Public Service Company of New Mexico
NMPRC Case No. 16-00276-UT
Executive Summary

Introduction

Since the last rate case filed in 2015, PNM has continued to invest in utility plant and facilities with an eye toward protecting the environment, promoting solar and other clean energy technologies, and providing safe and reliable service to customers. Although PNM has kept its O&M costs below average inflation levels, significant changes in PNM's generation portfolio, the need for PNM to invest in its system to maintain a high level of service, and changes in how PNM's retail and wholesale customers use energy and rely on the system necessitate the filing of another rate case with the Commission.

PNM's electric rate case filing requests a rate increase of approximately $99.2 million effective January 1, 2018. PNM recognizes that PNM customers are still adjusting to a general rate increase for the first time in several years. However, PNM's rates must reflect the retirement and replacement of coal-fired plant in 2018, and when rates do not reflect the reasonable costs of providing service, PNM's ability to provide customer services and reliably maintain its system is diminished. With PNM's current rates going into effect in October of this year, and with the need to change rates again in 2018, PNM recognizes that the proposed increase can place financial pressure on PNM customers. For this reason, if PNM's requested rate increase is approved by the Commission, PNM proposes to mitigate the rate impact on PNM customers by phasing in the rate increase over two years.

In addition to covering the cost to provide service, PNM is improving its rate design to ensure that the price a customer pays better reflects the costs of connecting that customer to the grid, and that PNM is able to recover its lost fixed costs when customers use less energy as a result of PNM's energy efficiency and load management programs. Commission approval of PNM's rate case will allow PNM to continue investing on behalf of PNM's 517,000 retail customers and maintaining PNM's infrastructure to support reliable service, economic growth and a sustainable energy future for New Mexico.

The Major Drivers for this Rate Case

The following table summarizes the key elements that account for approximately 85% of the rate request. The majority of PNM's projected $99.2 million revenue deficiency in 2018 directly relates to the costs of PNM's previously approved resource additions or retirements and ongoing capital investments.

Element	*Amount*
Generation Portfolio Changes from the BART Case	$35 million
Ongoing Capital Investments	$29 million
Customer Usage and Load Characteristics	$11 million
Changes in Jurisdictional Allocations	$9 million

In the BART Case, the Commission approved a stipulation among PNM, Staff and major stakeholders that helps New Mexico comply with the Regional Haze Rule under the Clean Air Act. PNM will retire coal-fired generation at San Juan Units 2 and 3 and replace them with 134 MW in Palo Verde Unit 3 and 132 MW in San Juan Unit 4 in 2018. These actions require rate changes for 2018. PNM also invests in its system to maintain the level of safe and reliable service that customers expect. These ongoing projects include investing in generation assets such as emission control technology at the Four Corners Power Plant, transmission and distribution projects that accommodate load and system operational requirements, and other investments that support the provision of service to PNM's customers.

While the need to maintain reliable service has required PNM to increase its investment in its electric system, PNM's energy sales have declined by more than 2% since the 2015 Rate Case. Customers' changing usage patterns and load characteristics contribute to a significant revenue deficiency that PNM is addressing in this case by proposing necessary changes in the structure of retail rates.

Additionally, PNM is updating the allocation of generation and transmission costs between PNM's New Mexico retail and FERC jursidictions in response to changes in the relative use of PNM's system by retail customers and wholesale generation and transmission customers. The updated allocation reflects the expirations of wholesale generation contracts, allowing PNM to assign existing generation to meet retail customer needs. The reallocation also reflects increased interconnections with third-party energy producers such as wind farms, and those wholesale customers' greater responsibility for transmission system costs.

Balancing Rate Design with Rate Impacts

PNM's current rates reflect the progress made in modernizing its rate design in the 2015 Rate Case. PNM's rate design proposal in this case continues to take a cost-based approach to rate design, through changes in customer-related and demand-related fixed charges. PNM's proposals will reduce inter- and intra-class subsidies and will modify rate differentials in the residential inclining block rate structure. At the same time, PNM continues to balance its rate design goals with a policy of mitigating significant differences in rate impacts among rate classes, and in particular the residential customer class. PNM's rate case keeps proposed rate changes within a "band" that limits the bill impacts for its customers.

The following table summarizes the non-fuel revenue requirement increase and the projected bill impact for each of PNM's major customer classes. As shown below, PNM's proposed increase would result in an overall bill impact to the residential customer class of 12.79%. The system average bill impact for all customer classes is slightly more than 11%.

Percentage Revenue Requirement Increase and Bill Impact for Major Classes		
Class	% Non-Fuel Revenue Increase	Bill % Increase
Residential	15.76	12.79
Small Power	12.64	10.29
General Power	12.64	9.51
Large Power	14.02	10.10
Large Power >= 8,000	12.64	8.99
Universities	12.64	9.44
Manufacturing	12.64	8.49
System Total	14.33	11.23

Even with the proposed increase, an average PNM residential bill would be about $85 per month, which remains relatively low compared with an average regional utility bill of about $105 per month.

A Mechanism to Recover PNM's Lost Fixed Costs

Since 2007, PNM has successfully implemented cost-effective energy efficiency and load management programs. PNM exceeded the 2014 requirement to save 5% of 2005 retail energy sales, as mandated by the Efficient Use of Energy Act (EUEA). Furthermore, PNM is on track to exceed the EUEA's 8% savings mandate for 2020.

PNM customers unquestionably benefit from PNM's energy efficiency programs. At the same time, however, the energy efficiency savings that are realized by customers do not reduce PNM's fixed costs. PNM currently collects approximately 88% of the residential class' fixed costs through volumetric charges. When PNM's residential customers use less energy as a result of energy efficiency programs, PNM does not recover its fixed costs to provide service. PNM estimates that its lost fixed costs from reduced sales tied to these savings is approximately $91 million from 2011 to 2016. During the same time period, PNM earned a total performance incentive of $8.7 million. This is less than 10% of the lost fixed costs incurred but never recovered by PNM. PNM has consistently met or exceeded its statutory savings goals, but the reward for those successes is dwarfed by the magnitude of the regulatory disincentive that results from complying with the EUEA. The EUEA recognizes that it is only fair for PNM to have the opportunity to earn an incentive for its efforts without being required to suffer financial harm as a result of offering energy efficiency programs to customers. This is why the EUEA requires the Commission to identify and remove regulatory disincentives.

It is critical for the Commission to address the regulatory disincentive identified in this rate case. PNM is therefore proposing a narrowly-tailored "Lost Contribution to Fixed Costs" (LCFC) mechanism that will apply to residential and small commercial customers. This mechanism, which is used in some form in 17 states today, will allow PNM to collect the fixed costs otherwise lost to energy sales reductions that result from energy efficiency programs. PNM believes that this mechanism meets the criteria that the Hearing Examiner recommended and the Commission adopted in the 2015 Rate Case. PNM's proposal satisfies the legislative mandate to the Commission to remove regulatory disincentives in a manner that balances the public interest, consumers' interests and investors' interests. Importantly, Commission approval of this mechanism will not change the cost-effectiveness of PNM's energy efficiency programs.

Summary of Rate Case Filing

Financial	*Rate Design*
Future Test Year Period of January 1 to December 31, 2018 selected to align rates with resource retirements and replacements	Two-phase rate implementation of 7.2% in 2018 and additional 7.1% in 2019, with approval of full non-fuel rate increase
A non-fuel revenue requirement for base rates of $791.6 million; increase to revenue requirement of $99.2 million in 2018	Rate design combines an embedded cost methodology with banding to mitigate customer impact
Average system non-fuel revenue requirement increase of 14.33%; average non-fuel revenue requirement impact to residential class of 15.76 %	Maintains 2015 Rate Case's three-summer, one-winter coincident peak generation demand and transmission demand allocation methodology
Requested return on equity of 10.125%; Test Period capital structure: 49.61% common equity, 0.39% preferred equity, and 50% long-term debt	Continues improvements to rate design, including an increase to fixed customer charges and decrease to rate differentials between inclining block rates.
All fuel and purchased power expenses, renewable energy and energy efficiency and load management expenses are recovered outside of this proceeding	Proposes a LCFC mechanism to eliminate disincentives associated with energy efficiency and load management programs
Revenue requirement reflects disallowances for Palo Verde Unit 2 ownership and Balanced Draft	Proposes a transitional discount for rate class customers affected by 2015 Rate Case directive regarding PNM's interruptible IIPR tariff
No costs included for PNM's proposed Advanced Metering Infrastructure project	Filing includes functional electronic models for cost of service and rate design