BEFORE THE RÉGIE DE L'ÉNERGIE

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IN THE MATTER OF:

HYDRO QUÉBEC DISTRIBUTION

Demande du Distributeur relative à l'établissement des tarifs d'électricité pour l'année tarifaire 2012-2013

DOSSIER R-3776-2011

prepared on behalf of:

l'Association québécoise des consommateurs industriels d'électricité (AQCIE)

Conseil de l'industrie forestière du Québec (CIFQ)

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prepared opening statement of:

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OPENING STATEMENT OF ROBERT D. KNECHT

Good afternoon Madame President and members of the panel. Thank you for this opportunity to summarize my evidence, which is focused on tariff design for Rate M.

The tariff structure for Rate M consists of a single demand charge, and two blocked energy charges differentiated for consumption above and below 210,000 kWh per month (or roughly 500 kW for a typical Rate M customer). In this proceeding, the Distributor proposes to increase the demand charge and the first energy block charge by about 0.7 percent, and the tail block energy charge by 7.8 percent. The Distributor's rationale for this approach is that this approach will better align the tail block energy charge with the long-run avoided cost of energy, and that because tail block energy is the most responsive to price (or price elastic), this approach will more efficiently encourage conservation. With this change, the Distributor's tail block energy charge will have increased by 34.4 percent over the past seven years, compared to 7.4 percent for the demand charge and 14.0 percent for the first block energy charge. As you know, this pattern imposes disproportionate rate increases on larger customers with higher load factors, of a factor of more than 2:1.

While I recognize that the Distributor's proposals for the Rate M tariff charges are generally consistent with a policy previously established by the Régie, I recommend that, for the purposes of this proceeding, across-the-board rate increases be applied to the three components of the Rate M tariff. My reasons for this recommendation fall into a "traditional" category, which applies to the policy in general, and a "new" category, which relates to specific factors in this proceeding. I also offer several suggestions for alternative rate design options that should be considered as the Régie and the Distributor begin to wrestle with the implementation of Bill 100 into the tariff.

TRADITIONAL RATE DESIGN CONSIDERATIONS

First, it is not clear that the long-run price elasticity of tail block energy consumption is any higher than that of the first block. The Distributor does not offer any hard empirical support for this assertion. From a practical perspective, it is important to recognize that major decisions about operating levels, plant expansions and closures, and major conservation efforts will consider all aspects of the electricity tariff. While tail block energy may possibly be more short-run elastic than other energy, the Distributor does not base its tariff on short-run cost considerations.

Second, the proposed tariff will result in a significant share of Rate M customers facing little increased incentive to conserve.

Third, the cost allocation study approved by the Régie does not support reducing the demand charge relative to the energy charge. In fact, it implies just the reverse.

Fourth, the cost allocation study, combined with the recognition that larger Rate M customers generally have higher load factors than smaller Rate M customers, supports a lower tail block energy charge.

Fifth, if the Régie were to use the cost allocation study to assign rate increases to the various customer classes, Rate M customers will be penalized for reacting to these price signals by being assigned higher costs.

Sixth, the proposed Rate M tariff design changes, combined with the proposed Rate L tariff changes, will continue to widen the discontinuity between the Rate M and Rate L tariffs, creating an increasing incentive for customer migration from Rate M to Rate L. As proposed, a Rate M customer with a billing demand as low as 3,600 kW can pay a lower tariff by switching to Rate L and increasing its contract demand to the Rate L minimum of 5,000 kW. Such a shift eliminates any incentive for the customer to minimize its peak demands, and will in the longer term impose higher capacity costs on all of the Distributor's customers.

NEW RATE DESIGN CONSIDERATIONS

In addition to these traditional economic and regulatory principles, there are three new factors which militate against disproportionate rate increases for the Rate M tail block charge in this proceeding.

First, long-run avoided costs have declined sharply since the policy was implemented. Even using the Distributor's long-run avoided cost estimates, the proposed tail block energy charge will exceed the off-peak Rate M avoided cost of energy. While it is certainly possible that the economics will shift again in the future, the tail block energy charge is already much closer to avoided cost than the Régie and the Distributor would have imagined only a few years ago.

Second, the unit cost increases exhibited by the Rate M class in this proceeding appear to be related to a shift in customers from Rate G to Rate M, meaning that the smaller customers are causing the increase in per-kWh allocated costs. It is therefore inconsistent to apply a disproportionate increase to the larger customers within the class.

Third, implementing Bill 100 will exacerbate the rate discontinuity between Rate M and Rate L for industrial customers. I understand that the issue of how Bill 100 will eventually be implemented is not a subject for this proceeding. However, it will be difficult enough under the current Rate M and Rate L tariff structure to implement Bill 100 without creating enormous incentives for customer gamesmanship. In my view, it is not appropriate to increase the magnitude of that future problem by further widening the Rate M/Rate L gap in this hearing.

Thank you for your attention. I look forward to answering any questions that you may have.