



Memorandum from the Office of the Inspector General

July 9, 2020

A. Douglas Perry

FINAL REPORT – EVALUATION 2020-15712 – GRID ACCESS CHARGE

The Tennessee Valley Authority (TVA) and its local power companies (LPC) reached an agreement to institute a rate reduction of 0.5 cents per kilowatt-hour (kWh) and establish a grid access (or fixed-cost) charge to recover the equivalent amount of revenue. The TVA Board of Directors approved the rate change in May 2018. TVA implemented the rate change in October 2018, which included a revision to the structure of its wholesale electric power rates charged to LPCs.

Due to concerns expressed by stakeholders surrounding TVA's grid access charge, we performed an evaluation to determine if TVA's implementation of the grid access charge was revenue neutral as intended. The scope of our evaluation was the grid access charge's effect on TVA's revenue for fiscal year (FY) 2019.

We determined TVA's implementation of a grid access charge was revenue neutral because it resulted in an immaterial change in revenue to TVA.

BACKGROUND

TVA and its LPCs reached an agreement to institute a rate reduction of 0.5 cents per kWh and establish a grid access (fixed-cost) charge to recover the equivalent amount of revenue. The TVA Board of Directors approved the rate change in May 2018. TVA implemented the rate change, which included a revision to the structure of its wholesale electric power rates charged to LPCs. All LPCs were given the option to implement the grid access charge in October 2018 or defer until October 2019. Seventy-nine LPCs elected to implement the grid access charge in October 2018, while the remaining 75 elected to defer implementation until October 2019.

According to TVA, the primary objectives of this rate change were to (1) improve the alignment of wholesale rates with underlying costs to serve and facilitate measured, managed changes in LPC retail rate structures; (2) reduce upward rate pressure by mitigating the effects of uneconomic development in distributed energy resources, and (3) ensure rates remain as low as feasible for all consumers, consistent with TVA's mission to serve and improve the quality of life in the Valley. Additionally, TVA stated the rate change would not affect the total revenue collected by TVA, but the allocation of revenues across customer classes and among LPCs would change slightly.

According to TVA's Annual Report for FY 2019, TVA's current rate structure included three base revenue components: time of use demand charges, time of use energy charges, and a grid access charge. The demand charges were based on the customer's peak

monthly usage and increases as the peak increases, and the energy charges were based on time differentiated kWh used by the customer. The grid access charge captures a portion of fixed costs and was offset by a corresponding reduction to the energy rates. Demand and energy charges can be significantly impacted by weather; conversely, the grid access charge reduces the impact of weather variability to the overall rate structure.

According to TVA's original letter sent to LPCs in August 2017, the intention of the rate change was not to raise additional revenue for TVA, but to improve pricing to better align wholesale rates with the underlying costs.

Due to concerns expressed by stakeholders surrounding TVA's grid access charge, we performed an evaluation of TVA's implementation of the grid access charge.

OBJECTIVE, SCOPE, AND METHODOLOGY

The objective of this evaluation was to determine if TVA's implementation of the grid access charge was revenue neutral as intended. The scope of the evaluation was the grid access charge's effect on TVA's revenue for FY 2019. To achieve our objective, we:

- Interviewed Commercial Energy Solutions employees and reviewed their calculations to determine how the grid access charge was calculated and how it was revenue neutral.
- Calculated the revenue for TVA and for each customer for FY 2019 using rates that included the grid access charge. We recalculated the revenue for TVA and for each customer for FY 2019 using the energy rate structure that did not include the grid access charge. We then compared the calculations to determine if the difference was revenue neutral.

This evaluation was performed in accordance with the Council of the Inspectors General on Integrity and Efficiency's *Quality Standards for Inspection and Evaluation*.

FINDING

We determined the implementation of the grid access charge was revenue neutral because it resulted in an immaterial change to TVA's revenue. We identified a difference in revenue of less than \$2 million for the 79 LPCs that implemented the grid access charge in FY 2019. Our calculation of FY 2019 energy revenue for the 79 LPCs was \$3.216 billion, while our calculation without the implementation of the grid access charge for those 79 LPCs was \$3.218 billion.

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This report is for your review and information. No response to this report is necessary. If you have any questions or wish to discuss our observations, please contact Lindsay J. Denny, Evaluations Manager, at (865) 633-7349 or E. David Willis, Director, Evaluations at (865) 633-7376. We appreciate the courtesy and cooperation received from your staff during the evaluation.

A handwritten signature in black ink that reads "David P. Wheeler". The signature is written in a cursive style with a large, stylized "D" and a long, sweeping underline.

David P. Wheeler
Assistant Inspector General
(Audits and Evaluations)

LJD:FAJ

cc: TVA Board of Directors
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OIG File No. 2020-15712