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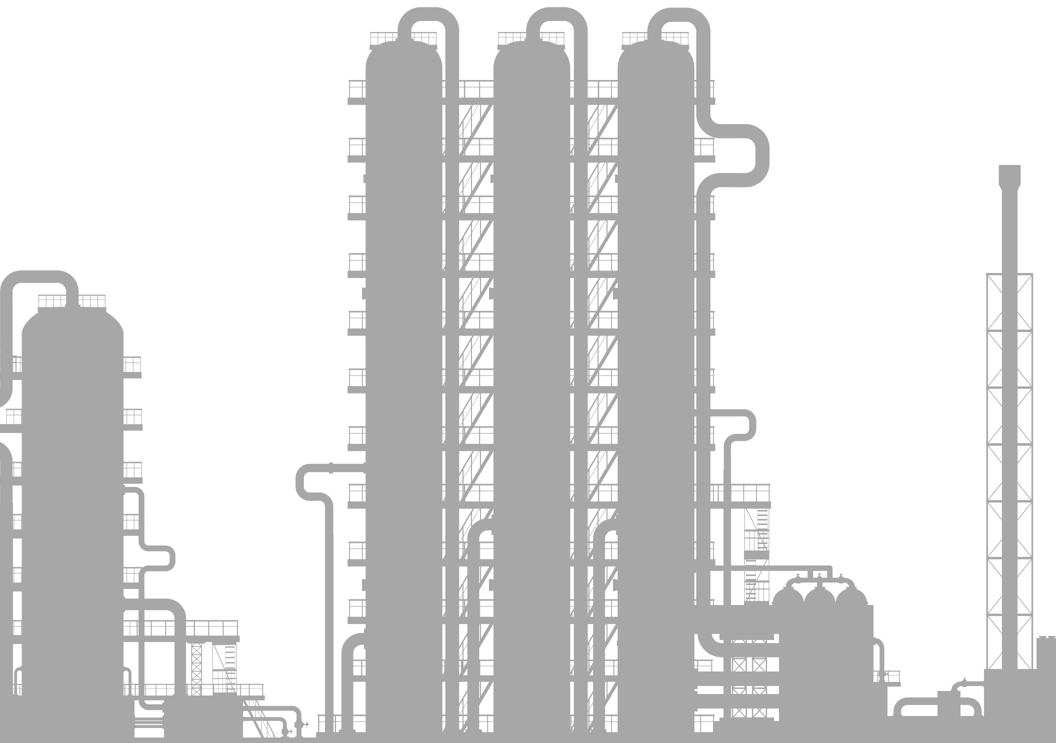
Atmos Cities Steering Committee

LICENSE TO BILL:

How the Gas Reliability Infrastructure Leads to Utility Rate Increases for Texas Consumers



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Executive Summary and Overview

The Gas Reliability Infrastructure Program, or GRIP, allows gas utilities to increase rates as the company's overall expenses are declining, revenues are increasing, or while the company is earning windfall profits. Under GRIP rules, a utility need only claim it has made extra investments associated with one part of its business — capital costs — and then it can obtain a rate increase. Regulators grant these increases as an administrative act without consideration of the utility's overall revenues, without consideration of offsetting savings in other areas of the utility's business and without considering whether its infrastructure investments are prudent. There is no avenue in a GRIP case to prevent a utility from charging ratepayers for imprudent utility expenditures.

The Atmos Cities Steering Committee (ACSC) offers this policy guide to help our readers understand the Gas Reliability Infrastructure Program. GRIP reform is necessary. This report examines the history and impact of the program, especially as it pertains to the north and central Texas customers of Atmos Energy. The report includes Major Findings and a section with Proposals for Reform.

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Major Findings

This report examines the history and impact of the Gas Reliability Infrastructure Program. Among the major findings:

1. GRIP has contributed to increased utility bills for home consumers and businesses, despite drops in the cost of natural gas.

2. GRIP may have been implemented with the best of intentions, but it needs to be re-evaluated and improved.

3. GRIP has been subject to abuse by gas utilities, including examples of expensive travel, cases of wine, and gym equipment included in some GRIP filings.

4. GRIP has permitted gas utilities to increase rates even during periods when those utilities are earning more revenue than authorized by the Texas Railroad Commission.

5. GRIP has contributed to increased utility spending because it ignores the efficiency impacts of the regulatory process.

Recommendations for Reform

1

Gas utilities should be barred from seeking rate hikes under the GRIP program during periods when they are otherwise earning more than their authorized rate of return.

2

The GRIP program should be amended in such a way as to take into account load growth and other offsets that could eliminate or reduce rate increases.

3

The GRIP program should be amended to clarify that only invested “pipe-in-the-ground” (i.e. infrastructure) may be allowed in the interim rate requests.

4

Limit the number of annual GRIP cases to three before the utility must have its costs examined.

The Gas Reliability Infrastructure Program: An Overview

The Texas Railroad Commission traditionally considers gas utility expenditures, revenues, tax offsets, the prudence of investments and other factors when setting gas utility rates. In 2003, however, the Texas Legislature authorized the Gas Reliability Infrastructure Program, or GRIP, which created new rules that permit gas utilities to increase rates without substantive agency review. Utilities can apply for these GRIP increases once a year, for up to six years. At the end of that period, the utility is required to submit to a comprehensive rate case.

As an unfortunate consequence of this program, Texas gas utility customers have endured year after year of rapid rate increases. Consider, for example, the case of Atmos Pipeline, a division of Atmos Energy that charges rates that go into the home utility bills of most North Texas residents. Atmos Pipeline used the GRIP statute to increase rates 14 times between 2004 and 2017, according to a review of documents filed at the Texas Railroad Commission. Those rates have gone up by more than a quarter billion dollars during that period.

The GRIP increases commanded by Atmos Pipeline also have become incrementally larger, with an increase of $1.8 million in 2005, to four relatively recent GRIP increases of $30 million, $45.6 million, $37.3 million and $40.7 million respectively. In the division's GRIP case from May of 2016, pipeline rates increased by 12.9 percent; in December of 2017, they increased another 6.4 percent.

Statewide, average residential gas bills have increased over a recent 10-year study period, even as the commodity price of natural gas has dropped precipitously. [See page 8]

GRIP is in Need of Revision

Utilities claim that such quick rate increases allow them to manage their infrastructure investments in a more efficient manner. More specifically, the utilities claim the GRIP program reduces "regulatory lag," which is that period of time between when a utility makes infrastructure investments and when it would receive reimbursement for the investments through rates.

However, utilities *already* have a duty and incentive to make prudent infrastructure investments — no further regulatory incentive should be required. Leading economists also note that some amount of regulatory lag encourages utility efficiency. This is because utilities always will seek to check their expenditures during the lag period, according to economists. "Freezing rates for the period of the lag imposes penalties for inefficiencies … and offers rewards for (the) opposite," writes Dr. Alfred Kahn, author of *The Economics of Regulation.* Such efficiencies disappear if utilities know they can rapidly increase rates every time they spend more.

Utilities also claim the GRIP statute reduces the necessity of more full-scale rate cases. Prior to GRIP, however, municipalities and gas utilities commonly reached settlements without the expense or necessity of litigating rate cases. As a partial result of court and Texas Railroad Commission determinations that no meaningful review of GRIP expenditures can occur until a later general rate case, the GRIP statute has led to more — not fewer – rate proceedings.

The experience of Atmos and its predecessor utilities in North Texas is a good case in point. Prior to the adoption of the GRIP statute in 2003, the Texas Railroad Commission adopted only one rate increase in 20 years for the customers served by Atmos Mid-Tex or its predecessors. In the decade and a half afterwards, there have been on average at least one rate increase *each year.* Some increases were through the GRIP process, some through a separate but related process, and some through major rate cases.

GRIP has contributed to increased utility bills for home consumers and businesses, despite drops in the commodity cost of natural gas.

Gas utilities also claim that consumers who pay too much under GRIP will be made whole later, after the utility participates in a more traditional rate review. The problem here is that gas utilities can go for years without such review. In the meantime, consumers get stuck paying inflated rates, and the utilities rake in millions in excess profits.

Determining whether utilities prudently incurred expenses during the long gap between full-blown rate cases also can be extremely difficult.

GRIP: A Short History

In 2003, when Texas lawmakers first created GRIP with their adoption of Senate Bill 1271, their clear intent was to encourage prudent infrastructure investment by gas utilities. Two years later the Texas Legislature slightly modified GRIP with the passage of House Bill 872, legislation that adjusted timing requirements in the program. Lawmakers did not specifically employ the term "Gas Reliability Infrastructure Program" in either statute (GRIP is a regulatory term used by the Railroad Commission), but rather drafted new rules for "interim rate adjustments" by gas utilities. Although adopted with the best of intentions, the GRIP laws have allowed a piecemeal regulatory process to take hold in Texas, one in which utilities increase rates frequently and with no significant oversight.

Atmos (the gas utility serving north and west Texas) has employed GRIP on 14 separate occasions since 2004 to increase pipeline division rates. These increases have cost ratepayers more than a quarter billion dollars. The utility employed GRIP to increase its Mid-Tex division and West Texas division rates six times apiece. Other utilities also have employed GRIP to increase rates frequently in other parts of Texas.

One of Atmos' more controversial GRIP filings came in 2006 when its Mid-Tex division attempted to include expenses relating to furniture, food, executive travel, office supplies and artwork. The utility eventually removed many of those expenditures from its filing after they became the subject of unflattering media reports. Gas utilities over the years also have employed GRIP to increase rates during periods in which the utilities were already collecting more than their authorized rate of return. [See page 9]

In response to persistent problems with GRIP, the Atmos Cities Steering Committee in 2007 negotiated an alternative procedure called the "Rate Review Mechanism," or RRM for short. Participating cities judged RRM necessary on a trial basis to avoid many of the problems inherent with GRIP. Under the RRM program (which, like GRIP, utilities employ on a voluntary basis) cities agree to annual expedited piecemeal rate reviews. But the RRM, unlike GRIP, allows for a review of utility expenditures within each filing, and includes a path to disallow those costs deemed unreasonable. The RRM also includes customer protections not found in GRIP.

Utilities have employed GRIP repeatedly throughout its history to hike rates, but they would have employed it even more frequently if not for the RRM process. Despite its advantages, however, the RRM offers ratepayers only limited protection against rapid rate hikes associated with gas distribution systems located within city limits and absolutely no protection for hikes associated with gas pipelines located outside city limits. For these outside-city-limit cases, utilities continue to file for GRIP increases.

Why Aren't Texas Gas Utility Bills Lower?

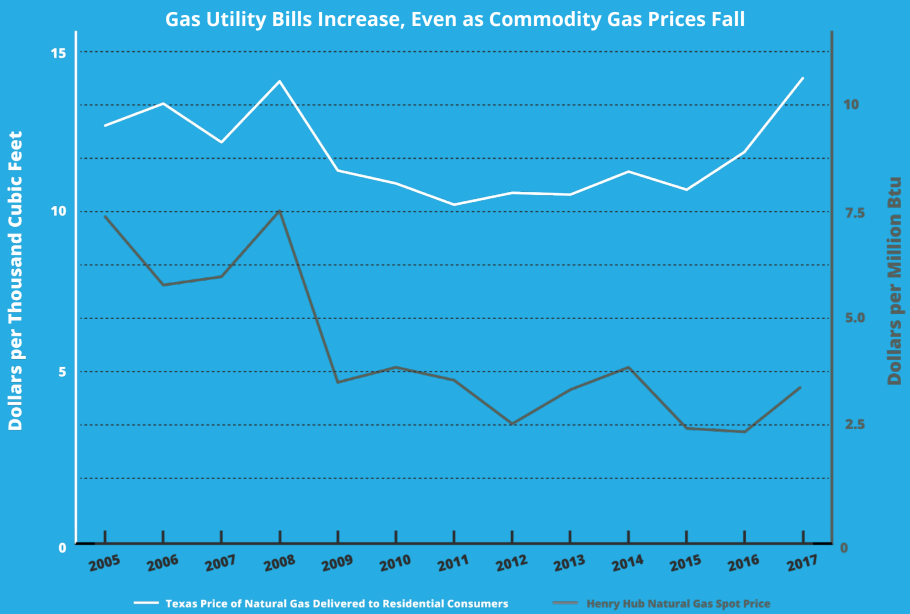
Natural gas commodity prices are much less than half what they were in 2005 and yet average home gas bills in Texas have gone up. How can this be? Why aren't Texans enjoying real savings in their gas utility bills?

The answer relates to pipeline and distribution charges, which have continued to increase since 2005.

According to the United States Energy Information Administration, the average annual commodity (Henry Hub) price for natural gas declined by 65.8 percent from 2005 through 2017.[9]

At the same time, average overall natural gas prices for Texas home consumers (delivery charges, plus those commodity costs) increased by 10.6 percent — from an average of $12.48 (per thousand cubic feet) to $13.80.[10]

GRIP and other piecemeal ratemaking procedures have contributed greatly to these rate increases for end-users. Without them, Texas consumers should have expected greater benefits from dropping natural gas prices.



Media Reports: GRIP Allows Rate Hikes Despite Windfall Profits

The state's leading newspapers have questioned the fairness of the Gas Reliability Infrastructure Program. The *Dallas Morning News* has noted that GRIP increases have masked precipitous declines in natural gas prices over the last several years. "The program … amounts to a license to skirt serious regulatory oversight," the paper's editorial board stated.

The Houston Chronicle, meanwhile, reported that gas utilities already reporting excessive profits employ GRIP to charge their customers even more. The newspaper reviewed GRIP cases going back about 10 years, comparing the outcomes in those cases with rate-of-return profit levels also reported by the utilities. The newspaper found that "Atmos earned above the allowable level in 2013 and 2015 … and both times the Railroad Commission allowed the company to raise rates with few questions asked."

Atmos Steering Committee Cities

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Argyle
Arlington
Aubrey
Azle
Bedford
Bellmead
Benbrook
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Blossom
Blue Ridge
Bowie
Boyd
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Buffalo
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Colorado City
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Coppell
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Corinth
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Crowley

Dalworthington
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Denison
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Keller
Kemp
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Lavon
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McKinney
Melissa
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Newark
Nocona
North Richland
Hills
Northlake
Oak Leaf
Ovilla
Palestine
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Paris
Parker
Pecan Hill
Petrolia
Plano
Ponder
Pottsboro
Prosper
Quitman
Red Oak
Reno (Parker
County)

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Richardson
Richland
Richland Hills
River Oaks
Roanoke
Robinson
Rockwall
Roscoe
Rowlett
Royse City
Sachse
Saginaw
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Sherman
Snyder
Southlake
Springtown
Stamford
Stephenville
Sulphur Springs
Sweetwater
Temple
Terrell
The Colony
Trophy Club
Tyler
University Park
Venus
Vernon
Waco
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Westlake
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Westworth
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This document is legislative advertising: Atmos Cities Steering Committee, which may be contacted at Mail Stop 63-0300, P.O. Box 90231, Arlington, Texas 76004-3231.

About the Atmos Cities Steering Committee

Cities have been standing up for the rights of natural gas consumers for generations — especially at the Railroad Commission of Texas. The experience of cities handling gas ratemaking issues on behalf of consumers is unparalleled.

One of the most important municipal coalitions currently active in gas ratemaking is the Atmos Cities Steering Committee, an organization of more than 170 cities in north and central Texas with nearly 1.2 million residential customers. Membership in this standing committee is determined by passage of a resolution by each governing body. The Steering Committee undertakes activities on behalf of its city members and their citizens such as participation in rate cases, rulemakings and legislative efforts that impact natural gas rates.

Get the Facts

Find out more from the Atmos Cities Steering Committee, a city coalition that represents the public in gas utility regulatory matters

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