



Richard Riazzi
President and Chief Executive Officer

411 Seventh Avenue | Pittsburgh, PA 15219
Tel 412-393-1150 | Fax 412-393-1190
rriazzi@duqlight.com

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Written Testimony on Behalf of Duquesne Light Company

Submitted to the House Consumer Affairs Committee

Re: Support for House Bill 1782- Alternative Ratemaking

Chairman Godshall, Chairman Caltagirone, and Members of the Committee:

On behalf of Duquesne Light Company, thank you for the opportunity to provide written comments detailing our support for Representative Delozier's alternative ratemaking proposal, House Bill 1782. Duquesne Light is an electric distribution company (EDC) providing service to nearly 600,000 customers in Allegheny and Beaver Counties, including the City of Pittsburgh. We sincerely appreciate the Committee's willingness to hold a hearing on alternative ratemaking, as well as Representative Delozier's efforts to put forth a strong proposal that we are pleased to support.

Traditional Ratemaking and the Need for a Modernized Approach

To understand the significance of the concepts contained in HB1782, it is important to first generally discuss current ratemaking methods and frame the problem that HB1782 seeks to address. As regulated utilities, EDCs' rates, investments, and returns are regulated by the PA Public Utility Commission (PUC). Through the rate case process, the PUC approves a utility's revenue requirement, which is the amount that a utility is allowed to collect from ratepayers in order to cover reasonable expenses and earn a fair return on capital investments. Under the current construct, utility revenue requirement from residential customers is largely collected through volumetric rates, or throughput. This means that the more customers use, the more they pay. Conversely, it means customers pay less for less usage.

On its face, the current construct may seem equitable, and DLC agrees that well-designed rates align usage with cost. However, the traditional approach is outdated and is a disincentive for utilities to encourage and promote alternative and efficient uses of the distribution grid. Many of our costs, such as grid infrastructure, are fixed, and remain the same regardless of the volume that customers use. So as customers become more efficient, either through technological advances in energy efficient appliances, or customer education and smarter energy use, they are using less volume. While these actions result in energy conservation and lower bills, it can pose a serious concern for sustainability of the grid. Traditional ratemaking ignores these evolving uses of the

grid, and does not account for the fact that the majority of costs to a utility to serve these customers and maintain the grid in a safe and reliable manner remain the same.

The problem is brought into even sharper focus when one considers newer technologies like solar panels or other forms of distributed generation. Customers who install solar panels use less energy from the grid when the panels are generating electricity, but those customers still require a connection to the broader distribution grid so that they have power at night and on cloudy days. Further, solar customers who net meter are not only using less volume, but are also selling energy back to the grid. Thus, these and other net metering customers need a connection to the distribution system in order to put their generated power back onto the system and get compensated for it. So, again, these customers are using less volume from their EDC, but the utility's fixed costs to serve them remain the same. So if these customers are paying less via volumetric charges billed by their EDC, the majority of fixed costs to maintain the grid for this use are shifted to other customers. This shift arguably most directly impacts low income customers, as DLC believes that most of our low income customers would be unlikely to install solar panels or other forms of distributed generation. These customers would be constrained not only by their income level but also by the fact that a majority of our low income customers are renters, which limits their ability to install distributed generation.

Alternative Ratemaking- House Bill 1782

It is clear that technological advances and fundamental shifts in the way that customers use the distribution grid require a modernized approach to ratemaking, which is precisely what HB1782 provides. The bill authorizes the PUC to approve, but does not require, use of alternative ratemaking mechanisms by electric or natural gas distribution companies. Rather than a "one-size-fits-all" approach, the bill authorizes a range of mechanisms from which companies can choose. Importantly, the bill still contemplates and requires PUC review and approval before implementation of any mechanism.

Perhaps the most well-known alternative rate mechanism is revenue decoupling, which disassociates a utility's profits from volumetric throughput. It instead relies on a formulaic rate of return aligned with revenue targets, and then rates are typically adjusted up or down at the end of an adjustment period. Other examples of alternative ratemaking mechanisms include performance based rates, which provide incentives for over-performance, and penalties for under-performance. This approach focuses on delivering results rather than recovering costs, which aligns goals of utilities, regulators and customers. Formula rates set the upcoming year's rates based on the previous year's expenses, through a predetermined formula derived from the utility company's costs, and a reasonable rate of return. Multi-year rate plans set a utility's base rates for longer than a single 12-month period, and then specify rates beyond the year of a rate case using a formula, index or forecasts for allowable changes over the plan period.

We appreciate that HB1782 contains flexibility and does not require a specific rate mechanism, which will allow utilities to explore innovative ways to sustainably fund the grid. It is critical to

note that the service territories of each EDC are very different, both geographically and with regard to our respective customer bases. Duquesne Light's customer base is approximately 89% residential, 25% of whom are low-income and only about 5% of whom use electric heat. The profiles of each company are different and as such, each EDC would likely take a different approach to the alternative ratemaking mechanisms it would file.

All of the previously-discussed examples would allow utilities to better align the costs of service with the way in which the distribution system is actually being used. It is not possible to state at this juncture which of these approaches is preferred or the singular "best" method, as utilities have not had the opportunity to implement them and review their impacts. This legislation allows utilities to implement alternative ratemaking mechanisms in a responsible and measured manner, after PUC review and approval and with the assurance of continued PUC oversight.

As general principles, Duquesne Light believes that alternative rate designs should: result in just and reasonable rates; provide rate stability, simplicity, and fairness to customers; reflect the impacts of energy efficiency programs on volumetric throughput as they happen, rather than waiting for a base rate case; be implemented gradually to mitigate rate impacts, address unintended consequences, and allow for customer understanding and adoption; give EDCs revenue stability; and minimize cross-subsidization. We are confident that the approach to alternative ratemaking in HB1782 will allow us to realize these results.

Conclusion

In summary, it is clear that the way in which customers use the distribution system is changing. It is crucial that utilities have flexibility in ratemaking so that they can support and encourage innovation while also ensuring grid sustainability. It is absolutely critical that utilities have the ability to better align rates with the cost of providing service, so that as customer use of the grid evolves, we can eliminate unfair cost-shifts and increased costs to other customers. Approval of alternative ratemaking mechanisms will help ensure that utilities can eliminate cross-subsidization and encourage energy efficiency and new technologies, all while ensuring that the grid is sustainably and reliably maintained.

I commend the Committee for its willingness to thoroughly discuss and vet this issue, and Duquesne Light stands ready to assist in any way in which we can be helpful. Please feel free to contact us at any time by reaching out to Lauren Barr Katarski, Manager of Government Affairs, at (412) 393-6232 or lkatarski@duqlight.com

Thank you for your consideration, and for the opportunity to provide Duquesne Light's perspective.

Rich Riazzi
President and CEO
Duquesne Light Company