Distribution Demand-Related Costs
    4. Energy and Demand Line Loss Factors
    5. Residential Rate Design (including the Customer Charge, Tier Structure, and Outside-City Customer Rate Differential)

- AE calculated the General Fund Transfer in accordance with its financial policies, and its proposal of $120 million should be adopted.

- AE's proposal to allocate distribution load dispatch expense to customer classes based on 12 Non-Coincident Peak (NCP) demand is consistent with how AE allocates other costs in this proceeding and should be adopted.

- TIEC and NXP's proposals to create a separate substation rate for "Primary Substation customers" should be rejected. Primary voltage customers should be allocated costs for the primary distribution poles and lines that are part of these feeders. However, AE would be open to exploring options that include allowing the "Primary Substation customers" to purchase existing substation equipment and instead take service at transmission level.

- AE's System Loss Study for FY 2018 (Line Loss Study) should be adopted, although AE is willing to commit to conducting a new Line Loss Study before its next base rate case.

- AE's proposed residential rate design should be adopted. AE's proposal is fair, reasonable, required, and necessary for its financial stability.

    - Currently, the majority of in-city residential customers are billed on a five-tier inclining structure. The 40% of residential customers whose bills fall entirely with the first and second tiers are priced well below cost. The stark reality is that there are simply not enough residential customers with consumption in the higher tiers to make up the revenue deficit from the lower tiers. This is exacerbated by the fact that high-use

customers are gradually retiring from the system, and new growth in sales is occurring primarily in the lower tiers. The current tier structure is simply unsustainable.

- Current base rates and structures do not support the long-run financial strength and stability of the utility, and AE's proposed changes to the residential base rate design are needed to support the continued viability of AE to meet current and future obligations. The IHE agreed: *"AE has established that, under the current structure, it is not collecting sufficient revenue from the residential class to ensure its financial stability."*

- AE's proposal for a new residential base rate structure is designed to capture the changing composition of the residential customer class, relying more heavily on cost recovery in the initial, lower consumption, tiers. However, the proposed redesign only moves classes 50 percent to unity.

- AE proposes to modify the residential base rate structure by reducing the number of tiers and flattening the steepness of the rate increases between each tier. Under AE's proposal, the number of tiers is reduced from five to three, and the tier breakpoints are adjusted downward. This is designed to match the shift in the bill frequency distribution toward lower levels of consumption. AE's proposed rate design preserves the price signals sent to customers, as high use customers who use more energy will continue to have higher bills.

- AE's proposal increases the customer charge from $10 to $25 to reflect fixed customer costs that do not vary with consumption. Matching the customer charge to the customer unit costs will result in customer charge revenues directly tracking the underlying cost driver—the number of customers. Despite the increase in the customer charge, its proposed customer charge is still less than the total combined customer and delivery costs suggested by the COS Study. Further, AE's CAP waives the customer charge for CAP participants, magnifying the effect of this exemption for CAP customers.

- The IHE found that *"the rate design changes sought by AE are well-articulated and consistent with certain City and ratemaking policies and principles;"* and *"one way or another AE must recover its revenue requirement through its rates."*

- AE's proposed base rate increase of $35.7 million strikes an appropriate balance among the objectives of ensuring the long-term financial stability of the City-owned utility, achieving the Council's goals for affordability, encouraging the efficient use of energy, and charging each customer class its appropriate cost of service. AE's proposal aims to bring customers closer to what it costs to serve them, establishing more equitable charges as the community continues to grow and consumption patterns change. The IHE found: *"AE's concerns of financial stability are well founded, regardless of whether AE implements its proposed customer charge or adopts a more sharply tiered rate structure."*

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AUSTIN ENERGY'S RESPONSE TO THE IMPARTIAL HEARING EXAMINER'S FINAL RECOMMENDATION

TO THE AUSTIN CITY COUNCIL:

Austin Energy (AE) files this Response (Exceptions) to the Impartial Hearing Examiner's (IHE) Final Recommendation (Recommendation) issued September 9, 2022 in the above referenced proceeding, pursuant to Base Rate Review Procedural Guideline section H1(b) and the 2022 Base Rate Review Procedural Schedule.

I. INTRODUCTION

AE commends the IHE on a well-developed, 146-page Recommendation that comprehensively sets out the issues in this proceeding in a clear and cohesive manner. AE agrees with the majority of the IHE's recommendations, and on such topics where it does not agree, such as residential rate design, AE believes that continuing to follow the established process, in conjunction with the public hearings scheduled by the City Council, can lead to the desired result of setting rates for the Greater Austin community that will be in all customers' interest.

AE proposes a $35.7 million base rate increase that strikes an appropriate balance among the objectives of ensuring the long-term financial stability of the City-owned utility, achieving the Council's goals for affordability, encouraging the efficient use of energy, and charging each customer class its appropriate cost of service. AE also proposes revisions to its outdated residential rate design to stabilize revenues and more equitably recover its costs by relying less on energy sales. Overall, AE's proposal aims to bring customers closer to what it costs to serve them,

establishing more equitable charges as the community continues to grow and consumption patterns change.

The IHE's Recommendation was based on a thorough and unbiased review of all participants' positions and the record evidence. It confirms that AE's proposed base rate increase is warranted and necessary, and that AE has met its burden of proof in seeking an increased revenue requirement and revised base rate design. In particular, the IHE's Recommendation substantiates AE's revenue requirements by recommending adoption of AE's position on all but one revenue category. The IHE also recommends approval of AE's cost allocation methods and its new approach to the Value of Solar (VoS) tariff.

Although the IHE raised some questions about AE's proposed residential rate design, he did not propose a specific alternative. Instead, he recommended it be "revisited by AE and the participants."[1] Despite his stated concerns regarding rate shock and affordability, the IHE also said that "[t]he rate design changes sought by AE are well-articulated and consistent with certain City and ratemaking policies and principles."[2] In addition, the IHE noted that "if City Council prefers a rate design focused on cost causation, it would be appropriate to approve AE's proposed rate design."[3] Most significantly, the IHE made it clear that "one way or another AE must recover its revenue requirement through its rates."[4]

AE's proposed residential rate design changes are supported by the principles of cost causation, conservation, affordability, and gradualism. Although AE agrees with and supports the majority of the IHE's Recommendation, AE respectfully requests City Council reject the IHE's

[1] Impartial Hearing Examiner's Final Recommendation at 7 (Sept. 9, 2022) (IHE Recommendation).

[2] *Id.* at 1.

[3] *Id.* at 4.

[4] *Id.* at 6.

position on the following five issues: (1) General Fund Transfer, (2) Distribution-Demand-Related Costs, (3) Primary Distribution Demand-Related Costs, (4) Energy and Demand Line Loss Factors, and most importantly (5) Residential Rate Design—including the Customer Charge, Tier Structure, and Outside-City Customer Rate Differential. Finally, this pleading offers clarification or corrections on several other issues discussed below.

II. REVENUE REQUIREMENT

A. General Fund Transfer

AE proposes a General Fund Transfer (GFT) in the amount of $120 million for purposes of calculating its revenue requirement. This amount is based upon a known and measurable adjustment to the test-year GFT to align it with proposed base rates that, if approved, are expected to be in effect for several years or more. The IHE recommended that the GFT be set based on the test-year GFT of $114 million or, at most, the $115 million estimate that AE used only for Fiscal Year (FY) 2023.[5]

As described in AE's Closing Brief, Council's Financial Policy Nos. 12, 13, and 17 prescribe how the GFT is determined.[6] Per Financial Policy No. 13, the GFT is based on 12% of AE's three-year average base revenues using the current year estimate and the previous two years' actual revenues and exclude power supply and district cooling revenues. Despite this requirement from the Council's Financial Policies, the IHE recommends that the GFT be calculated in accordance with AE's financial policies *using known data*.[7] Adopting this recommendation would, however, fail to include all GFT payments made in accordance with the Financial Policies as described below.

[5] IHE Recommendation at 28.

[6] Austin Energy's Closing Brief at 20 (Aug. 9, 2022).

[7] IHE Recommendation at 28 (emphasis added).

The proposed FY 2023 budgeted GFT of $115 million is based on 12% of a three-year average of actual base revenues for FY 2021 and 2020 and estimated revenues for FY 2022. The revenues for those years utilize existing base rates and not the proposed base rates, which would not be in effect until FY 2023. As shown on Work Paper C-3.2.1 of the Rate Filing Package (RFP), the GFT amount of $121 million included in the Base Rate Filing Package is based on 12% of operating revenues, minus revenues from the PSA and non-electric business (rounded to the nearest $1 million). However, rather than take a three-year average (two actual and one estimate) of revenue, as is done when establishing the GFT annually, the amount of the GFT in the base rate review relied on the amount of revenue that is estimated from the test year only in order to align the amount of the GFT with the base rates proposed. Because the GFT will be recovered in base rates that may be in place for potentially five years or more, it is important that the amount of the GFT to be paid during the time the proposed rates are in effect is properly calculated. The budget process is separate from the rate setting process. The budgeted GFT is calculated pursuant to financial policies and should not be used as a basis for approving a GFT for purposes of ratemaking. The $120 million GFT is the amount AE would expect to pay over the time the proposed base rates are in effect. Failure to align the GFT with base rates will result in AE under-recovering this cost.

Regardless of the GFT amount, the IHE separately recommended that the GFT be collected from all customers, which is appropriate. Although many outside-city customers benefit from services resulting from the GFT, the obligation to pay GFT is not contingent upon the customer receiving a benefit, per Texas Government Code § 1502.059 and basic ratemaking principles. Further, Texas Government Code § 1502.059 does not distinguish between inside-and outside-city customers.

B. Present Revenues and Billing Determinants

The IHE raised questions regarding the effect of Winter Storm Uri on present sales and billing determinants. Specifically, instead of adopting the recommendations of Texas Industrial Energy Consumers (TIEC), the IHE asked that AE better explain how Winter Storm Uri had no impact on test year energy sales and base revenues. At the same time, the IHE acknowledged that "AE's claim that Winter Storm Uri had no impact may be correct."[8]

As explained in its Base Rate Filing Package, AE used FY 2021 as the historical test year in preparing its cost of service in this matter, including sales and base revenues. Winter Storm Uri occurred in February 2021, and although the storm was extreme in nature, its impact on AE's test year energy sales and base revenues was not. The IHE's speculation is based on TIEC's false premise that AE overstated its test-year base revenue deficiency by failing to account for URI and that AE's projected revenue deficiency is therefore overstated. This is simply incorrect. AE stated in its Closing Brief and in certain Request for Information (RFI) responses that Winter Storm Uri had little to no impact on 2021 sales and base revenues. In response to the IHE's request, AE provides more context below.

Looking at actual data, the presumption that Uri must have caused a reduction is usage for the test year is not validated. The table below shows energy sales for February and March—the billing periods impacted by Winter Storm Uri. The table compares budgeted kWh sales, normalized test year sales, and actual FY 2021 sales.

Month	**2021 Budgeted Energy Sales (GWh)**	**Weather Normalized Energy Sales (COS)**	**Actual Energy Sales (2021)**
February	908.8	920.4	927.8
March	891.8	884.7	924.3

[8] IHE Recommendation at 49.

This table shows that actual kWh sales for the two months actually exceeded the anticipated (budgeted) and test year normalized energy sales. Objectively, the Winter Storm Uri weather had no negative impact on sales. This is completely contrary to the assumption that Winter Storm Uri caused test year billing determinants to be understated.

In addition to the above analysis, AE compared the weather-normalized, customer-adjusted test year GWh sales with the most recent historical rolling 12 months ending July 2022. The rolling 12-month period was weather normalized and customer adjusted using the same premise count as in the test year, creating an apples-to-apples comparison. The data is shown below.

Rolling 12 months ended July 2022	13,511.966 GWh
Test Year	13,352.049 GWh
Difference	159.917 GWh
Percent change	1.2%

This data compares the test year weather-normalized sales, which included Winter Storm Uri, with the most recent 12 months of sales, which did not include Uri. The fact that the data shows relatively flat sales and an immaterial difference between the two periods speaks to the fact that AE's treatment of Winter Storm Uri in the test year was reasonable, and that whatever impact COVID-19 may or may not have had on the test year has not meaningfully changed since the end of the test year.

Based on this analysis, it is clear that the outages resulting from Winter Storm Uri did not depress test-year kWh sales and base revenues, so AE did not adjust test-year sales for the relatively short event. AE again reinforces that although Winter Storm Uri had huge impacts on the health and wellbeing of citizens across the state, from a financial viewpoint, it did not impact test-year sales, revenues, and billing determinants. Therefore, AE requests that its test-year sales, revenues, and billing determinants be adopted.

III. COST ALLOCATION

A. Distribution-Demand-Related Costs: Load Dispatch Expense

In its Base Rate Filing Package, AE proposes to allocate distribution load dispatch expense to customer classes based on 12 Non-Coincident Peak (NCP) demand. This is consistent with how AE allocates other costs in this proceeding. However, the IHE instead recommends adoption of the Independent Consumer Advocate's (ICA) proposal to allocate the expense on the basis of average demand.[9] In support of its recommendation, the ICA cites precedent from the Public Utility Commission of Texas (PUC or Commission) in which the Commission found that Southwestern Public Service Co.'s allocation of transmission and distribution dispatch expense based on average demand was reasonable.[10] That one case for an investor-owned utility operating outside of ERCOT, however, does not prove that other allocation methods are unreasonable. AE has proposed to allocate distribution load dispatch expense to customer classes based on 12NCP demand because it is consistent with how AE allocates all other demand-related distribution costs. The IHE found that the use of the 12NCP method recognizes that distribution facilities provide value throughout the year, and better captures the contributions of off-peak or seasonal customers whose demand may not be fully reflected in their class's peak. Therefore, AE recommends that a consistent approach be used for all demand-related distribution costs, including load dispatch expense, and respectfully requests that City Council reject the IHE Recommendation on this issue.

B. Primary Distribution Demand-Related Costs

The IHE recommends that a separate substation rate be developed for "Primary Substation customers" consistent with the proposals of NXP Semiconductors, Inc. (NXP) and TIEC.[11] AE

[9] IHE Recommendation at 82

[10] *Id*., (citing *Southwestern Public Service Co.*, Docket No. 43695, Proposal for Decision at 246 – 247).

[11] IHE Recommendation at 85.

respectfully disagrees with the IHE's recommendation. As explained in its Rebuttal Testimony and Closing Brief, AE serves three primary customers with demands larger than 20,000 kW, and none of these customers is served directly from any substation on AE's system. The point of interconnection (POI) for each of these customers is outside of the AE substation. Therefore, AE must install and maintain the primary distribution poles and lines to serve customers up to the POI, regardless of the geographic location of the interconnection point. Distribution feeders can be direct or shared. Distribution feeder lengths vary between a few hundred feet up to several miles, and there is no direct correlation between the location of the substation and a customer's property. In addition, it is common ratemaking practice to recover system costs on a class average basis regardless of the physical location of the interconnection. Therefore, it is AE's position that primary voltage customers should be allocated costs for the primary distribution poles and lines that are part of these feeders.

The ICA supports AE's approach to allocate primary distribution costs to customers near or adjacent to substations because it is consistent with standard cost ratemaking principles. It is inappropriate to set rates based upon the geographical location of the customer as NXP and TIEC propose. Therefore, their proposal to remove the allocation of primary distribution poles and lines for the primary voltage above 20,000 kW class and create a separate substation rate class should be rejected. AE also notes that NXP and TIEC's proposal, as adopted by the IHE, would shift costs on to other customer classes, including the residential class, which the IHE expressed concern about throughout his Recommendation. For these reasons, his recommendation on this issue should be revisited.

As noted in the IHE's Recommendation, AE must transform power down to a primary distribution voltage for Primary Substation customers.[12] AE, is open at this time to exploring options that include allowing the Primary Substation customers to purchase existing substation equipment and instead take service at transmission level.

C. Energy and Demand Line Loss Factors

In developing line loss factors, AE relied upon a System Loss Study for FY 2018 (Line Loss Study). Based upon the Line Loss Study, AE adjusted normalized energy sales and demands at the meter for each customer class to the generation level. This was done in order to properly take into account the percent of energy losses at each applicable voltage level. Both NXP and TIEC take issue with the Line Loss Study and make recommendations. The IHE does not adopt participants' recommendations, but instead "proposes that AE and the industrials revisit this issue."[13]

Regarding NCP cost allocation, NXP and TIEC recommend the use of demand losses. AE disagrees with this recommendation, because the NCP of a customer class may occur at any time during the month, and the losses associated with each class peak would prove difficult to measure on a consistent and regular basis. Therefore, the use of average energy losses as a proxy for the 12NCP demand loss is reasonable and should be adopted in this proceeding. The IHE did not disagree.[14]

Regarding CP cost allocation, both NXP and TIEC recommend the use of demand losses, and AE does not disagree with this recommendation. Ideally, demand losses should be utilized to adjust load, but AE has a demand loss measured only for the peak hour of the year (1CP). It does

[12] IHE Recommendation at 83.

[13] IHE Recommendation at 93.

[14] *Id*.

not have a demand loss measured for each peak hour of the month applicable to the 12CP cost allocation. Losses would be expected to be different at different loads and different ambient temperatures throughout the year. Therefore, the use of the average energy loss as a proxy for the 12CP demand loss is reasonable and acceptable. In support of AE's position, the IHE stated he "does not reject as unreasonable AE's use of the average energy loss as a proxy for the 12CP demand loss."[15]

The IHE recommended "that if reasonable adjustments could be made to AE's Line Loss Study to accommodate the industrials' concerns, then AE should cooperate with them in that endeavor."[16] While AE disagrees with TIEC and NXP regarding the use of demand losses for NCP cost allocation and disagrees entirely with TIEC's proposed methodology for directly deriving energy and peak demand loss factors from AE's Line Loss Study, AE is mindful of the IHE's recommendation. As such, AE is willing to commit to conducting a new Line Loss Study before its next base rate case.

IV. RATE DESIGN

A. Residential Rate Design

1. Introduction

Although the IHE made several recommendations that align with AE's proposed base rate case, residential rate design is one area of divergence. Although AE respects and understands the IHE's concerns and is also mindful of the impact of its proposal on the residential community, AE stands by its proposed residential rate design.

[15] IHE Recommendation at 93.

[16] *Id*.

Although AE's proposal has been characterized as unfairly targeting the residential rate class, AE's proposal is fair, reasonable, required, and necessary for its financial stability. The current rate structure has fundamental flaws that, if not corrected, will inexorably continue to drive AE's financial deterioration. The current structure depends far too heavily on energy sales, and particularly on sales in the higher rate tiers that are increasingly devoid of customer usage. Further, the lower consumption residential tiers are not currently paying near what it costs to serve them, contrary to any fair and reasonable ratemaking principle. Even if City Council adopts every one of the IHE's revenue requirement recommendations, AE will not recover its revenue requirement under the residential rate structure proposed by the participants, unless there is a substantial subsidy by another class of customers. The IHE was aware of this possibility and noted in his Recommendation that, "one way or another AE must recover its revenue requirement through its rates."[17]

AE's proposed residential base rate design was opposed by several participants, including the ICA, Sierra Club, Public Citizen, and Solar United Neighbors (SCPC/SUN), Two Women Ratepayers (2WR), and Paul Robbins. The IHE correctly declined to adopt any of their proposals. Instead, the IHE poses policy choices that must be incorporated by City Council, and phrases AE's proposed residential rate design as one that possibly subordinates conservation, affordability, and gradualism to AE's legitimate goals of increasing financial stability and aligning to intra-class cost causation.[18] AE respectfully disagrees with this assessment and believes its proposed residential rate design incorporates all competing interests in a balanced way that is equitable, fair, and reasonable. Just because a rate design raises costs for some residential customers does not in and

[17] IHE Recommendation at 6.

[18] IHE Recommendation at 100.

of itself make it unfair, and does not mean that the increase is unaffordable, especially given that this is AE's first base rate increase in more than ten years and AE's rates will still have increased less than the inflation rate for this time period.

While several participants categorize AE's residential base rate design proposal as radical, unfair, harmful, and abrupt, it is actually more fair to customers and provides greater benefits to AE's most vulnerable customers than the current rate design. AE has demonstrated that its proposal is necessary due to residential customer growth occurring in the first and second tiers—therefore creating more customers who are paying well below cost of service, exacerbating the problem—and changes in consumption patterns, and corrects for years of subsidizations in an effort to move all classes toward their cost of service. AE's current residential base rate structure is an industry outlier, and AE's proposal moves residential customers closer to cost, which is a typical measure of fairness. Although AE's proposed base rate design results in an increase for some classes, it is closer to being cost-based, fair, and avoids rate shock, while still maintaining its emphasis on conservation and energy efficiency, which are all discussed further below.

2. Financial Stability

AE has more than proven the financial need for its proposed base rate increase at every opportunity in this proceeding—in the Base Rate Filing Package, through the discovery process, in its rebuttal testimony, during the Final Conference, and in its Closing Brief. The IHE agrees with AE and believes that "AE has articulated reasonable goals and policies designed to increase its financial stability."[19] Therefore, AE does not take exception to that portion of the IHE's Recommendation, other than to reiterate that its proposed base rate increase is:

[19] IHE Recommendation at 101.

1. Required to ensure compliance with future Net Revenue requirements as defined in the Rate Covenant in the Master Ordinance;
2. Necessary to improve its financial health, fully comply with financial policies, and maintain credit ratings; and
3. Reasonable to increase base rates for the first time in ten years, yet still produce competitive residential bills compared to other electric utilities in Austin and remain below historical inflation.

While AE is mindful of all goals to be considered in a base rate case, it urges that the principle of financial stability must be prioritized. That is not to say that the other principles should be subordinated. AE is still addressing the principles of conservation, affordability, energy efficiency, gradualism, and others in many ways, both inside and outside of this proceeding. AE cannot promote and further any of these principles without effectively yielding the revenue requirement and providing stable revenues and ensuring the long-term financial strength of the utility. Current base rates and structures do not support the long-run financial strength and stability of the utility, and AE's proposed changes to the residential base rate design are needed to support the continued viability of AE to meet current and future obligations. The IHE concurred, and found that "AE has established that, under the current structure, it is not collecting sufficient revenue from the residential class to ensure its financial stability."[20]

3. Fairness and Subsidy

As laid out in AE's Base Rate Filing Package, under the existing five-tier structure, the first and second tiers are priced far below cost and are subsidized by the fourth and fifth tiers that are above cost. The first and second tiers are also subsidized by the commercial S2 and S3 classes,

[20] IHE Recommendation at 104.

because there aren't enough customers in tier four and five to recover the subsidy. More than 40% of residential customers are being subsidized by other residential customers that reside in the higher tiers and by commercial S2 and S3 classes. Under traditional rate design principles, such subsidization is undesirable and exacerbates financial instability. AE's proposed base rates address the subsidy issue by lowering the rate differentials between tiers as well as reducing the number of tiers. The overall effect of its proposed redesign is that the amount of subsidy will be much lower and the prices charged to customers will be more closely aligned with the cost to serve them. However, the proposed redesign only moves classes 50% to unity.

AE's proposal also mitigates fairness issues with respect to customers' load factors. Capacity costs for residential customers are primarily driven by peak demand, rather than by total energy. For residential customers, AE currently recovers its capacity costs through charges on total energy. Customers with flatter load profiles are effectively subsidizing capacity costs to serve customers with more peaked load profiles because both are charged according to total energy irrespective of load profile. Additionally, capacity costs are fixed in nature and do not vary based on consumption. AE's proposed base rate design mitigates this issue by increasing the customer charge and flattening the tiers.

AE's proposed residential base rate structure is more transparent and offers adequate support to lower income customers. AE stands by its position that reducing the energy burden on vulnerable customers is best addressed through targeted programs rather than rate structures because the latter approach unfairly benefits and subsidizes a large percentage of higher-income customers. As previously argued, using rate structures to support lower income customers can have unintended consequences for both the customer and AE.

Several participants, namely those who represent residential customers in the first and second tiers, oppose AE's proposed residential base rate structure. Importantly, however, the IHE did not adopt any of their proposals. The IHE instead agreed with AE that "specific programs to address economically vulnerable customers, funded through the CBC, is a more transparent method to provide bill assistance to lower income individuals than a subsidy contained within the base rate structure itself."[21]

The IHE also accepted AE's evidence and found that "under the current tier system, high tier customers pay rates that exceed their allocated cost of service and low tier customers pay rates below their allocated cost of service."[22] Because most of AE's residential customers reside in the first and second tiers, AE simply cannot afford to continue to implement a rate design that drastically subsidizes those customers. The money it costs to serve those customers must come from somewhere. AE believes its approach takes great strides toward correcting this unfair and imbalanced rate design, while still maintaining a subsidy under a gradualist approach, such that those customers are not immediately moved to cost. Although the IHE found that "AE has presented a reasonable gradualism proposal," the IHE agreed with other participants' "affordability and gradualism concerns and recommends that the parties revisit either AE's rate design, CAP, or perhaps different customer assistance programs."[23] For AE's financial stability and those residential customers who have been heavily subsidizing their neighbors for more than ten years, AE respectfully requests City Council reverse the IHE's recommendation on this issue.

[21] IHE Recommendation at 107.

[22] *Id.*

[23] IHE Recommendation at 107.

B. Rate Design and Conservation

Throughout the proceeding, some participants have classified AE's rate design proposal as one that disincentivizes energy efficiency and conservation. AE's proposed base rate design still predominantly focuses on conservation. One hundred percent of the demand costs are designed to be recovered in energy rates. The energy rates are proposed in three tiers of inclining blocks of consumption, which amplifies the conservation price signals. Further, the IHE found that "AE's history reflects conservation goals as part of its mission."[24]

Several participants criticize AE's position on conservation, but none of them provide evidence that AE's customers are responding to conservation price signals, and none of them provide evidence for their claim that AE's proposed residential base rate design will increase future electricity consumption. AE stands by its position that its proposed rate design will not weaken conservation price signals, and that residential customers largely do not change their behavior in response to the conservation price signals. Lastly, there is no data showing consumption will increase under the proposed rate design. The IHE does not disagree with AE on these issues and does not adopt the recommendations of any other participants on these issues.

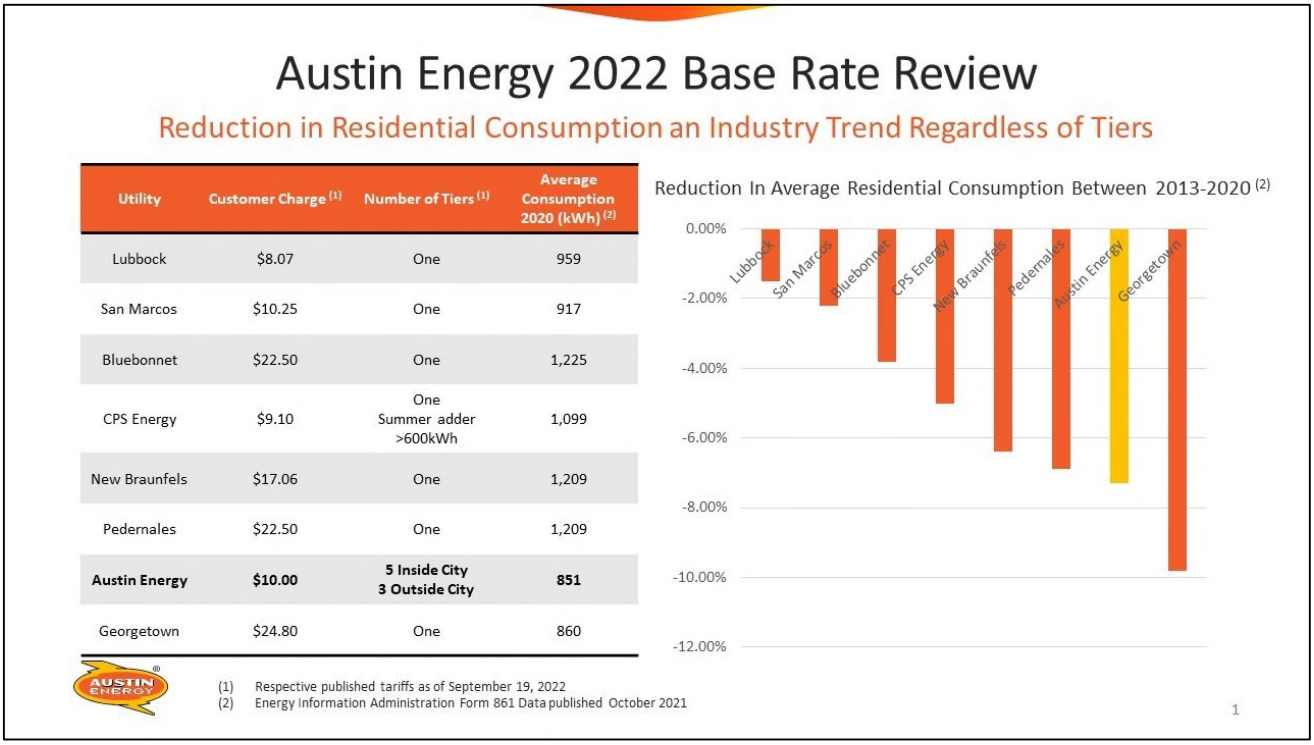
However, the IHE does cast doubt on AE's analyses that support its argument that customers do not respond to the conservation price signals in the present rate structure. AE analyzed whether residential customers changed their consumption behavior based on their relative tiers using a bunching analysis.[25] The bunching analyses demonstrated both visually and statistically that AE's customers' behavior was not responsive to tiers in base rates. AE's bunching analysis showed that bunching was not observed in the distribution of kWh in customer bills, and

[24] IHE Recommendation at 110.

[25] "Bunching" describes the theory that as customers approach a higher priced tier, customers modify their behavior and conserve their energy consumption to avoid the higher priced tier.

only a very small percentage of customers even take steps to access information that would indicate bunching occurs. These findings are detailed in AE's Base Rate Filing Package. From its bunching analyses, AE concluded that the number of tiers and the breakpoints of the tiers do not have a noticeable effect on energy conservation.

In addition, recent Energy Information Administration (EIA) data shows all utilities have declining residential consumption, but only AE has tiered rates. This new data shows that conservation and energy efficiency occurs under flat rates, and is not dependent on tiers. The below chart shows the reduction in residential consumption across several utilities in Texas.



Austin Energy 2022 Base Rate Review

Reduction in Residential Consumption an Industry Trend Regardless of Tiers

Utility	Customer Charge (1)	Number of Tiers (1)	Average Consumption 2020 (kWh) (2)
Lubbock	$8.07	One	959
San Marcos	$10.25	One	917
Bluebonnet	$22.50	One	1,225
CPS Energy	$9.10	One Summer adder >600kWh	1,099
New Braunfels	$17.06	One	1,209
Pedernales	$22.50	One	1,209
Austin Energy	**$10.00**	**5 Inside City 3 Outside City**	**851**
Georgetown	$24.80	One	860

(1) Respective published tariffs as of September 19, 2022
(2) Energy Information Administration Form 861 Data published October 2021

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Although the IHE raised some concerns with AE's bunching analysis, he also noted that "no party has articulated a convincing analysis on price elasticity,"[26] indicating that no other

[26] IHE Recommendation at 110.

participant offered contravening evidence. Therefore, AE's analyses should be given proper consideration until there is some evidence to the contrary.

C. Rate Design and Affordability

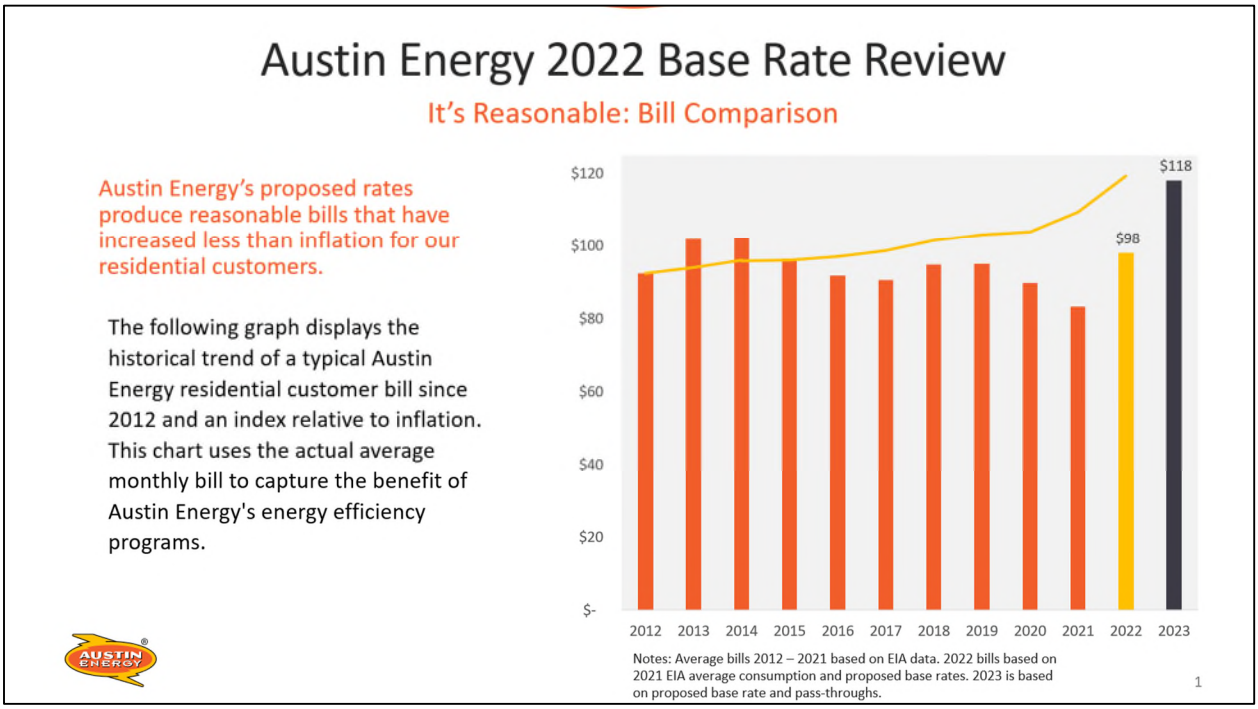
Several participants argue the proposed rate design will increase bills for low and median income customers while leading to lower bills for higher income, higher consumption customers. AE disagrees with this characterization regarding income levels.[27] Although AE's proposal is designed to move away from the intra-class subsidization in its current rate design, which means that tiers with lower consumption will experience a rate increase, customers in these lower usage tiers will still be paying less than customers in higher usage tiers. AE does not track consumption by income, because it cannot ask its customers what their income levels are, and because it has found that tracking income by zip code, as proposed by some participants, is equally problematic. However, AE uses its automatic enrollment Customer Assistance Program (CAP) customers as a proxy for low-income customers, and AE's analyses show that CAP customers, on average, use more energy than non-CAP customers. Other participants attempted to demonstrate the opposite, but AE has not found that to be the case. The IHE found that evidence presented by other participants was not persuasive.[28]

The participants also argue that AE's proposed redesign will harm vulnerable customers. The IHE repeatedly refers to "economically vulnerable customers" who are not within AE's CAP and raises concerns about the rate impact on those customers. However, the IHE does not define the term "economically vulnerable," or define what amount of a rate increase would be acceptable

[27] In preparing the base rate proposal, AE compared two ZIP codes within Austin—downtown and East Austin). AE's analysis shows that downtown Austin has a much higher average income, a much lower number of Customer Assistant Program (CAP) customers, a much lower average consumption, and much lower average bills.

[28] IHE Recommendation at 112.

for those customers to withstand. It is true that AE's proposed residential rate design will result in an increase for residential customers. But this fact should be viewed in a historical context. AE has not requested a rate increase for its customers in more than a decade. Even with the proposed rate increase, AE's residential customers will experience reasonable bills that have increased less than inflation. The following graph displays the historical trend of a typical AE residential customer bill since 2012 and an index relative to inflation. This chart uses the actual average monthly bill to capture the benefit of AE's energy efficiency programs.



Although AE has done everything it can to shield its customers from a base rate increase, it is not unreasonable for customers to pay more for electricity than they did ten years ago in 2012. Low consumption residential customers have also been, perhaps unknowingly, enjoying subsidization from customers in higher consumption tiers and from customers in other classes. This subsidization is unfair and has proven to be financially unsustainable. AE's proposal should not be characterized as radical or unfair for attempting to remedy this problem.

The IHE also discussed participants concerns regarding AE's CAP. Although perhaps not perfect, AE's CAP is a robust program that automatically enrolls customers who qualify for certain federal, state, and local assistance programs. AE's robust CAP waives the customer charge for vulnerable customers, which mitigates the concern about vulnerable customers not being able to bear a higher fixed component of the bill, and not being able to otherwise avoid it, such as via changes in usage. AE's proposed base rate design will also significantly increase benefits under the CAP to achieve greater levels of social equity among AE's residential customers. The value of the CAP's waiver of the customer charge increases by 150%, from $10 per month to $25 per month. Using load information from the COS Study, AE expects the total value of CAP benefits to increase from $8.3 million to $14.4 million. The increases in this value do not affect the base rates of any customer, but rather are funded exclusively through the Community Benefit Charge (CBC).

The participants' characterizations of CAP are misplaced, especially when viewed in a benchmarking context. AE has one of the most robust customer assistance programs in the state. AE analyzed how its well-designed CAP program compares to assistance programs at other local utilities. For example, while AE waives the customer charge and CAP CBC, San Antonio City Public Service (CPS Energy) does not. AE also gives a 10% discount on remaining charges. CPS Energy requires the customer to apply for enrollment, whereas AE automatically enrolls customers who are already on certain federal, state, and local assistance programs. CPS Energy qualifies customers who are at or below 125% of Federal Poverty Guidelines, while AE reaches up to 200%. Additionally, Lubbock Power and Light (LP&L) does not appear to offer any assistance to vulnerable customers. AE's programs are far more considerate to its CAP customers' needs and

AE is in a different position relative to CPS Energy and LP&L with respect to the potential impact of a customer charge on vulnerable customers.

The IHE recommended balancing AE's legitimate policy priorities of financial stability with limiting rate shock for those vulnerable customers who are not covered by CAP.[29] AE believes its proposal does just that. AE appreciates the IHE's concerns and will continue to evaluate programmatic changes that can enhance the CAP's impact on economically vulnerable customers even more.

D. Gradualism and Rate Shock

The IHE raised concerns about the possibility of AE's proposed rate design causing rate shock for certain low usage sub-groups of the residential class.[30] Despite the fact that the IHE did not recommend adoption of AE's proposed residential rate design, the IHE found "that AE has presented a reasonable gradualism proposal."[31] AE proposes moving all rate classes closer to COS, which must be done in order to correct for the flawed system that has led to AE's financial deterioration. However, AE is mindful of rate impacts on customers and the need for gradualism. As such, AE proposes an initial step of moving the residential class to only 50% of cost. Recent Commission precedent supports rate classes being set at COS, unless gradualism would be appropriate to avoid rate shock, which is exactly what AE proposes to do here.[32]

E. Customer Charge

The IHE expressed concern about AE's proposed customer charge. AE proposes to increase the customer charge from $10 to $25 to reflect fixed customer costs that do not vary with

[29] IHE Recommendation at 100.

[30] IHE Recommendation at 113-114.

[31] IHE Recommendation at 107.

[32] AE Ex. 9 at 11.

consumption. Matching the customer charge to the customer unit costs will result in customer charge revenues directly tracking the underlying cost driver—the number of customers. Despite the increase in the customer charge, its proposed customer charge is still less than the total combined customer and delivery costs suggested by the COS Study. Further, AE's CAP waives the customer charge for CAP participants, magnifying the effect of this exemption for CAP customers.

The IHE stated he is "concerned that AE's proposed 150% customer charge increase will result in rate shock for some residential customers."[33] While this number read in isolation may seem alarming, an increase that is large on a percentage basis is still reasonable in absolute terms when the dollars involved are relatively small. Both the current customer charge, at $10, and the proposed customer charge at $25, represent only a minority share of the customer's total bill. The $15 increase to the customer charge is needed to improve AE's financial health and increase fairness. Ultimately it is the overall bill impact that must be considered, not an isolated percentage increase in a single component.

Several participants, along with the IHE, also raise concerns with benchmarking analyses conducted both by AE and by other participants. AE acknowledges that no benchmarking analysis is perfect, because there are differences in multiple factors such as geographic area, number of customers, cost of service, and utility structure that make it difficult to make accurate and meaningful comparisons among utilities. AE's only goal in providing benchmarking analyses is to show that its proposal, both with regard to the customer charge and its tier structure, (discussed more below) is not an outlier and actually compares favorably with the rates of other similarly situated utilities serving residents in and around the Austin area. For example, AE's customer

[33] IHE Recommendation at 120.

charge is comparable to customer charges at Pedernales Electric Cooperative, Bluebonnet Electric Cooperative, and the City of Georgetown, which all surround AE's service territory and represent the local alternatives to AE.

The ICA argued that AE should instead be compared to CPS Energy and LP&L, which each maintain a customer charge lower than AE's current customer charge.[34] However, that comparison fails to take into account other factors, including that neither CPS Energy nor LP&L use tiered base rates, and both have higher average consumption. Utilities that have higher average residential consumption than AE can afford lower customer charges because they have more kWh sales to recover their costs. Further, these utilities have flatter rate structures than AE's. It is misleading to compare AE's proposed customer charge to other municipally-owned utilities' (MOU) customer charges to the extent that the comparison MOUs may have flat or declining block rate structures as opposed to AE's inclining structure. The comparison also fails to consider demographic trends in Austin, including high customer growth and shifts to smaller housing units. Revenue stability has taken on heightened importance and urgency because of these factors, and it is therefore appropriate for Austin's rates to differ from other MOUs in Texas. In addition, the comparison fails to account for how AE's CAP compares favorably to assistance programs at those other utilities.

The IHE's recommendation regarding the customer charge centered on concern over the steep increase, which AE addressed above. However, the IHE also found "that AE's concerns of financial stability are well founded, regardless of whether AE implements its proposed customer charge or adopts a more sharply tiered rate structure."[35] The IHE recommended that in either case,

[34] IHE Recommendation at 115.

[35] IHE Recommendation at 120.

the policy considerations of conservation, gradualism, and affordability be observed. AE believes its proposal is consistent with the IHE's recommendation.

F. Tier Structure

Any proposal that is adopted must make changes to AE's current tier structure. Currently, the majority of in-city residential customers are billed on a five-tier inclining structure. The 40% of residential customers whose bills fall entirely with the first and second tiers are priced well below cost. The stark reality is that there are simply not enough residential customers with consumption in the higher tiers to make up the revenue deficit from the lower tiers, and new customers being added to the system fall into the first and second tiers, and do not pay their cost of service. This is exacerbated by the fact that high-use customers are becoming a much smaller percentage of customers as new growth in sales is occurring primarily in the lower tiers. In FY 2021, 76% of residential energy sales occurred in the first two tiers. The disappearance of energy sales from higher-priced tiers and the concentration of sales in the tiers priced below cost of service are two of the factors that have caused the residential class to drift further away from cost of service since the last base rate review. It is important to note that lower energy consumption is not a result of the current rate structure's price signals, but rather changes in technology, building codes, and housing density in the interim, along with a large amount of new residential construction and population growth adding customers in the below cost of service tiers. The current tier structure is simply unsustainable.

AE proposes a new residential base rate structure designed to capture the changing composition of the residential customer class, relying more heavily on cost recovery in the initial, lower consumption, tiers. AE proposes to modify the residential base rate structure by reducing the number of tiers and flattening the steepness of the rate increases between each tier. Under AE's proposal, the number of tiers is reduced from five to three, and the tier breakpoints are

adjusted downward. This is designed to match the shift in the bill frequency distribution toward lower levels of consumption. AE's proposed rate design preserves the price signals sent to customers, as high use customers who use more energy will continue to have higher bills.

The IHE discussed the proposals put forth by several participants, but declined to recommend of any of them. The IHE's concerns, again, focus on the potential rate impact to residential customers, which AE has thoroughly addressed in the sections above. AE is mindful of this concern and is willing to work with City Council on a proposal that reduces seasonal volatility, provides greater financial stability to AE as residential consumption continues to decrease, preserves conservation price signals, avoids intra-class rate shock and subsidization, and protects economically vulnerable customers. AE appreciates that the IHE is cognizant of all of these goals, some of which may be at odds with each other. AE has designed its rate structure proposal in a way that it believes best addresses each of these competing concerns and believes its proposal should be adopted.

G. Outside-City Customer Rate Differential

The IHE disagreed with AE's proposal to eliminate the base rate distinction between inside- and outside-city customers. The IHE appeared to be compelled by the ICA's argument that AE's proposal shifts revenue responsibility from the outside-city customers to the inside-city customers and is therefore unfair. However, no evidence supports the ICA's theory that AE's proposed single residential base rate structure is unfair to inside-city residential customers, other than an apparent preference for subsidization of inside-city residential customers by outside-city residential customers. Further, leaving outside-city residential customers unchanged would violate cost causation principles used in ratemaking. The IHE notes the "differences in usage characteristics" between inside-city and outside-city residential customers, but AE would argue that there are "differences in usage characteristics" between next door neighbors and between any

two inside-city customers. AE certainly would not design rates differently for every household who consumed electricity differently than its neighbor. Therefore, AE respectfully disagrees with the IHE's recommendation to leave the outside-city residential tariff unchanged, and requests City Council reject the IHE's Recommendation on this issue.

V. VALUE OF SOLAR

The IHE recommended that AE's VoS proposal is reasonable, appropriate, and that it be calculated in accordance with AE's recommendation. In addition, he recommends: (1) AE evaluate opportunities for additional public and stakeholder input in future VoS determinations, and (2) AE more clearly define what comprise the "rates, methodology, and inputs" that must be reassessed consistent with AE's VoS tariff.[36] AE appreciates the IHE's thoughtful consideration of these issues and will commit to working on his recommendations in advance of its next base rate case, or the next opportunity to evaluate AE's VoS tariff.

VI. OTHER ISSUES

A. Proposed Power Supply Adjustment Factor Adjustment for Primary Substation Customers

The IHE recommended that "AE, TIEC, and NXP work to develop a Primary Substation rate for distribution service where the ratepayer is the only recipient of service on that line."[37] First, the PSA is not under review in this proceeding, so the proposal by TIEC and NXP was out of scope, and the IHE's recommendation "that AE revisit the PSA to ensure that it is consistent with [his] recommendation" was outside of his scope of review. Further, AE has differentiated the PSA charges by voltage—specifically, the service provided at transmission, primary, and secondary voltages—to recognize the differences in energy losses. AE does not have any primary

[36] IHE Recommendation at 128, 140.

[37] IHE Recommendation at 141.

substation customers. Primary distribution customers are within the primary distribution class and should be allocated a proportional share of the costs for the primary distribution system as developed by AE and included in the proposed base rate charge. Therefore, AE respectfully disagrees with the IHE and urges City Council to reject the IHE's recommendation on this issue.

VII. CONCLUSION

AE agrees with the majority of the IHE's recommendations other than those concerning rate design, and although AE does not agree with the IHE's recommendations in that area, it believes that the IHE's Recommendation is thorough, thoughtful, and well-reasoned. It has achieved the goal of providing guidance to AE and the City Council in moving forward to reach a proper outcome in this proceeding.

AE extends its appreciation to the IHE for his thoughtful consideration of the evidence and patience with this process. Toward that end, AE has limited these Exceptions to identifying the key issues that warrant reversal by City Council. Accordingly, it is respectfully requested that AE's Exceptions to the Recommendation, as set forth above, be granted and such other and further relief to which it may be entitled.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of this pleading has been served on all parties and the Impartial Hearing Examiner on September 26, 2022, in accordance with the 2022 Austin Energy Base Rate Review Procedural Guidelines.

THOMAS L. BROCATO