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BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of The East Ohio Gas Company dba Dominion East Ohio for Authority to Increase Rates for its Gas Distribution Service.	:	Case No. 07-829-GA-AIR
In the Matter of the Application of The East Ohio Gas Company dba Dominion East Ohio for Approval of an Alternative Rate Plan for its Gas Distribution Service.	:	Case No. 07-~~838~~ 830-GA-ALT
In the Matter of the Application of The East Ohio Gas Company dba Dominion East Ohio for Approval to Change Accounting Methods.	:	Case No. 07-831-GA-AAM
In the Matter of the Application of The East Ohio Gas Company dba Dominion East Ohio for Approval of Tariffs to Recover Certain Costs Associated with a Pipeline Infrastructure Replacement Program Through an Automatic Adjustment Clause, and for Certain Accounting Treatment.	:	Case No. 08-169-GA-ALT
In the Matter of the Application of The East Ohio Gas Company dba Dominion East Ohio for Approval of Tariffs to Recover Certain Costs Associated with Automated Meter Reading and for Certain Accounting Treatment.	:	Case No. 06-~~1452~~ 1453-GA-UNC

REPLY BRIEF OF THE STAFF OF THE PUBLIC UTILITIES COMMISSION OF OHIO

INTRODUCTION

Staff believes the Commission should approve a straight-fixed-variable rate design for The East Ohio Gas Company, dba Dominion East Ohio, in this case. The choice involved here is the same as that the Commission confronted in *In re Duke Energy*

Ohio, Case No. 07-589. The factors leading the Commission to approve a "levelized" rate design, like the straight-fixed-variable, in that case exist in this one also. The Commission's reasoning in the *Duke* case applies in this case as well. Staff believes the Commission should make the same choice it made in the *Duke* case for the same reasons. The straight-fixed-variable rate design more closely aligns fixed costs with fixed rates and more appropriately recovers those costs for that reason. It also sends better price signals. Staff believes it is the better rate design.

DISCUSSION[1]

I. The public received adequate notice of the straight-fixed-variable rate design contemplated in this proceeding.

OCC claims the public notice accompanying Dominion's rate increase application was inadequate because it did not mention the straight-fixed-variable rate design. OCC bases its claim on the supreme court's holding in *Committee Against MRT v. Pub. Util. Comm.*, 52 Ohio St. 2d 231 (1977) that the court again applied in *Ohio Association of Realtors v. Pub. Util. Comm.*, 60 Ohio St. 2d 172 (1979). In both these cases, the utility sought a new rate plan but did not provide adequate notice *of the rate plan sought in the application.* This is a distinguishing fact between those cases and the present case. Dominion did not seek the straight-fixed-variable rate design in its application. As the Commission is aware, Dominion sought the existing rate structure with a sales reconciliation rider in its application. Staff's later proposal of a different rate structure in the Staff Report did not invalidate the public notice Dominion issued or violate Revised

[1] Staff does not intend to respond to every argument presented by those objecting to the straight-fixed-variable rate design; Staff does not believe it is necessary to do so. Accordingly, Staff's silence regarding any matter should not be construed as acceptance or acquiesance.

Code requirements. *AT&T Communications of Ohio v. Pub. Util. Comm.*, 51 Ohio St. 3d 150 (1990).

In *AT&T Communications of Ohio v. Pub. Util. Comm.*, 51 Ohio St. 3d 150, GTE sought a rate increase and requested local exchange users pay the entire increase. As in this case, Staff proposed a different method in the Staff Report. *Id.* The Commission did not adopt either approach ultimately and assigned the rate increase to most existing rates, including the common carrier line charge, on a uniform percentage basis. *Id.* at 151. The common carrier line charge was the charge GTE collected when long distance companies, such as AT&T and MCI, gained access to GTE's local loop to complete local calls. AT&T and MCI objected to increasing the common carrier line charge and appealed the Commission's decision. They complained, in part, that the rate plan the Commission approved did not appear in the public notice of the rate increase application and cited the two cases relied upon by OCC. *Id.* at 152-153. The supreme court rejected that argument distinguishing the cases relied on by OCC. The court distinguished the cases because GTE, as Dominion in this case, did not propose the rate plan at issue. GTE, as Dominion in this case, included the rate plan it proposed in the public notice of its rate increase application. That satisfied the Revised Code requirements. *Id.* at 153. The supreme court explained:

> In the instant case, GTE did not propose, in its application, to increase the CCLC [the common carrier line charge]; the CCLC increase, consequently, was not within the "substance and prayer" of the application. [R.C. 4909.19 requires the utility seeking a rate increase to "publish the substance and prayer of the application.]. Thus, R.C. 4909.19 did not require GTE to mention the increase in the notice.

Id. at 153. As in *AT&T*, Dominion published notice of the rate increase it sought. In doing so, it met the Revised Code requirements. *Id.* The Commission's ultimate adoption of a different rate plan is not constrained by that notice and it does not invalidate that notice. *Id.* at 155.

Beyond that, Dominion's public notice noted recommendations that differ from the application may be made by Staff or intervening parties and may be adopted by the Commission. Tr. IV at 42. In other word, Dominion provided the public with notice at the time of its application that what happened in this was a possibility. For that reason, alone, no one should complain.

Additionally, the Commission offered multiple opportunities for public comment on the straight-fixed-variable rate design throughout Dominion's service territory. This is similar to the remedy the supreme court ordered in *Committee Against MRT* and in *Ohio Association of Realtors.* As a remedy in *Committee Against MRT*, the court only ordered the Commission to conduct a hearing. *Id.* In *Ohio Association of Realtors,* the court remedied the lack of notice "by ordering the commission to reissue appropriate notices and conduct further hearings on the original application." *Id.* In this case, the Commission held public hearings at many locations throughout Dominion's service territory after the Staff Report was issued. The Commission directed Dominion to include notice of the straight-fixed-variable rate design in the public notices of those hearings. Tr. IV at 85. Those notices included that notice and also stated other approvals may be made. *Id.* The company published those notices in newspapers throughout its service territory over multiple weeks. *Id.* at 87. The parties to this case, of course, have been well aware of Staff's recommendation of the straight-fixed-variable rate. They had the ability to present evidence, cross-examine witnesses and present argument in the evidentiary hearing.

In short, the public and the parties to this case received ample notice of the contemplation of the straight-fixed-variable rate and had an opportunity to comment. The Commission has already provided what the remedies the supreme court ordered in *Committee Against MRT* and *Ohio Association of Realtors.* Simply, any complaint about the notice or process in this case is not val*Id.* The notice and process provided in this case comply the Revised Code.

II. Decoupling the link between gas consumption and Dominion's ability to recover its revenue requirement is appropriate.

This topic was discussed in Staff's merit brief and that argument will not be presented again here. Despite the facts demonstrating decoupling is appropriate for reasons endemic to natural gas distribution companies some have suggested that the current rate structure should continue and the case for change has not been made. Such arguments ignore the facts of this case.

No one has refuted the existence of the problem mandating decoupling. The rate design behind the company's current rates recovers most of the company's fixed distribution costs through a variable rate component that is dependent upon gas usage. Accordingly, the ability of Dominion, as well as other natural gas distribution companies, to recover their fixed distribution costs hinges in large part on sales as the Commission has recognized. *In re Duke Energy Ohio,* Case No. 07-589-GA-AIR (Opinion and Order at 17) (May 28, 2008). This rate structure allowed the companies the opportunity to recover the recommended revenue requirement *as long as gas consumption remained level or increased.* Staff Ex. 1 at 34 (Staff Report); DEO Ex. 1.0 at 41-42 (J. Murphy Dir.

Test.). But, that circumstance no longer exists in Ohio's natural gas distribution industry, in general, or in Dominion's service territory, in particular.

Consumption is declining in Dominion's service territory and it has declined for years. DEO Ex. 1.0 at 41-42 (J. Murphy Dir. Test.). Additionally, the company projects such declining consumption will continue in the future. Tr. IV at 72-73. The company's long term forecast report for the 10-year period through 2017 projects continuing declining sales. *Id.* Accordingly, the company will continue experiencing difficulty recovering its fixed distribution costs if that recovery depends on sales. For these reasons, alone, decoupling Dominion's recovery of its distribution costs from its sales is warranted and the record supports it.

III. The straight-fixed-variable rate design results in smaller subsidies than Dominion's current rate design that is associated with the sales reconciliation rider.

Some have claimed that the straight-fixed-variable rate design results in low usage customers subsidizing high usage customers. That claim is not true. As the Commission appreciates, the straight-fixed-variable rate design is a change from the current rate design and, "as with any change, there will be some customers who will be better off and some customers who will be worse off, as compared to the existing rate design." *In re Duke Energy Ohio,* Case No. 07-589-GA-AIR (Opinion and Order at 19) (May 28, 2008). Some will not be affected by a switch to the straight-fixed-variable rate design. *Id.* These results do not mean a subsidy has been created.

Rather than creating a subsidy, the straight-fixed-variable rate merely *reduces* a subsidy that exists under current rates. The current rate design recovers most of the company's fixed distribution costs through a variable rate, that varies with usage, and it recovers a small part of the costs through a fixed rate. Accordingly, the current rate design distributes more of the fixed costs to higher users of natural gas. The straight-fixed-variable rate design more evenly distributes fixed costs by increasing the portion of those costs recovered through a fixed rate component, thereby, matching fixed and variable cost recovery more closely with the costs actually incurred. Staff Ex. 3 at 4-5 (S. Puican Prefiled Dir. Test.). Since some low usage customers have not paid the entirety of their fixed costs under the current rate design, they may pay more. The converse is true for higher usage customers. The Commission explained:

> The levelized rate design [the straight-fixed-variable] will impact low usage customers more, since they have not been paying the entirety of their fixed costs under the existing rate design. Higher use customers who have been overpaying their fixed costs will actually experience a rate reduction. Average users will see only the impact of the increase … [due to the rate increase rather than the change in rate design]; they will see no additional impact as a result of the Commission choosing the levelized rate design.

In re Duke Energy Ohio, Case No. 07-589-GA-AIR (Opinion and Order at 19) (May 28, 2008). As the Commission described, this effect is not a *subsidy*. It is a reduction in one that results from a more appropriate reflection of cost causation and proper rate design.

IV. The beneficial impacts of the straight-fixed-variable rate design on higher usage customers who have been overpaying their fixed costs is also beneficial to low-income customers.

The rate effects of the straight-fixed-variable rate design are not affected by the income of individual rate payers. Higher use customers who have been overpaying their fixed costs, including those with low-income, will experience a rate reduction. Conversely, lower use customers who have not been paying all their fixed costs, including those with low-income, will experience an increase. Average use customers who have been paying their fixed costs, including those with low-income, will not see an effect from a change in rate design. *In re Duke Energy Ohio,* Case No. 07-589-GA-AIR (Opinion and Order at 19) (May 28, 2008).

The record shows that many low-income customers will be benefited. The average annual usage of PIPP customers, historically, has been over the break-even level of 100 Mcf. For example, the average natural gas consumption of PIPP customers in the period 2000 through 2007 was 144.43 Mcf. Staff Ex. 3 at 7 (S. Puican Prefiled Dir. Test.). In the test year, the average usage level of PIPP was approximately 131 Mcf. Tr. IV at 19-20. Accordingly, the record demonstrates that many customers with low-income have been overpaying their fixed costs and they will be benefited by a change to the straight-fixed-variable rate.

V. The straight-fixed-variable rate design does not result in a disincentive for customers to conserve.

Some have alleged that the straight-fixed-variable rate design discourages conservation. Based on this claim, some also allege the straight-fixed-variable rate violates Revised Code provisions promoting conservation. The claims are not true. The straight-fixed-variable rate design does not discourage conservation.

As Mr. Puican explained, "customers make conservation decisions based on their total bill." Staff Ex. 3 at 4 (S. Puican Prefiled Dir. Test.). The largest component of that bill is the cost of natural gas. *Id.* The gas cost rate is many times greater than the distribution rate. *Id.* at 3. For example, Mr. Puican noted, "Dominion's annualized gas cost rate over the test year period was $9.1228 per Mcf." *Id.* The Staff Report proposed a volumetric rate of $0.36495 for up to 50 Mcf per month and $0.62 for each Mcf thereafter. *Id.* Dominion's proposed rate was $1.62 per Mcf. *Id.* Accordingly, the annualized gas cost rate was approximately 25 times greater than the Staff Report's volumetric rate up to 50 Mcf and approximately 15 times greater than the Staff Report's volumetric rate for each additional Mcf. The annualized gas cost rate, also, was approximately 6 times greater than the volumetric rate Dominion proposed under the current rate structure. As this comparison shows, whatever distribution rate is ultimately approved in this proceeding will be relatively small in comparison to the cost of gas. *Id.* at 3-4. Accordingly, the cost of natural gas is the largest factor, by far, in conservation decisions.

"Customers will always achieve the full value of the gas cost savings regardless of the distribution rate," as Mr. Puican noted. *Id.* The savings in the cost of natural gas drive the size of bills and, accordingly, conservation decisions. The rate design does not affect them and, for that reason, it will not have a significant affect on conservation decisions.

A change in consumer's total bill due to a change in distribution rate design should not have a chilling effect on conservation decisions. The largest component of those bills, natural gas cost, is volatile. *Id.* at 4. For example, those costs increased every month from January, 2008 through July, 2008. *Id.* In one month the increase was $1.70 per Mcf., and that was greater than a15% increase from the prior month. *Id.* The entire period experienced a $5.93 increase, approximately a 69% increase. *Id.* Such fluctuations led Mr. Puican to conclude, "Given these types of extreme fluctuations, I believe customers recognize the imprecision of any payback analysis and will incorporate that uncertainty into their energy efficiency investment decisions." *Id.* Accordingly, the change to a straight-fixed-variable rate structure can not be expected to adversely affect consumer conservation investment decisions.

Rather than impede investment decisions, the straight-fixed-variable rate design will benefit them because it sends better price signals. Including fixed costs in a variable rate distorts price signals. *Id.* Since the straight-fixed-variable rate design aligns fixed costs with fixed rate components and variable costs with variable rate components better than the current rate structure, it provides better price signals for consumers' investment decisions. *Id.* Mr. Puican explained:

> The variable rate component of rates should reflect a utility's true avoided Costs, *i.e.* the costs that a utility does not incur with a unit reduction in sales. The SFV [straight-fixed-variable] rate design satisfies this condition by more closely matching fixed and variable cost recovery to those actual costs incurred. Artificially inflating the volumetric rate beyond its cost basis skews the analysis and will cause an over-investment in conservation.

Id. The straight fixed variable rate design provides better information and results in more informed consumer decisions. That is a benefit, not a detriment, to consumers and conservation.

In that fashion also, the straight-fixed-variable rate design eliminates a disincentive for Dominion to promote energy efficiency. Mr. Puican explained that any gas distribution utility has a disincentive to promote energy efficiency when its must recover its fixed costs through volumetric rates. *Id.* He stated:

> To artificially require the Company to recover its fixed costs through the volumetric rate creates a disincentive for the Company to promote energy efficiency. Staff is proposing a rate design [straight-fixed-variable] that eliminates this disincentive. The relatively small potential disincentive for customers to conserve due to the volumetric rate is more

> than offset by the removal of the Company's disincentive to actively promote and fund energy-efficiency.

Id. Even if some small potential disincentive was associated with the straight-fixed-variable rate design, it is more than offset by the removal of the company's disincentive to promote and fund energy-efficiency. *Id.*

For these reasons, the straight-fixed-variable rate design encourages conservation, contrary to the claims of some. Accordingly, it is in accord with state policy and it does not violate any provision of the Revised Code encouraging conservation.

VI. The straight-fixed-variable rate design proposal incorporates the rate design principle of gradualism.

Some have suggested the Commission proceed more slowly in adopting a straight-fixed-variable rate design. They have suggested studies and other time-consuming activities. Staff believes those proposals are not necessary for the reasons expressed in its briefs. As discussed, the straight-fixed-variable rate design more appropriately aligns fixed costs with fixed rate components and better reflects the fixed costs customers should incur. Additionally, this rate design does not affect recovery of the principle cost that drives a consumer's bill. Accordingly, Staff does not believe a slower approach is warranted.

Moreover, the straight-fixed-variable proposal incorporates the principle of gradualism as discussed in Staff's merit brief. The proposal leaves a portion of the fixed costs in the variable rate component and it phases-in the transfer of fixed costs from the variable to the fixed rate component over two years. Staff believes the two-year period should not be changed.

CONCLUSION

For all the reasons discussed in this brief and the Staff's merit brief, Staff recommends the Commission approve the straight-fixed-variable rate design.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true copy of the foregoing Reply Brief submitted on behalf of the Staff of the Public Utilities Commission of Ohio was served via regular U.S. mail, postage prepaid, upon the following parties this 16th day of September, 2008.

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