PROJECT NO. 39829

RULEMAKING TO ESTABLISH BILLING DEMAND FOR CERTAIN UTILITY CUSTOMERS PURSUANT TO PURA §36.009	**§**	**PUBLIC UTILITY COMMISSION OF TEXAS**

ORDER ADOPTING §25.244
AS APPROVED AT THE MAY 18, 2012 OPEN MEETING

The Public Utility Commission of Texas (commission) adopts new §25.244, relating to Billing Demand for Certain Utility Customers, with changes to the proposed text as published in the *Texas Register* (37 TexReg 1047) on February 24, 2012. The rule provides for the waiver of demand ratchet provisions in the approved tariffs for certain customers of transmission and distribution utilities (TDUs), pursuant to House Bill 1064 of the 82nd Legislature, Regular Session in 2011 (HB 1064). Project Number 39829 is assigned to this proceeding.

The commission received written initial and/or reply comments on the proposed rule from AEP Texas Central Company (AEP-TCC), AEP Texas North Company (AEP-TNC), CenterPoint Energy Houston Electric (CenterPoint), and Texas-New Mexico Power Company (TNMP) (collectively, Joint Utilities); City of Houston (COH); Oncor Electric Delivery Company LLC (Oncor); Southwestern Public Service Company (SPS); the Steering Committee of Cities Served by Oncor (Cities); Texas Industrial Energy Consumers (TIEC); Texas Energy Aggregation LLC (Texas Energy); Texas Energy Professionals Association (TEPA); Texas Baptist Christian Life Commission (the Christian Life Commission); Texas Impact (Texas Impact); and TXU Energy Retail Company LLC (TXU Energy). Additionally, Chairman Byron Cook of the House

Committee on State Affairs and State Representative Charles "Doc" Anderson filed comments, and Aaron Gregg, an aide to State Representative Jim Pitts, provided comments at the public hearing on the rulemaking. Representative Pitts also filed comments prior to the publication of the proposed rule.

Public Hearing

On March 28, 2012, at the request of the Christian Life Commission and Texas Impact, commission staff conducted a public hearing in this proceeding. Parties' statements at the public hearing were generally similar with their filed written comments, but where different are noted below.

General Comments

Texas Impact and Texas Energy commented that HB 1064 is intended to "grant demand charge relief to small nonprofits, churches, and other similarly situated entities whose seasonal or occasional usage peaks trigger an artificially high demand charge." Texas Impact commented that the proposed rule would, in fact, grant relief to congregations as well as other low-load-factor customers adversely impacted by demand ratchets, and it also indirectly presents an opportunity to send a proper pricing signal and correct intra-class subsidization in a utility's next rate case.

Oncor and Joint Utilities commented that they would stress that the intent of the legislation was to remove the ratchet billing mechanism for certain customers, and it was not to guarantee either a rate reduction for low-load-factor customers or provide them

"relief from demand charges." Joint Utilities pointed out that the aide to Representative Pitts, the primary author of the legislation, stated in the public hearing that lowering customers' bills was not the intent of the legislation; rather, the intent was to bill monthly demand charges based on actual demand and not on the basis of the highest demand during a 12-month period. Oncor stated that the impetus behind the legislation was customer confusion and dislike with respect to the billed kilowatt (kW) demand being more than actual demand in those months when the ratchet provisions had effect. Oncor provided an example where seasonal customers with 30 kW of load in the summer objected to or did not understand why they were billed 24 kW in demand during the winter months when their actual demand was much below that level, or even zero. Oncor submitted that nothing in the statutory language suggests that total annual billings would go down.

Cities commented that they supported the legislation that required the commission to implement ratchet waivers based on load factor. Cities stated that low-load-factor customers face the most significant bill impacts from ratcheted billing demand rate structures, and that in many instances these low-load-factor customers have monthly peak demands that are off-peak relative to the system. Cities commented that, as a consequence, the ratchet may require the customer to pay monthly bills based on a non-summer month or weekend or night-time peak, even though such customer peak periods are unlikely to contribute to congestion on the distribution system. Cities contended that there is little relationship between ratchets and cost causation, and ratchets do not recognize the system benefits related to the off-peak nature of many municipal loads such

as lighting for ballparks, flood water pumping, or night-time water pumping. Cities stated that, as evidenced by the coincidence-factor data filed in this project, the lower load-factor customers are much less likely to have maximum demands that contribute to system peak demand than the high-load-factor customers, and the legislation provides relief to low-load-factor customers because these customers have encountered the most significant bill increases from a ratchet rate structure.

In response to the public hearing comments by a staff member of the office of Representative Jim Pitts stating that the intent of the statute was never to reduce bills for low-load-factor customers currently subject to a ratchet, but that instead, the intent of the legislation was to provide a clearer billing structure for low-load-factor customers, Cities commented that such an interpretation of PURA §36.009 would lead to the establishment of very high kW charges in lieu of a ratchet for those customers eligible for the waiver. Cities commented that they and other consumers have consistently expressed concern about the continuing use of ratchets by utilities since the "unbundled" cost-of-service (UCOS) cases, and that this concern has stemmed not simply from worry that consumers would be confused by bills that contain ratchet charges, but primarily from the unreasonableness of the ratchet charges and the disconnect between the ratchet mechanism and cost causation. Cities submitted that ratchets have constituted an excessive penalty for a customer's maximum use occurring in one month, particularly given the possibility that other months may be of equal or greater concern in terms of congestion on the system, and that as a result, a demand ratchet waiver should not be thought of as a "subsidy" from some members of a class to another. Cities stated that, in

fact, the opposite is true, and noted that they pointed out nearly 12 years ago in the generic UCOS case that high-load-factor customers tend to favor ratchets because they shift cost recovery to customers with load factors that are lower than the class average load factor.

Texas Impact commented that demand charges send a pricing signal to consumers to encourage a reduction of load during system peak demand when electricity is the most expensive, the most polluting, and the system is at greatest risk of rolling blackouts, and to be effective, a customer's peak demand must coincide with the system peak. Texas Impact stated that worship facilities and other off-peak consumers make up a very small market segment, and a rate that sends a proper pricing signal could be beneficial to both worship facilities and, for purposes of resource adequacy, the entire state. Texas Impact commented that although the proposed rule is not a perfect solution for the faith community because of charges based on non-coincident peak (NCP) demand and the off-peak load profile of workshop facilities, the rule reaches a much broader customer base and removes a significant barrier to sending proper pricing signals that incentivize conservation from low-load-factor customers, and this serves to bolster resource adequacy. Texas Impact submitted that under a rate structure that includes demand ratchets (compounded by a rate structure that bases charges on a measurement of NCP demand to customers whose highest demand is achieved on a weekend), little incentive exists for a worship facility to shed load during system peak demand, and that this applies to both the month (charges based on NCP demand) and to the year (demand ratchets). Texas Impact stated that for worship facility consumers, demand ratchets fail to send a

pricing signal that incentivizes the reduction of load during system peak demand, and Cities similarly stated that because of their relation to the provision of essential public services, municipal loads associated with flood control, police and fire protection, and similar services are often out of the municipality's control, and a municipality cannot respond to price signals by modifying its consumption characteristics in the way that commercial customers can. Texas Impact stated that there is an unintended intra-class subsidization that occurs because of both demand ratchets and billing systems based on measurements of NCP demand when applied to off-peak users, and as a result, worship facilities and other off-peak users are paying premium prices for non-premium power. Texas Impact submitted that off-peak users are paying more than their cost of service, and that from the perspective of these off-peak users, the proposed rule does not unfairly shift costs onto other customers within the same rate class, but begins to correct an existing inequity in current rate structures.

Oncor commented that much of Texas Impact's comments deal with system coincident peak (CP) demand, how demand charges serve to send a price signal to reduce load during system peaks, and the minor impact of worship facilities on system peak demand. Oncor stated that such comments, while perhaps useful with respect to generation-related demand charges and peak demand reduction goals, are misplaced as applied to distribution facilities and demand charges, and Oncor suggested that Texas Impact may not fully understand how costs are incurred and rates are designed for TDUs such as Oncor. Oncor stated that distribution facilities must be, and are, sized to meet the customer's NCP load, irrespective of when that NCP occurs, and that if the NCP demand

for a customer is 30 kW, then the facilities must be sized for that NCP demand. Oncor stated that it does not matter whether that customer's NCP demand occurs during the hottest day in August when the system hits its peak for the year, on an unusually warm Easter Sunday in April, or on unusually cold Christmas Eve in December. Oncor asserted that the relative contribution, or lack thereof, of low-load-factor worship facility customers to the system peak in August has basically nothing to do with setting demand charges (ratcheted or otherwise) for distribution service to customers. Oncor stated that distribution charges are not meant to be a price signal, but instead are charged on a demand basis in order to reflect the fixed nature of the facilities used to meet the customer's NCP requirements. Oncor submitted that Texas Impact's statement that "worship facilities, and other off-peak users, are paying premium prices for non-premium power….Off-peak users are paying more than their cost of service" is simply wrong as applied to setting rates for a TDU such as Oncor.

Similar to Oncor's comments, Joint Utilities stated that, with regard to Cities' comments that the load of low-load-factor customers is unlikely to contribute to congestion on the distribution system, such a conclusion results from an inappropriate leap in logic. Joint Utilities submitted that the Cities incorrectly insinuate that only a customer's maximum demand contributes to the system peak demand and because low-load-factor customers may be peaking at time other than the system peak, they are not contributing to congestion on the distribution system. Joint Utilities contended that this is an incorrect argument because any load at the time of the system peak is contributing to congestion on the distribution system. Joint Utilities noted that the coincidence-factor information cited

by Cities actually shows that for 25% or lower load-factor customers, approximately 50% of the maximum demand is applicable at the time of the system peak and, therefore, low-load-factor customers are contributing to congestion on the distribution system. Joint Utilities commented that data show that as you increase the load-factor level, the amount of usage that occurs on peak increases significantly. Using data for CenterPoint Energy as an example, Joint Utilities stated that at a 25% load-factor level, the coincident ratio of NCP to the average of coincident peak demand in the Electric Reliability Council of Texas (ERCOT) area for the four months of June, July, August, and September Four Coincident Peak (4CP) is 56%, but at a 40% load-factor level, the coincident ratio rises to 83%, indicating that the vast majority of the customer's load is occurring at the time of the system peak. Consistent with Oncor's comments, Joint Utilities stated that it is important to note that distribution facilities are sized to meet the maximum demands of the individual customers as well as when that demand occurs relative to the system peak, and the distribution ratchet is designed to reflect the costs of providing distribution service and the way the distribution system is used. Joint Utilities commented that distribution facilities are fixed-cost facilities that are planned and constructed to meet local or individual peak demands regardless of the relationship of that point in time to the time of the system peak, and gave the example of a distribution line serving end-use customers that is sized to meet the maximum load likely to be imposed by those end-use customers, regardless of when it occurs. Joint Utilities commented that individual customer peaks, along with system peaks, are an important consideration in the design of distribution system charges, and that Cities' comments disregard the way the distribution system is designed and used by end-use customers.

TEPA commented that applying a demand ratchet to a low-load-factor customer can artificially increase a customer's bill by a significant amount. TEPA stated that for low-load-factor customers, the use of a billing demand, rather than actual demand, can produce a significant increase in the cost for which a customer is billed in a given month, and when these artificially inflated demand charges are spread over the relatively small amount of energy consumption that is characteristic of low-load-factor customers in periods of low or no consumption, the effect is to create an unusually high cost per kilowatt-hour (kWh). TEPA commented that the current ratcheted billing provides a disincentive to a customer to invest in energy efficiency measures because the customer cannot realize the savings of that investment for 11 months. TEPA provided the example of a customer that makes an investment in a high efficiency air conditioning (AC) system to lower that customer's demand and consumption. TEPA stated that such a customer would not see the reduction in demand-related costs on his electric bill attributable to his investment for 11 months. TEPA stated that with a change to billing based on the actual demand, the customer can start seeing the reduction in demand and TDSP charges the month after the efficient air conditioners are installed, and this type of change should encourage additional investments in energy efficient equipment and enhance the resource adequacy goals of ERCOT.

Oncor disagreed with TEPA's example, stating that if the customer's previous peak demand had occurred in the previous August, such an installation in May of a given year will likely result in lower demand-related billing beginning in August or September—the first billing period that the ratchet is calculated under the new, lower peak demand—

which is a period of three or four months, not 11. Oncor stated that, in fact, it is possible the customer would see a benefit in the very next month—it would be realized on the customer's bill once the customer's demand exceeded the 80% ratchet level because at that point the ratchet would not apply, and the actual billed kW demand would be lower than it would have been without the AC unit. Oncor further stated that TEPA's claim that, "with a change to billing based on the actual demand, the customer can start seeing the reduction in demand and TDSP charges the month after the efficient air conditioners are installed" overstates the argument. Oncor stated that this claim would only be true in a month that the customer utilizes air conditioning (i.e., a system purchased in January will probably not reduce the customers actual demand in January). Oncor submitted that, ultimately, the investment analysis behind an AC purchase (an investment with a 10 to 20 year life) should not be made by over-emphasizing the economic benefits of the first several months of the asset life. Oncor stated that TEPA's argument totally ignores the fact that Oncor's load-factor rate uses actual kW and the customer would realize savings in the billing month immediately following the installation of the energy efficient equipment.

Oncor additionally commented that TEPA's comments that the use of demand ratchets results in "artificially inflated demand charges" ignores the cost-of-service aspects inherent in the development of the class demand charges. Oncor and Joint Utilities stated that class demand charges are designed to recover a fixed number of dollars (i.e., the demand-related costs of a given class), and this can be accomplished using monthly actual demands or monthly billing demands based on a demand ratchet. Oncor and Joint

Utilities commented that rates designed using monthly actual demands are based on fewer billing units and, consequently, a higher stated demand charge ($/kW) than rates that include a demand ratchet. Oncor and Joint Utilities noted that a ratchet simply changes the timing of the recovery of the costs charged to the class, not the total amount of costs to be recovered. Joint Utilities stated that the higher the load-factor threshold is set, the greater the impact on the rates of all nonresidential secondary voltage customers, because the greater number of customers exempt from the ratchet, the greater the amount of costs that must be collected from customers to make up for the foregone ratchet.

With regard to the basic purpose of HB 1064, and in response to a specific question from commission staff at the public hearing on March 28, 2012, about whether the legislation's intended relief was a reduction in the total charges paid by affected customers or, more simply, a reduction in the customer confusion related to the use of ratchets, Aaron Gregg, an aide to Representative Pitts, stated that, "I guess, just to kind of clarify, the intention of the author of the bill was—it was brought to us by a group of small school districts, and they were kind of the original reason that my boss got involved with this. From our perspective, to answer your question, was that relief in the terms of 'they would not get an unexpected charge in the middle of the summer' or whatever time of the year that they had not planned for in their budgets; relief not in the sense of a reduction in overall costs, but a relief in the sense of more predictability in their bill. That's the understanding that we've been operating under the entire time we've been working on this."

Commission Response

Parties' general comments largely address the conceptual basis of demand ratchets and the merits of their use in developing electric rates, which are issues that exceed the scope of this rulemaking. PURA §36.009(a) provides that the commission by rule shall require a transmission and distribution utility to waive the application of demand ratchet provisions for each nonresidential secondary services customer that has a maximum load factor equal to or below a factor set by commission rule. The rule adopted herein implements that requirement. To the extent that parties' general comments include specific points related to the development of an appropriate load-factor threshold, the commission takes into account these points in the discussion below.

Comments on Specific Sections of the Proposed Rule

Section 25.244(a): Application

Oncor commented that there are several places where the proposed rule refers to "retail distribution service." Oncor recommended the replacement of that phrase with "retail delivery service" so that it would be consistent with the provision of service through the Tariff for Retail Delivery Service. Oncor submitted language pursuant to this point.

Commission Response

The commission declines to make Oncor's proposed change. The use of "distribution" indicates that the rule does not apply to TDUs that provide service only at transmission voltages. The term "distribution service" is also used in the

applicability statement in §25.243(a) of this title (relating to Distribution Cost Recovery Factor (DCRF)).

Cities noted that the proposed rule states that "a demand ratchet shall not apply to a nonresidential secondary voltage service customer that has an annual load factor less than or equal to 25 percent." Cities expressed concern that this language may be interpreted as requiring a demand ratchet for all customers with a load factor greater than 25%, even if the customers are currently subject to a ratchet exemption. Cities commented that such an interpretation was not intended in the draft rule, and provided modified rule language addressing this point. TEPA stated similar concerns and supported the clarifying language that the rule is only applicable to the TDUs requesting the use of a ratchet.

Commission Response

The commission agrees and has added a sentence to subsection (c) to address this issue.

Section 25.244(b): Definitions

Oncor commented that two abbreviations in the proposed rule should be changed to conform to industry standards: "KW" should be changed to "kW" and "kVa" should be changed to "kVA."

Commission Response

The commission agrees and has modified the language accordingly.

Section 25.244(c): Rates

25% Load-Factor Threshold

TXU Energy expressed its support for the rule, stating that the modifications proposed in this rulemaking to eliminate demand ratchets for nonresidential secondary voltage service customers with load factors less than or equal to 25% are consistent with the requirements of HB 1064 and should assist retail electricity provider (REP) call centers in their efforts to explain demand billing to customers. TXU Energy stated its belief that the impact of the commission's decision in a recent Oncor rate case demonstrates that the elimination of a demand ratchet for low-load-factor customers will lead to a more positive customer experience. TXU Energy commented that in that rate proceeding (Docket No. 35717), the commission approved rates for Oncor that apply a demand ratchet for nonresidential secondary voltage service customers only if such customers have a load greater than 20 kW, and that in Oncor's subsequent rate proceeding (Docket No. 38929), the commission approved a modification to the nonresidential secondary voltage service customer rates to eliminate the demand ratchet for customers with loads greater than 20 kW if the annual load factor for those customers is less than or equal to 25%. TXU Energy stated that its experience with customers following the elimination of the demand ratchet for all nonresidential secondary voltage service customers with a load factor less than or equal to 25% has been a generally positive one, indicating a reduction in customer confusion and complaints.

Texas Impact stated that it has no recommendation as to the exact load-factor percentage, but expressed its desire that the exemption threshold include as many of its members as possible. Texas Impact stated that it recognizes that a higher load-factor threshold means increasing the total number of eligible customers, thus depleting the number of high-load-factor customers to which the ratchet is still applicable and from whom the utility would be able to recover costs, but given that a 25% load-factor threshold encompasses 90% of its membership, Texas Impact stated that it is very supportive if this load-factor percentage reflects the appropriate balance of those considerations.

Chairman Cook stated his belief that the 25% threshold should help address current concerns about varying rates and would provide relief to a substantial number of customers currently being affected by demand-ratchet charges. The Christian Life Commission also expressed its support for the proposed 25% threshold, and Texas Energy supported the comments of the Christian Life Commission and Texas Impact that the load-factor ceiling should not exceed 25%. Texas Energy further stated that the ceiling should not be less than 15%.

Cities and TEPA commented that although the 25% threshold is not necessarily unreasonable, it could be increased to a somewhat higher level without a significant adverse impact on other customers. Cities stated that for the four largest utilities, increasing the load-factor percentage from 25% to 30% would provide relief from the demand ratchet to more than 27,000 customers, but would be accompanied only by a

relatively small incremental change in the percentage of class load subject to a ratchet. Cities stated that for the two largest utilities (CenterPoint and Oncor), a 30% load-factor threshold would result in excepting 40% or less of the class monthly demand from the ratchet rate structure and, furthermore, a 30% load factor is clearly a low load factor relative to the average load factors for secondary >10 kW customer classes. Cities stated that increasing the load factor threshold to 30%, from the proposed 25%, is consistent with the intent of the Texas Legislature (Legislature) to provide relief from demand ratchets to low-load-factor customers.

TEPA commented that the load-factor threshold for application of the waiver should be increased from the 25% contained in the proposed rule to 35%. TEPA submitted that many of the intended beneficiaries of this rule have load factors that are above 25%, and stated that data on the load characteristics of a sample of churches provided by Texas Impact revealed that, although the majority of the accounts have load factors of 25% or below, 10% of the accounts have load factors above 25%. TEPA stated that 30% of the energy consumption of these churches is attributable to accounts with load factors above 25%, and although the data on churches are not comprehensive, extending eligibility for the ratchet waiver to customers with load factors less than or equal to 35% would increase coverage of the sample of church accounts from 70% to 97%. TEPA further stated that data provided in this project have revealed that approximately 40% of their clients' accounts have load factors greater than 25%, and increasing the load-factor threshold to 35% would increase the coverage for the meters represented in the data from 63% to 84%.

TEPA additionally commented that what constitutes a "low" load factor is subjective but that there are several reasons that the threshold should be increased above the proposed 25%. First, ERCOT has defined low-load-factor customers as those with load factors below 40%. In addition, establishing the threshold for the ratchet waiver at 25% would have detrimental effects on customers with load factors just above the threshold. TEPA stated that because the waiver of the ratchet is intended to not impact customers outside the nonresidential secondary voltage service class, the revenue previously associated with the imposition of a ratchet must be recovered from customers within this class. TEPA noted that the imposition of a ratchet results in the billing units for billing demand being greater than those for actual demand, and waiving the demand ratchet for certain customers will result in fewer total billing units because some of the billing units that were created by the ratchet will be eliminated. TEPA commented that to recover the same amount of revenue without affecting other rate classes, the original rates must be increased to recover the same amount of revenue from the reduced number of billing units. TEPA commented that the resulting small increase in the demand rate for all customers is offset by the reduction in billing demand for customers that are eligible for the waiver, but customers that are above the threshold continue to have the same amount of billing demand and would be subject to a higher rate that causes their bill to be higher than before. TEPA stated that a review of the data reveals that this negative impact on customers that are not eligible for the ratchet waiver becomes less pronounced as the load-factor threshold is increased, and although the 35% load-factor threshold has less benefit for extremely low-load-factor customers than a lower load-factor threshold, the

difference is slight, and the higher threshold spreads the benefits of the waiver to a greater number of customers. TEPA recommended that the ceiling/threshold for application of the ratchet waiver be set at an annual load factor of 35%, as setting the threshold at this level would benefit the greatest number of customers while minimizing negative impacts on other customers.

Representative Charles "Doc" Anderson filed comments indicating that ERCOT is on record as saying any load factor below 40% is considered low, and that while that level might bring some consternation to providers who rightly pursue the function of cost recovery for building and maintaining an electrical network, he would recommend the rulemaking process take a look at adopting a load-factor threshold somewhere between the proposed 25% and 40%. Representative Anderson stated that while demand charges overall are a reasonable and necessary component of building and maintaining an electrical network, the burden at the lower end of the load-factor spectrum has an appearance, if not the effect, of disproportionality; further, the lack of relief serves as a barrier to those entities wishing to implement energy-saving capital upgrades in order to take their own steps toward lowering their peak usage and overall usage.

COH stated that it strongly disagrees with Cities, TEPA, and Representative Anderson to increase the load-factor threshold above 25%. COH stated that raising the threshold increases the number of low-load-factor customers and decreases the number of high-load-factor customers in the affected customer class, and the resultant reduction in billing determinants ultimately raises the rate for high-load customers if the class's allocated cost

of service is not treated as it was in Docket No. 38929 in which Oncor's proposed rates were based on a 25% load-factor threshold.

COH expressed support for Staff's recommended 25% threshold, which relies upon data provided in response to Staff's request for information in this project. COH commented that application of the ERCOT 40% threshold is not appropriate, and that ERCOT processes are designed for ERCOT's own particular needs and are not relevant to the rate design associated with TDU distribution function costs. COH stated that TEPA is correct in acknowledging that intra-class rate design is a zero-sum game—changing the rate calculations of one or some customers affects other customers. COH commented that HB 1064 was enacted to provide relief to small-load customers who lack energy expertise primarily because of prohibitive costs to adequately address the demand and consumption of electricity. COH commented that customers with higher demand and usage have the ability to bear the costs of energy management and should not be eligible for reduced demand charges through a waiver simply because they fit a particular customer cost profile such as a church. COH stated that this would most likely shift costs to customers that are billed using demand ratchets. COH stated that should the commission elect to raise the threshold, it supports a rule that allows flexibility in setting the threshold in a TDU's base rate case proceeding. COH agreed with TXUs recommendation for one load-factor threshold for all TDUs to avoid "unneeded complexities," but conversely, if the commission increased the threshold, COH disagreed with TXU's recommendation, unless exception language was included.

Joint Utilities commented that while TEPA cites to the 40% load-factor definition employed by ERCOT and suggests that the exemption be set at a 35% load-factor level, ERCOT uses that definition for its own purposes, and if such a level were to be established in this rule, the commission would not be striking a balance but merely excluding as many customers as possible from the ratchet. Joint Utilities stated that the proposed 25% threshold would result in an exemption from the demand ratchet application for 66% of the nonresidential secondary service customers for AEP-TCC, 65% for AEP-TNC, 54% for CenterPoint, and 61% for TNMP. Joint Utilities stated that increasing the load-factor threshold to 40% increases the percentage of customers exempt from the ratchet to increase to the following levels: AEP-TCC—85%, AEP-TNC—86%, CenterPoint—82%, and TNMP—84%. Based on these data, Joint Utilities observed that a 40% load-factor threshold would virtually eliminate the entire nonresidential secondary service class from the ratchet, and with a load-factor exemption impacting such a large percentage of customers, it may be appropriate to eliminate the ratchet for the nonresidential secondary service customers entirely. Joint Utilities observed that a 20% load-factor threshold limits the number of exempted customers to approximately 50% and reduces the amount of costs previously collected through the ratchet, and might more appropriately balance the goals of the statute. Joint Utilities commented—and TEPA agreed—that the rule should make clear that each TDU has the option of completely eliminating the demand ratchet provision for the nonresidential secondary service customers in the rate design phase of any base rate proceeding. Joint Utilities commented that all exceptions to the proposed rule should be thoroughly examined in the context of a rate review and suggested language indicating this rule is only applicable to

rate design for the secondary distribution classes that have or are proposed to have a demand ratchet.

Commission Response

The commission concludes that a load-factor threshold of 25% is appropriate. This figure strikes a balance between a threshold that is high enough to provide demand-ratchet relief to low-load-factor customers with primarily off-peak usage, but not so high as to affect customers with a large degree of on-peak usage or interfere with a utility's ability to reasonably recover the costs of providing distribution service while avoiding significant intra-class subsidization. Although some commenters suggested increasing the load-factor threshold to as high as 35% to 40%, such higher levels would, according to data from Joint Utilities, virtually eliminate the use of ratchets for the entire nonresidential secondary customer class. The commission notes that HB 1064 does not mandate that demand ratchets be abolished completely. Moreover, as a practical matter, doing so would result in a significant reduction of the class's billing determinants and a potentially dramatic adverse impact on affected customers' rates.

Based on information provided by Joint Utilities, a 25% load-factor threshold would result in an exemption from the demand-ratchet application for 66% of the nonresidential secondary service customers for AEP-TCC, 65% for AEP-TNC, 54% for CenterPoint, and 61% for TNMP—in other words, these percentages indicate that more than one-half to nearly two-thirds of the class's customers would be

exempted from the demand-ratchet mechanism. Taking into consideration the objectives of (1) meeting the statutory requirement to provide a demand-ratchet waiver for low-load-factor customers, (2) precluding inter-class subsidization, and (3) minimizing intra-class cost shifting, the commission concludes that a load factor of 25% provides a reasonable balancing of these goals. The commission agrees with Joint Utilities and TEPA, however, that the rule should not require the use of demand ratchets for any customers. The commission has modified the rule accordingly.

Specific load-factor thresholds for each TDU

Joint Utilities commented that setting a specific load-factor threshold across all TDUs fails to account for differences among the utilities, and this should be considered when establishing an exemption. Joint Utilities recommended that the commission consider the fact that not all TDU territories and mix of customers are the same, and the commission should consider allowing the TDUs a degree of flexibility in setting a load-factor exemption. Joint Utilities commented that if the commission believes, however, that a load-factor threshold should be specifically included in the rule, then a lower threshold should be set and the rule should allow each TDU to establish a threshold in its next rate case that is appropriate for that TDU's service area. Based on the proposed 25% threshold, Joint Utilities commented that, for example, the 66% exemption eligibility produced by application of the 25% ratchet threshold for AEP-TCC is 22% higher than the 54% of eligible customers in the CenterPoint service area, and this variance illustrates why a "one size fits all" approach is not the optimal strategy and demonstrates why the

commission should retain the flexibility to set the exemption level at an appropriate level in a TDU's rate case proceeding.

Joint Utilities further noted that the higher the threshold, the greater the impact on the rates of all nonresidential secondary voltage customers, because there will be a reduction in billing determinants used in the development of the nonresidential secondary rates due to elimination of the ratchet. Joint Utilities suggested that keeping flexibility in the rule is reasonable and allows for specific utility cost and load data to be examined prior to establishing a demand ratchet threshold that will impact the rates of other customers. Joint Utilities additionally noted that Representative Jim Pitts filed comments on December 16, 2011, indicating that the commission should retain some flexibility to recognize the different aspects of differing service territories. Specifically, the letter filed by Representative Pitts stated that, "as the bill's author, I would like to provide guidance on legislative intent…" and that it is "…important to allow some flexibility, if needed, to recognize the unique aspects of each transmission and distribution utility."

Cities commented that to the extent the Joint Utilities argue for setting a different load-factor threshold in each rate case, their proposal is not consistent with the law. Cities stated that PURA §36.009(1) specifies that the exemption be based on a "maximum load factor to or below a factor set by commission rule," and this language clearly instructs the commission to implement a rule that sets one load-factor threshold. Cities stated that nothing in the law supports multiple load-factor thresholds or different thresholds set in each utility's rate case, and the implementation of a uniform load-factor threshold is also

consistent with the commission's decision to develop uniform customer classes and rate designs for unbundled TDUs, and this avoids customer confusion and rate complexity. Cities commented that the commission's policy has favored uniformity in TDU rate structures to facilitate retail competition, and that uniform rate structure terms allow retail electric providers to offer similar commercial rate offerings in multiple service territories. With respect to Joint Utilities' comments that TDUs should be allowed the option of eliminating the ratchet entirely for non-residential secondary classes, Cities stated that they have no objection to clarifying that the rule does not prevent a utility from complying with the law by abolishing ratchets in the secondary class. Cities submitted that a secondary greater than 10 kW class with an exceptionally low class-load factor may be a candidate for ratchet elimination, particularly if a large proportion of the class falls below the load-factor threshold set in the rule.

TXU Energy stated its support for applying one threshold load factor for all TDUs for demand ratchet waivers instead of thresholds that would vary among TDUs, observing that if the threshold for demand ratchet waivers were to vary by TDU, both customers and REPs would face unneeded complexities. Customers having service addresses in multiple TDU territories could see their bills substantially vary based on higher or lower demand ratchet waiver thresholds even if their usage among service addresses remained relatively consistent. TXU Energy additionally noted that REP call centers would be burdened because customer care personnel would need to be trained to understand and explain different demand billing parameters by TDU territory.

TEPA stated its agreement with TXU Energy on the arguments for applying one threshold load factor for all TDUs. TEPA further commented that contrary to Joint Utilities' comments that a 25% "one size fits all" approach is not optimal, the data from Joint Utilities that 54% to 64% of customers fall within that threshold actually demonstrate remarkable consistency among TDUs and are further evidence that a single threshold is reasonable and appropriate for application to all TDU service areas.

Joint Utilities replied that the commission is charged with establishing just and reasonable rates to be charged by each TDU based on its costs, that rates across TDUs and REPs already differ, and that REP call centers already deal with those differences by using scripts tied to the TDU serving the area in which the customer is located. Joint Utilities stated that TXU Energy's arguments are not sufficient to justify imposition of a uniform threshold on a TDU that can show the commission that valid reasons support a deviation from the threshold established in the rule, and suggested language providing flexibility to the setting of a TDU's load factor.

Commission Response

While the commission agrees with the comments of TXU Energy and Cities that avoiding customer confusion is desirable, the commission notes that some degree of rate and billing variability for different TDUs already exists and the use of demand ratchets is but one factor that may contribute to this variability. The commission agrees with Representative Pitts and Joint Utilities that allowing the commission to have flexibility is important when considering the unique circumstances of each

TDU's service territory, and the adoption of a load-factor threshold higher than 25% may therefore be appropriate if the commission finds doing so reasonable in the context of a comprehensive base-rate proceeding. Factors underlying the commission's consideration of setting a higher threshold in a base-rate proceeding may include, at a minimum, the number of additional customers that would be exempted from the demand ratchet, the concomitant degree of intra-class cost shifting and how this could be minimized (for example, with the use of a tiered intra-class rate design as has been used by Oncor), and a justification of how the benefits of a different threshold would outweigh the potential for increased billing complexity. As noted in the commission's response to comments on subsection (a) of the rule, the commission has added a statement in subsection (c) that clarifies that the rule does not require the imposition of a demand ratchet on any customer. Consequently, parties in a base-rate proceeding are free to advocate for or against the use of a demand ratchet for customers above the 25% load factor established in the rule and the commission has the authority to set rates based on its assessment of those arguments pursuant to its general authority to set just and reasonable rates under PURA § 36.003.

Section 25.244(d)—Annual Verification

Joint Utilities suggested that the annual verification process as described in subsection (d) is unnecessarily overly burdensome and vague. Joint Utilities stated although there appears to be a presumption that the annual verification process would not be easily designed and implemented by the TDUs, and thus stringent verification would be

necessary, this is in fact far from the truth. Joint Utilities commented that since the deregulated market opened, CenterPoint has had a process in which the REPs of end-use customers with differing load factors have been charged differently, a process that was initially developed to deal with Price to Beat headroom issues. Joint Utilities submitted that the fact that a verification process should not be difficult to design and implement, coupled with Representative Pitts' filed comments that the commission should not impose a burdensome process for the annual verification requirement, illustrates why the proposed rule's requirement to attach a thorough description of the procedures is unnecessary. Joint Utilities further commented that no reason exists for the commission to review the computer programming technical "jargon" associated with billing systems, and that a simple affidavit stating that a process has been implemented to comply with the requirements of the rule is more than sufficient to satisfy the PURA requirement. Joint Utilities suggested modified language pursuant to this point.

Oncor commented that it has already implemented a procedure for annual verification, which occurs each December and uses calendar-year data for the verification. Oncor stated that an annual verification process that occurs on the anniversary of the implementation of the rate would be unwieldy and would cause customer confusion. Oncor submitted recommended language consistent with this point.

COH commented that the commission's final order setting base rates must contain specific criteria to determine (1) whether each of a TDU's nonresidential secondary service customers qualifies for a waiver of the demand ratchet, (2) findings on specific

procedures the TDU will use to ensure that the customers to whom a demand ratchet shall not apply are accurately identified and billed, and (3) the form of affidavit the TDU must use. COH stated that the identification, tracking, and reporting of eligible customers is of the utmost importance in implementing the new rule. COH stated that the commission should have enough information to determine the sufficiency of these activities, and that while divulging every detail of the process, such as the computer programming language associated with billing systems, should not be necessary, more information about these activities than an unsubstantiated affidavit must be required and would not be burdensome.

Commission Response

The commission agrees with Joint Utilities and COH that the annual verification affidavit does not need to be so detailed that it includes technical "jargon" or computer programming information. However, the commission disagrees with Joint Utilities that the language in subsection (d) is unnecessarily burdensome and vague and that the rule's use of the word "thorough" is unnecessary. PURA §36.009(2) requires the utility to "implement procedures to verify annually" whether a customer meets the load-factor threshold, and the rule's requirement to simply provide a "thorough description" of such procedures is not burdensome on a utility. Additionally, the word "thorough" is included merely to underscore the requirement that the description of the procedures a utility uses to ensure accurate identification and billing of customers should be comprehensive and complete with regard to important details—that is, it should not be superficial or partial. The

commission concludes that the rule's use of the word "thorough" is reasonable and, accordingly, no modification to the rule is required in this regard.

Regarding the point in time at which the annual verification would occur, the commission agrees with Oncor that the anniversary of the implementation of the rate could result in customer confusion, and therefore the use of calendar-year data soon after the end of December is appropriate for the verification. The commission has accordingly modified the rule using language suggested by Oncor.

Comments on Other Issues

Oncor's Tiered System

Texas Impact and the Christian Life Commission expressed concerns pertaining to how TDUs will choose to implement the proposed rule. The Christian Life Commission stated its concern that the implementation strategy used by Oncor has helped fewer customers than was expected in its service territory, and that because of Oncor's tiered system, customers with lower load-factors, including some houses of worship, are still experiencing higher distribution bills even though they are not placing a greater strain on the distribution system than other customers.

Texas Impact stated that Oncor's current tariff creates a multi-tiered, load-factor-based rate that charges customers based on their maximum NCP at declining rates per kW as the load factor increases. The lowest load-factor customers (under 10% to 15%) most impacted by demand charges are granted less relief than those between (15-25%) who are

less severely impacted by demand charges. Texas Impact commented that this type of tier system should be disallowed. Texas Impact requested that the commission monitor the utilities' implementation of this rule in the next rate case to assure that the 50% of congregations having less than a 15% load factor see equal rate relief because they are hit harder by charges based on a measurement of demand than those congregations that have a load factor exceeding 15%.

TEPA and Texas Energy similarly commented that the rule should prohibit multi-tiered load-factor-based rate structures. TEPA commented that the purpose of the legislation is to make low-load-factor customers' billing dependent on their usage in the current billing period rather than usage in previous periods. TEPA commented that PURA §36.009 explicitly states that "a demand ratchet shall not apply" to a nonresidential secondary voltage service customer with a load factor below a certain amount. TEPA stated that Oncor's multi-tiered, load-factor-based rate explicitly charges low-load-factor customers more than high-load-factor customers, resulting in a very similar effect to the ratchet penalties that currently exist in other utilities' rates but which the commission is attempting to eliminate in this proceeding. TEPA stated that this type of rate structure penalizes low-load-factor customers in several ways, is contrary to the intent of the statute and the proposed rule, and should be prohibited.

Chairman Cook stated that he encourages the commission to adopt a rule that does not include a tiered system in which rates would vary by load factor for affected customers. Chairman Cook expressed his belief that all customers with load factors less than or equal

to the specified threshold should pay the same rate rather than creating subsections within the group of affected customers.

Oncor stated that Texas Impact's complaint that the lowest load-factor customers are not seeing as much "relief" as higher load-factor customers under Oncor's tiered rate approach is wrong, as both sets of customers are being provided the relief of not being subject to a ratchet, and that is the only relief the statute is designed to provide. Oncor stated that the fact that the demand charge for lower load-factor customers is higher, under Oncor's tiered approach, than for higher load-factor customers is simply a result of mathematics: the same revenue requirement is to be recovered from less billing units (actual kW). Therefore, if the cost to serve Customer A and Customer B is equal, because they have equal NCP demands, but Customer A has a 10% load factor and Customer B has a 20% load factor, the per-kW rate for Customer A must be higher than for Customer B, because Customer A has fewer billing units over which to recover the same level of cost. If the rate is the same for both, then Customer B is subsidizing Customer A. Oncor stated that its tiered rate approach is designed to minimize such subsidization and is reasonable. Oncor stated that Texas Impact's proposal to have the commission monitor implementation of the rule such that a certain percentage of congregations with a certain load factor obtain "equal rate relief" is inconsistent with the statute, unreasonable, and should be rejected.

Oncor additionally stated that there is nothing in PURA §36.009 that mandates (or even suggests) a prohibition of multi-tiered, load-factor-based rates, and if the Legislature had

thought tiered rates were inappropriate, it certainly could have spoken to that issue and prohibited load-factor based rates. Oncor pointed out that the Legislature did not, and therefore TEPA's proposal is well beyond the actions that the Legislature required this commission to take. Oncor observed that the statutory language requires the commission to distinguish between customers based on load factors—below a certain load factor, a demand ratchet is not to be applied—and once the ratchet is removed, PURA §36.009 in no way prohibits using the customer's load factor in designing the actual per-kW rate. Oncor commented that once the ratchet is eliminated and the customer is billed only for his actual demand, how to develop a cost-based, per-kW rate for that customer is within the discretion of the commission to determine. Oncor submitted that developing rates using tiers based upon load factors is in no way a ratchet, and is certainly permissible under PURA §36.009, which simply does not address anything beyond "demand ratchet" waivers.

Oncor further commented that the impact of TEPA's separate proposals to: (1) increase the load-factor ceiling from 25% to 35% and (2) eliminate the current multi-tiered load-factor-based rate—in favor of a single rate applicable to all tiers—must be evaluated together. Oncor stated that adoption of these two TEPA proposals would, for Oncor, result in: (1) a large decrease in the number of demand billing units; (2) a lower demand charge for the customers in the lower load-factor tiers; and (3) a higher demand charge for customers in the upper load-factor tiers. Oncor stated that the end result of TEPA's proposals would be a single rate applied to a 0-35% load-factor tier, and this rate would not be appreciably different from a class-wide demand charge based on actual monthly

demands. Oncor asserted that, simply stated, TEPA's proposals—increasing the ratchet exemption to load factors up to 35% and its "one-size-fits-all single tiered rate structure"—would significantly dilute the benefits of Oncor's current rate structure because of the large weighting on class demand revenue from loads in the 25% - 35% load-factor tier, and these impacts would, in large part, defeat the legislative intent of the proposed rule.

Oncor further elaborated that, as the ratchet is waived for more customers, and those customers are put into a single tier and pay the same per-kW demand charge, the more the rate approaches a simple single "actual demand" rate design, with intra-class subsidization issues. Oncor stated that two sets of facts highlight this impact. First, Oncor stated that it currently has the following rate tiers and rates for customers with peak demand greater than 20 kW and a load factor less than 25%:

0-10% load factor: $6.10/kW

11-15% load factor: $5.47/kW

16-20% load factor: $5.16/kW

21-25% load factor: $5.01/kW

Oncor stated that a single per-kW demand charge for these customers would be $5.37/kW; thus, the higher load-factor customers would pay more than under Oncor's tiered approach, while the lower load-factor customers would pay less. Second, for customers with load factors in the 26-35% range, moving them into a single subclass of customers (0-35% load factor), with a single per-kW demand rate that would be

$5.19/kW, would result in almost 80% of those customers paying more on a total annual basis than if the ratchet continued to apply to them. Oncor emphasized that ratchet provisions are not "penalties," and taking load factor into account in calculating rates does not "penalize" low-load-factor customers, but instead recognizes the actual costs to serve each tier of customers, and recovers those costs over the actual billing demand. Oncor stated that TEPA's proposal increases intra-class subsidization—whereby lower load-factor customers would be subsidized by higher load-factor customers—and TEPA's proposal to mandate such an approach should be rejected. Oncor stated in the public hearing that in its current tiered system, a customer within a tier pays only for actual kW, and the customer tiers are grouped in such a way as to minimize the impact on customers within the tiers. Oncor stated that it is not suggesting that every utility must have a tiered rate design—that will likely depend upon the customer characteristics of each utility—but where the commission finds it appropriate for any given utility, a tiered approach should be an available rate design tool.

Oncor stated that the distribution system charges for each load-factor tier are based on the demand-related costs applicable to that tier, and as such, Oncor's rate design for customers in the 21%-25% tier has no effect on the rate applicable to customers with annual load factors greater than 25%. Oncor stated that its rate design for customers in the 0%-10% tier has no effect on the rate design for the 21%-25% tier—or on any other tier. Oncor pointed out that each tier is designed to recover the costs of serving only the customers in that tier, based upon only the kW billing demands incurred by customers in that tier.

Oncor replied that its tiered approach was adopted before PURA §36.009 was adopted, and that it was designed to minimize the number and extent of the "winners" and "losers" caused by the removal of a ratchet and the resultant change in billing units and the kW demand charge. Oncor additionally stated that while it is true that the load factor is calculated based on the previous billing year demand and energy consumption, annually is the appropriate time period to determine the "maximum load factor" as required by PURA §36.009. Oncor stated that using an annual load-factor figure is in no way a continuation of a "ratchet" but simply recognizes that certain customer usage data must be determined on an annual basis in order to properly set rates. Oncor stated that neither houses of worship nor any other customer is being "penalized" for their usage, as those customers are paying for the costs that they caused to be incurred by Oncor in order to provide delivery service to their facilities.

Commission Response

The commission declines to include in the rule a provision that prohibits the use of tiers in designing rates. The commission agrees with Oncor that PURA §36.009 directs the commission to adopt a rule containing an appropriate load-factor threshold, and other than the prohibition of demand ratchets for certain customers with load factors below the threshold, the law contains no provisions regarding how a customer's load factor should be used to design rates. Because the law neither explicitly provides for nor explicitly prohibits the use of tiers, parties are free to advocate for or against the use of this rate-design methodology in rate proceedings,

and the commission has the discretion to consider it and other rate-design alternatives. Accordingly, no rule modification in this regard is required.

Similarly, PURA §36.009 contains no requirement that, after implementation of the rule, the commission ensure that customers below a certain load-factor threshold experience "equal relief." No change to the rule is required.

Application of Demand-Ratchet Waiver to Transition Charges and Riders

TEPA commented that the demand ratchet waiver should apply to all ratchet-based charges. TEPA argued that PURA §36.009 clearly states that TDUs are required to "waive the application of demand ratchet provisions for each nonresidential secondary service customer that has a load factor equal to or below a factor set by commission rule," and that in addition to distribution-related charges, other charges are currently included in utilities' tariffs that have historically been billed based on ratcheted demand. TEPA commented that these other charges include transition charges (TCs), nuclear decommissioning charges, rate-case expense surcharges, etc., and the Legislature has decided that demand ratchets are inappropriate for application to certain customers and there is no rationale for applying ratcheted demands to these other charges. TEPA stated that it is important to ensure that other charges to customers that are based on ratcheted demands are not artificially inflated by the imposition of a ratchet, and recommended that the commission clarify that the demand ratchet waiver applies to all charges that have been billed based on ratcheted billing demands.

In reply comments, TEPA elaborated that based on a review of the TC tariffs, it appears that TCs for CenterPoint and AEP-TCC contain provisions for annual true-ups and interim adjustments, to correct any overcollection or undercollection, and while the TC tariffs establish inter-class allocation factors, they do not specify how the costs are allocated within the class. TEPA stated that in the event that a true-up is necessary to ensure the proper collection of the TC amounts, it appears that an adjustment mechanism is already in place. To the extent that the tariffs of these TDUs require the use of ratcheted billing demands for TCs, TEPA agreed that the demand ratchet exemption should not be applied. TEPA stated that the existing tariffs are ambiguous in some cases, and this is an issue that may need to be investigated further and clarified in each TDU's rate case but is beyond the realm of what is possible in this proceeding.

Texas Impact and Texas Energy similarly observed that the riders in Oncor's tariff are based on a demand ratchet, and opined that this should be disallowed. Texas Impact stated that the rule should be interpreted to mean that any charge, tariff, or rider be based on a measurement of demand that actually occurred during that month's billing cycle and not in previous months.

COH disagreed with Texas Impact and TEPA that the demand ratchet waiver should apply to all ratchet-based charges, including TCs, nuclear decommissioning charges, and rate case expense surcharges. COH commented that in contrast to TEPA's position, the Legislature specifically authorized a demand ratchet waiver for customers billed for

distribution service charges. COH stated that the commission's rule must properly implement the statute's clear language.

Joint Utilities and Oncor commented that the total amount of TCs to be collected has already been set by the commission in the financing orders of Oncor, CenterPoint, and AEP-TCC. Oncor commented that under- and over-recoveries of transition charges in any one period are carried forward into the calculation of the next period's transition charge rate, and ratchets help provide stability to revenue recovery, and thus help to reduce any such under- or over-recoveries. Oncor commented that particularly with respect to under-recoveries, any significant deviation in revenues would be problematic, as the bonds must be paid in a timely manner, and there is no other revenue producing mechanism available. Oncor and Joint Utilities pointed out that the utility companies in Texas have numerous TCs approved by commission financing orders pursuant to specific statutory provisions. For example, PURA §39.303(d) provides that:

> A financing order shall become effective in accordance with its terms, and the financing order, together with the transition charges authorized in the order, shall thereafter be irrevocable and *not be subject to reduction, impairment, or adjustment by* further action of the commission, except as permitted by Section 39.307. (Emphasis added)

Similarly, PURA §39.310 provides that:

> The state pledges, however, for the benefit and protection of financing parties and the electric utility, that it will not take or permit any action that would impair the value of transition property, or, except as permitted by Section 39.307, *reduce, alter, or impair* the transition charges to be imposed, collected, and remitted to financing parties, until the principal, interest and premium, and any other charges incurred and contracts to be performed in connection with the related transition bonds have been paid and performed in full. (Emphasis added)

Joint Utilities and Oncor stated that, in sum, PURA §36.009 should not be interpreted as mandating that the commission impair the pledge found in PURA §39.310, nor act in a manner contrary to PURA §39.303(d). Joint Utilities and Oncor stated that the commission should not take any actions that would negatively impact the stability of TC revenues and should clarify that the provisions of the rule do not apply to TCs. Joint Utilities provided recommended rule langue pursuant to this point.

With respect to nuclear decommissioning charges, Oncor commented that while there is no similar state government pledge such as that for TCs, such charges are specifically authorized by PURA §39.205, and nuclear decommissioning charges are set at a certain level and cannot be changed until there is evidence that the current rates are under- or over-recovering the revenue requirement by a certain percentage set by commission rule. Oncor further noted that it does not have the authority, on its own, to revise the rates or how they are billed, because the power generation company responsible for the nuclear power plants has that authority.

With regard to rate case expense riders, Oncor noted that is has two such riders that are subject to ratchet provisions—the first is due to expire on October 29, 2012, and thus will end long before the provisions of this rulemaking and PURA §36.009 are applicable; the second rider is due to expire on approximately January 1, 2015, and, depending on the timing of Oncor's next rate case, could still be in effect, although it would be for a fairly limited period. Oncor additionally noted that its nuclear decommissioning and rate-case expense riders together total only about 1.2% of the total demand charges that are subject

to ratchets. Oncor submitted that there appears to be little reason to modify existing riders that have only a minimal dollar impact on any given customer and, with respect to rate-case expense riders, would only be in effect for a short period of time. Oncor commented that the commission could simply set the maximum load factor for ratchet exemption under PURA §36.009(1) equal to zero for the transition charge, nuclear decommissioning, and existing rate case expense riders, and if the commission desires, it could ensure that any possible future riders are covered by the rule.

Cities commented that they believe as a general matter that the load-factor limitation should apply to all delivery charges to the extent those tariffs include a ratchet requirement. This would prevent an anomalous result, such as a low-load-factor billing in which the nuclear decommissioning charge is a disproportionately large component of the monthly bill. With regard to transition charges, Cities acknowledged that the commission cannot modify an approved financing order, but Cities suggested a modification of the language in section (a) as requested by Joint Utilities; Cities stated that the modification would clarify that the exception for transition charges is applicable only if the financing order creates an actual requirement to utilize ratchets.

Commission Response

PURA §36.009 applies "notwithstanding any other provisions of this code." Subsection (1) requires a TDU to "waive the application of demand ratchet provisions" and subsection (4) requires that the waiver occur "in the utility's next

base rate case." Section 25.5(10) (relating to Definitions) of the commission's rules defines base rate as follows:

> **Base rate — Generally, a rate designed to recover the cost of service other than certain costs separately identified and recovered through a rider, rate schedule, or other schedule. For bundled utilities, these separately identified costs may include items such as a fuel factor, power cost recovery factor, and surcharge. Distribution service providers may have separately identified costs such as the system benefit fee, transition costs, the excess mitigation charge, transmission cost recovery factors, and the competition transition charge.**

This definition was in effect at the time HB 1064 was enacted. (The definition of "distribution service provider" includes a TDU that provides retail delivery service at distribution voltages. *See* §25.5(33).) The commission therefore interprets the demand ratchet waiver provision of PURA §36.009 to apply only to base rates, because the waiver will occur in the TDU's next base rate case and the statute does not state that all demand ratchet provisions must be waived. This interpretation avoids a conflict between PURA §36.009 and PURA provisions that address transition costs/charges, PURA §39.303(d) and §39.310. In addition, as explained by Oncor, rates that include a demand ratchet but that are not base rates constitute only a small portion of a nonresidential secondary service customer's bills. The commission has changed the rule to clarify that it applies only to base rates.

Legislative Prohibition against Shifting of Costs

TIEC, the Christian Life Commission, and COH commented that the Legislature did not intend for other customer classes to bear costs that might be associated with waiving

demand ratchets for certain secondary voltage customers, and cited comments to that effect by Representative Jim Pitts in both legislative proceedings and this rulemaking. TIEC stated that Representative Pitts' and the Legislature's intent in passing HB 1064 should be clearly stated in the rule to prevent confusions in any future rate proceedings in which the requirements of the rule are applied. TEPA agreed with TIEC that the rule should clarify that costs will not be shifted to other classes, but pointed out that some degree of cost shifting must occur within the class to achieve the intent of the law. Cities commented that while they do not object to TIEC's requested clarifying language, the commission's intent might be better addressed in the preamble to the adoption of the rule. Cities commented that the House Journal dated April 18, 2011, that is cited by TIEC expresses the intent to implement this provision without shifting costs onto other customer classes, and this should be distinguished from "intra-class" cost changes that are not prohibited by the legislative intent set out in the House Journal, as cited in Cities' comments.

COH commented that implementation of the rule should not result in a shifting of costs between or among ratepayers, and that this position expresses the fundamental ratemaking principle of cost causation. COH submitted that the proposed rule does not address this issue and lacks the language that would effectively implement the Legislature's intent, but that the methodology used in PUC Docket No. 38929 (Application of Oncor Electric Delivery Company LLC for Authority to Change Rates) to establish demand ratchet waivers minimized or eliminated the potential for cost shifting among low-load and high-load-factor customers. COH emphasized that costs should not

be shifted to other customers within the nonresidential secondary greater than 10 kW customer class, and that the commission should implement a rule that achieves revenue neutrality to avoid intra-class subsidization. COH proposed rule language that it believes is consistent with this result, and in the event that the commission decides to not use its recommended language, it requested that TIEC's language be incorporated with COH's suggested edits.

Joint Utilities commented that COH recommends that no cost shifting occurs among the customers within the rate class to which demand ratchet waivers apply (intra-class cost shifting) and that COH points to the rate design approved in Oncor's most recent rate case as fulfilling that goal. Joint Utilities submitted that the Oncor rate design, by using a tiered load-factor exemption approach coupled with costs recovered only from the customers within each tier, is exactly the rate design causing the Christian Life Commission and Texas Impact so much consternation, and does not eliminate cost shifting, but merely creates more narrowly defined categories within which cost shifting occurs. Joint Utilities suggested that such granularity within a customer rate class is not required and could produce overly burdensome results for customers. Joint Utilities suggested that recovery of foregone demand costs resulting from a ratchet waiver in the nonresidential secondary service classes be recovered from those classes and not from other classes; this would be consistent with the requirements in the commission's Rate Filing Package that costs of one customer class not be shifted to other customer classes.

At the public hearing, Aaron Gregg, an aide to Representative Pitts, stated that, "It's always been the intention of Representative Pitts that this certainly not affect any other rate classes other than the one rate class that we're specifically looking at, and…this was never intended to…make any changes between rate cases."

Commission Response

To explicitly prohibit inter-class cost shifting, the commission modifies the rule language consistent with TIEC's suggestions. With regard to COH's recommendation that the rule should also require intra-class revenue neutrality, the commission disagrees—the statute does not prohibit intra-class cost shifting, and depending upon the rate-design implemented in a TDU rate case, some degree of intra-class cost shifting may be unavoidable. Accordingly, the commission makes no changes to the rule in this regard.

Clarification Regarding Necessary Action by Regulatory Authority

COH commented that while PURA §36.009(4) requires the utility to implement the waiver in its next base rate case, the proposed rule appears to omit this timing element. COH suggested language to assure that waivers are implemented in each utility next comprehensive base-rate proceeding. COH suggested that the rule track the precise language of the statute when referring to the "base rate case" in which the regulatory authority must take action on demand-ratchet waivers. TEPA expressed its agreement with these points.

Commission Response

The commission disagrees with COH and believes that the rule is sufficiently clear that the demand ratchet waiver will be implemented in the context of a base-rate case. The commission thus declines to change the rule.

Applicability to TDUs Located within ERCOT

SPS, TEPA, and COH submitted that the proposed rule does not expressly limit the waiver to TDUs operating in ERCOT, and instead references only TDUs generally. SPS stated that while it is its understanding that the term "TDUs" is generally meant to reference ERCOT electric utilities that have separated transmission and distribution functions from power supply operations, the rule should be revised to clarify this point. SPS submitted modifying the rule language accordingly. TEPA stated that if the commission disagrees with this interpretation, then it recommends that there be no limit to the size of customer that is eligible for the waiver.

Commission Response

A TDU is a type of electric utility, but not all electric utilities are TDUs. PURA §39.105 states: "After January 1, 2002, a transmission and distribution utility may not sell electricity or otherwise participate in the market for electricity except for the purpose of buying electricity to serve its own needs." A vertically integrated electric utility like SPS is not a TDU, because it sells electricity. PURA §36.009 expressly applies to "a transmission and distribution utility," regardless of whether the TDU is located in ERCOT. However, all TDUs are currently in ERCOT.

Demand Ceiling

SPS stated that if the commission intends that the proposed rule applies to non-ERCOT utilities, the commission should set a ceiling of 100 kW for the demand ratchet threshold. TEPA commented that the proposed rule does not include any demand ceiling for application of the ratchet waiver and stated its desire that the rule have no maximum demand on eligibility for the waiver is implemented. TEPA stated that many of the targeted customers have demands in the hundreds of kilowatts but still exhibit low load factors because of their unique usage characteristics, and that data on a sample of churches revealed that the three largest facilities, with demands of 636, 733, and 967 kW, had load factors of 14.45%, 16.00%, and 20.18%, respectively, which are significantly below even the threshold contained in the proposed rule.

COH recommended instituting a kW limit for the ratchet waiver in order to avoid an unreasonable reduction in the number of customers that will continue to incur ratcheted billings. COH stated that should the commission decide to raise the load-factor threshold for customer waiver eligibility, it supports a ceiling on demand. COH and SPS commented that a demand ceiling allows the application of a demand ratchet to customers requiring significant levels of capacity to deliver high levels of power. COH agreed with SPS that establishing a maximum demand for demand ratchet waivers would balance two often conflicting rate design goals—reducing adverse bill impacts to small non-residential customers from demand ratchets, and allowing implementation of cost-based rates to larger non-residential customers that impose significant capacity costs as a result of large demands, regardless of the frequency of usage at those levels.

The Christian Life Coalition stated that HB 1064 did not include a maximum demand for eligibility and the proposed rule should strictly prohibit a demand ceiling. The Christian Life Coalition commented that the peak demand by houses of worship varies greatly and imposing a demand ceiling would defeat the purpose of this bill for many of the intended recipients of relief because of their usage patterns. The Christian Life Commission provided modified rule language consistent with its comments.

Commission Response

The commission agrees with the Christian Life Commission and TEPA that the statute contains no provisions for a demand ceiling. No modification to the rule is necessary.

Elimination of Ratchet Provisions for Houses of Worship

The Christian Life Coalition commented that the commission consider for houses of worship a provision, similar to that for agricultural customers, that eliminates the use of demand ratchets altogether.

COH disagreed, stating that the commission should not grant an exception for houses of worship, as rate relief based on cost shifting is not a subject for this rule making. COH stated its belief that overall bills can be reduced if demand is lowered coupled with demand ratchet relief intended by the law.

Oncor commented that requests for the commission to completely eliminate for houses of worship the use of demand ratchets exceeds the scope of the mandates of PURA §36.009, and should not be considered or granted in this proceeding. Oncor noted that its load-factor rate does not include any ratchet provision for distribution charges and the customers are billed on their actual monthly kW demand, not a ratcheted kW demand.

Commission Response

The commission agrees with COH and Oncor that the request to eliminate for houses of worship the use of demand ratchets exceeds the scope of the statute. No modification to the rule is necessary.

All comments, including any not specifically referenced herein, were fully considered by the commission. In adopting this section, the commission has made changes consistent with the discussion above and to clarify its intent.

The new section is adopted under the Public Utility Regulatory Act, Texas Utilities Code Annotated §14.002 (West 2007 and Supp. 2011) (PURA), which provides the commission with the authority to make and enforce rules reasonably required in the exercise of its powers and jurisdiction; §36.001, which permits a regulatory authority to establish and regulate rates of an electric utility; §36.003, which requires that the regulatory authority shall ensure that an electric utility's rates be just and reasonable; and §36.009, which requires the commission to establish by rule the requirement that a

transmission and distribution utility waive the application of demand ratchet provisions for certain nonresidential secondary service customers.

Cross Reference to Statutes: PURA §§14.002, 36.001, 36.003 and 36.009.

§25.244. Billing Demand for Certain Utility Customers.

(a) **Application.** This section applies to a transmission and distribution utility (TDU) that provides retail distribution service.

(b) **Definitions.** The following terms, when used in this section, have the following meanings, unless the context indicates otherwise.

(1) **Demand ratchet**—A provision in a TDU's tariff for retail distribution service that allows a customer to be billed based on the greater of the peak demand by that customer in the current month or some fixed percentage of the peak demand for that customer during previous months.

(2) **Nonresidential secondary voltage service customer**—A nonresidential customer that is billed demand charges for retail distribution service and that receives retail distribution service at secondary voltage through one point of delivery and that is measured using one meter.

(c) **Rates.** In a proceeding in which base rates are set for nonresidential secondary voltage service customers, the base rates set for nonresidential secondary voltage service customers shall provide that these customers shall be billed on a kilowatt-hour (kWh), kilowatt (kW), or kilovolt-amperes (kVA) basis, and that if a demand ratchet is utilized, the demand ratchet shall not apply to a nonresidential secondary voltage service customer that has an annual load factor less than or equal to 25 percent. This subsection does not require the use of demand ratchets

for any customers. This subsection shall not be applied in a manner that would shift costs to other customer classes.

(d) Annual Verification. Upon the implementation of base rates consistent with subsection (c) of this section, a TDU shall determine annually for each of its nonresidential secondary service customers whether to apply a demand ratchet. In addition, by January 15 of each year following the commission's final order in a proceeding described by subsection (c) of this section, a TDU shall file an affidavit certifying that it has accurately identified and billed nonresidential secondary service customers who under subsection (c) of this section cannot be charged a demand ratchet. In addition, the TDU shall attach to the affidavit a thorough description of the procedures that it uses to ensure that these customers are accurately identified and billed.

This agency hereby certifies that the new rule, as adopted, has been reviewed by legal counsel and found to be within the agency's authority to adopt. It is therefore ordered by the Public Utility Commission of Texas that §25.244, relating to Billing Demand for Certain Utility Customers, is hereby adopted with changes to the text as proposed.

ISSUED IN AUSTIN, TEXAS ON THE _____ DAY OF _____2012.

PUBLIC UTILITY COMMISSION OF TEXAS

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DONNA L. NELSON, CHAIRMAN

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KENNETH W. ANDERSON, JR., COMMISSIONER

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ROLANDO PABLOS, COMMISSIONER

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