



AARP and AKPIRG Comments on ML&P-Chugach Merger study

My name is Virginia Rusch. I am here testifying on behalf of AARP and AKPIRG. As consumer advocates, AARP and AKPIRG are interested in utility rates because they have a big impact on the public, including AARP members.

AARP and AKPIRG asked me to testify as their utility expert because I have worked on utility ratemaking for many years. I was an Assistant Attorney General with the Alaska Department of Law for 23 years, and for 14 of those years was assigned to represent the Regulatory Commission of Alaska and its predecessor the Alaska Public Utilities Commission in the roles of the public advocate attorney and the RCA's own legal counsel.

To begin with, AARP and AKPIRG commend the current leadership of these utilities for studying how combined utility operations might benefit the consumers by reducing future energy costs. For many years, these two utilities have battled each other, building competing facilities up through the 1970s, and more recently in litigating over potential customers. That wasn't good for customers, who had to pay the cost of duplicate facilities and litigation. So, AARP and AKPIRG are pleased to see these utilities making efforts to put aside rivalries from the past and work together in the public interest. AARP and AKPIRG are also pleased that the leadership of both utilities has promised a transparent and public process for the study of the merger potential of Chugach Electric Association (Chugach) and Anchorage Municipal Light & Power (ML&P). We are pleased to have the opportunity to present comments this evening and in future phases of consideration of the very important topic of a potential merger of these utilities.

With that said, we have a number of specific comments on the Navigant Phase I study.

1. A Transparent And Public Process Must Include Discussion Of Regulation Of Any Merged Entity And Any Change In Regulation Of Any Other MOA Utility That Occurs As A Consequence.

The Navigant Phase I report seems to assume, without detailed discussion, that any combined utility entity will continue to be regulated by the Regulatory Commission of Alaska, the state watchdog agency that is responsible for protecting utility customers by approving only just and reasonable, cost-based rates. However, under state law as it stands today, a merger of Chugach and ML&P could bring about an end to the RCA's consumer protection role, not only for the electric utility that emerges from this process, but also for Anchorage Water and Wastewater Utility (AWWU). This would happen

because, under the current statute, competition between Chugach and ML&P is the operative fact that triggers regulation of both ML&P and AWWU.¹

Now I don't think anyone would argue that the Navigant Phase I report we are discussing today justifies ending regulation of these electric utilities and especially of AWWU. AARP and AKPIRG don't want to find that deregulation has just happened as an unintended consequence. We would like to be assured that the transparent and public process that has been promised includes a full public discussion of any potential regulatory changes that would result.

AARP and AKPIRG support utility rate regulation by an authority that is completely independent of any utility or its owner, and that is adequately funded and staffed so that it has the resources to focus on protection of residential ratepayers.² The current statute

¹ The statute that establishes regulatory jurisdiction over these utilities is AS 42.05.141, which provides in part:

Sec. 42.05.141. General powers and duties of the commission.

(a) The Regulatory Commission of Alaska may do all things necessary or proper to carry out the purposes and exercise the powers expressly granted or reasonably implied in this chapter, including

(1) regulate every public utility engaged or proposing to engage in a utility business inside the state, except to the extent exempted by AS 42.05.711; .

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AS 42.05.711 exempts most municipally owned utilities from RCA regulation, but the exemption does not apply to ML&P or AWWU. This statute says:

Sec. 42.05.711(b). Exemptions. . . .

(b) Except as otherwise provided in this subsection and in (o) of this section, public utilities owned and operated by a political subdivision of the state, or electric operating entities established as the instrumentality of two or more public utilities owned and operated by political subdivisions of the state, are exempt from this chapter, other than AS 42.05.221 - 42.05.281 and 42.05.385. However,

(1) the governing body of a political subdivision may elect to be subject to this chapter; and

(2) *a utility or electric operating entity that is owned and operated by a political subdivision and that directly competes with another utility or electric operating entity is subject to this chapter and any other utility or electric operating entity owned and operated by the political subdivision is also subject to this chapter; . . . (emphasis added)*

² The AARP Policy Book 2007, at p. 10-4 sets out the following principles related to utilities:

- **Consumer Representation**—independent, fully funded and adequately staffed consumer advocacy organizations empowered to initiate investigations and authorized to represent residential ratepayers before state and federal regulators and in the courts
- **Regulatory Authority**—independent, fully funded and adequately staffed regulators who are focused on residential ratepayers and empowered to initiate investigations and enforce laws and regulations

should be changed if necessary to continue the regulatory protection that customers of these utilities currently enjoy.

2. The Benefits Of The Lower-Priced BRU Gas Belong To Current ML&P Customers.

The Phase I study considers uses of MOA's Beluga River Unit (BRU) Gas at pp. 43-47. The study doesn't propose any particular way of using the BRU gas, but it also fails to state clearly one important principle that must guide future use of the BRU gas. The RCA orders approving ML&P's purchase of a one-third interest in the BRU provided very specifically that the benefits of that gas belong to ML&P consumers (not to the utility, or its owner the Municipality). The RCA reasoned that the customers are entitled to the benefits of the lower-priced gas because the bonds issued to purchase ML&P's interest in the BRU are revenue bonds which must be paid back through rates charges to the utility's customers. Because the payment obligation rests with the utility's customers, not with the city's taxpayers, the utility customers are also entitled to the benefits of the gas field purchase. Any proposal to spread these benefits to a wider group of customers of a merged utility dilutes the valuable rights of the current ML&P customers to benefit from the BRU gas. An underlying assumption in continuing study of the merger potential ought to be that ML&P consumers must receive the benefits of their valuable interest in the BRU gas just as Chugach customers receive the benefit of their valuable interest in capital credits.

3. The Phase I Report Does Not Fully Explain Or Justify Cost Assumptions In Its Models.

The validity of the results of Navigant's cost comparison studies depends greatly on the accuracy of the cost predictions used in the models. At this stage, AARP and AKPIRG are unable to evaluate any specific cost projections used in the models, but we have a comment on the projected cost savings of 97 million dollars in Case 6, which is described on p. 6 as "Joint contracted operations." This concept is further described on p. 10 as follows:

"These combined operations would involve merging most of the combined staff and middle management of the two utilities into a separate combined operating organization to provide joint operations and administration of these two contiguous utility systems."

Certainly these utilities should attempt to save money for the consumers by combining operations for greater efficiency. To best serve the ratepayers, the combined operating organization should be structured to avoid an extra layer of profit that the utilities themselves could not add into the rate calculation. Under established ratemaking principles, a utility is entitled to recover the costs it incurs in providing the utility service, plus a return on its invested capital. The utility is not entitled to recover a cost-plus margin on its costs. For example, a utility incurs the costs of keeping its books according

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- **Public participation**—broadly publicized hearings on proposed changes in public utility rates that are conducted in the service area to be affected and allow consumers to express their views

to various accounting principles. Consumer rates cover these accounting costs, but the utility does not earn a profit margin on its costs. But if the utility contracts with any outside business to provide the accounting services, that business obviously needs to make a profit on the services its provides. Because of the profit margin expected on contracted services, the cost to consumers may be greater than if the utility provides the services itself. The impact of the profit margin on contracted services in Case 6 needs to be analyzed more carefully.

Contact Information:

Virginia Rusch, Attorney at Law
Law Office of Virginia A. Rusch
801 W. Fireweed Lane #202
Anchorage, AK 99503
Ph: 907-223-0604
Email: vrusch@acsalaska.net

Steve Cleary, Executive Director
AkPIRG
PO Box 101093
Anchorage, AK 99510
Ph: 907-278-3661
Email: akpirg@akpirg.org

J. Patrick Luby, ASD Advocacy
AARP AK
3601 C Street #1420
Anchorage, AK 99503
Ph: 907-762-3314
Email: jluby@aarp.org