



Salt Lake City/Phoenix

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To: SCL Review Panel, Councilmember Michael O'Brien
From: The Manufacturing Industrial Council
Date: July 16, 2012
Re: Comments on Greg Hill Proposed Rate Design Changes

Dear Councilmember O'Brien and Seattle City Light Review Panel,

Energy Strategies appreciates the opportunity to comment on behalf of the Manufacturing Industrial Council (MIC) on the recommended changes made by Greg Hill on March 20, 2012, regarding Seattle City Light's (SCL) rate design and cost allocation for customer classes.

Summary

Mr. Hill presents proposals on both rate design and cost allocation, which are distinctly different principles: rate design addresses the subject of designing rate components to collect a certain amount of revenue from a customer class, whereas cost allocation speaks to the subject of how cost responsibility is assigned to the different customer classes. Hill incorrectly uses these concepts interchangeably and thereby distorts his policy recommendations to the disadvantage of industrial customers.

Overall, MIC finds his suggestions harmful to industrial energy users and recommends that they not be considered.

Marginal Cost Allocation (Page 2)

One of the most misleading issues in Hill's paper is his combination of rate design and cost allocation. His discussion on "returning" to a marginal cost allocation method is confusing in that SCL has used a marginal cost approach since 1980¹. Thus, there is no need to "return" to it. Although most utilities allocate costs to customer classes based on embedded, or "average", costs, SCL has used the marginal approach in every rate case over the last three decades.

The marginal cost study results (Table 1) proposed by Hill have no work papers to support the data and appear to be based on dated or overstated prices and, thus, do not reflect current natural gas prices. Hill's incorrect use of rate design and cost allocation results in a proposal under which large customers see an increase in costs allocated to them of eight to nine percent, while residential customers see a cost allocation reduction of six percent. MIC believes Hill's proposal is simply an attempt to lower residential rates at the expense of larger customers under the guise of "efficient pricing." Efficiency gains and CO₂ reductions can be achieved through rate design. As noted above, rate design and cost allocation are completely separate issues.

¹ 2007 Rate Case Cost of Service and Cost Allocation, page 40

Elimination of Demand Charges (Pages 6-7)

MIC opposes Hill's proposal to eliminate demand charges. Demand charges are an important mechanism to recover to the costs of generation, transmission and distribution capacity in a fair and efficient way. If demand charges are reduced or eliminated, then energy prices must be increased, which unfairly shifts costs among industrial customers, from lower-load factor customers to higher-load factor customers within each demand-billed rate schedule.

MIC believes that SCL's current demand charges are already too low and consequently, its energy prices are too high. Hill's proposal to eliminate demand charges will force the energy charge to be increased, which will serve his objective of making the price of power charged to customers at the margin as high as possible. MIC emphasizes that any sense of fairness among customers is eliminated if his proposal is adopted. High-load factor customers would be overcharged for system capacity and low-load factors customers undercharged for it.

Baseline Rates (Pages 7-8)

Hill introduces a very complex pricing regime that MIC does not support. The proposal includes pricing increasing or decreasing energy use at a high price than the average price in rates. While a customer that doesn't change its energy usage pays the same total cost, a customer with increased usage pays a higher rate.

MIC believes such a rating policy is so complex that it would require significant staff time and customer time to properly implement. In addition, the pricing mechanism would **penalize economic growth**, which is contrary to good public policy, particularly when Seattle continues to struggle economically. Endorsing this policy will also penalize customers who have already been aggressive in their energy conservation investments, while those who have been slow to adapt conservation policies would be rewarded.

Global Warming Credit (Page 9)

MIC finds Hill's "global warming credit" proposal to be inequitable in that customers who use more power would pick up part of the cost of paying for the SCL system that was built to serve small customers. In order to greatly increase energy charges, SCL would be required to reduce charges someplace else in the bill; otherwise the utility would over-collect revenues that it needs to provide power to the system. The global warming credit – or negative customer charge - attempts to accomplish that, but it comes at the expense of shifting cost recovery from smaller usage customers to higher usage customers. MIC does not support this arbitrary cost shift to the detriment of high-end energy users.

Electric Rate Design for High Demand Customer Class (Page 10)

Hill's proposed new electric rate design for High Demand customers is also arbitrary and potentially detrimental to the economy that, as noted above, is still struggling and trying to recover. Under this proposal, the largest customers would receive a credit against their energy bills for the number of full-time employees on their payrolls, while the cost of energy per kilowatt-hour is greatly increased. For businesses expanding and hiring this mechanism may be something to consider, but under current economic conditions MIC believes it would be punitive for companies that are undergoing downsizing and could exacerbate their financial struggle.