

**BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN**

Payment in Lieu of Taxes (PILOT) Calculation for Municipal Utilities	5-GF-215
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**COMMENTS OF
JOINT INDUSTRIAL CUSTOMERS
(WI INDUSTRIAL ENERGY GROUP, WI PAPER COUNCIL)
REGARDING THE DRAFT STAFF REPORT**

**I.
Introduction**

The Joint Industrial Customers, collectively the Wisconsin Industrial Energy Group (WIEG) and the Wisconsin Paper Council (Paper Council), appreciate the opportunity to submit these comments regarding the draft *Investigation into Municipal Utility Payment in Lieu of Taxes (PILOT) – Staff Report* prepared by the Public Service Commission of Wisconsin (PSCW) in the above captioned docket.

WIEG represents over 30 large companies with operations in Wisconsin which employ approximately 50,000 people. WIEG's membership includes a diverse range of sectors including automobiles, chemicals, food processing, fabricating, metal casting, malting and pulp and paper. Some of these firms are the largest customers of the state's municipal water and electric utilities.

The Paper Council is the trade association of the pulp, paper and allied industry in Wisconsin. It is comprised of 19 companies which are manufacturers of pulp and paper products and approximately 75 companies which are suppliers of goods and services to the industry. Wisconsin is the nation's leading paper making state. In

existence since 1848, Wisconsin's paper industry employs more than 32,000 individuals and is the largest sector of the state's forest products industry.

The Joint Industrial Customers share the concern highlighted in the Commission staff's draft report that PILOTs are a significant portion of a water utility's revenue requirement as is evidenced by the data that indicates, on average, close to 15% of the revenue requirement of water utilities is associated with PILOTs. These payments – clearly subsidies – result in significant deviations from the cost of providing water service. The Joint Industrial Customers have consistently advocated for aligning rates closely with the cost to serve in electric utility-related issues – our advocacy remains the same here. We respectfully urge the Commission to investigate the issues in order to produce necessary reforms to municipal water pricing.

II.
**PILOT Program is a Serious Concern for
Businesses Dependent on Municipal Water**

The Joint Industrial Customers appreciate the PSCW's timely investigation into the PILOT program and its production of an informative draft report. We believe the PSC staff has done an outstanding job providing pertinent background to the PILOT program and highlighting contemporary issues of interest to stakeholders. We commend the PSC staff.

The Joint Industrial Customers view the draft report as the impetus for a continuing and expanding dialogue among all stakeholders regarding PILOT program purposes, policies and outcomes. The PSCW's investigation should serve as a platform that will build to an in-depth exploration of the PILOT program, including municipalities'

present reliance on PILOTs, and the serious concerns this raises for the subset of industrial water users most dependent on municipal water.

It should be understood that the Joint Industrial Customer's individual members rely on municipal water service to greater and lesser degrees. For example, some companies are able to access necessary water supplies through non-municipal sources such as surface water and private wells. Others, however, are substantially dependent on municipal water service, including those that rely on their local municipality for 100 percent of their needs.

It should also be understood that the paper industry typically returns about 88 percent of the water it requires, back to the environment¹. Since 1995, the volume of water discharged by paper companies nationally (a surrogate for water use) has decreased by almost 21 percent. Because of the importance of water to papermaking and other industrial activities, a water conservation ethic is characteristic of the firms represented by the Joint Industrial Customers.

These comments reflect the concerns of those Joint Industrial Customers that are entirely or substantially dependent on municipalities for reliable, economical water services at cost-based rates.

III. Cost-Base Rates, Free of Subsidies, Are Critical to Business

After reading the PSC's draft report, it should be no surprise that the crux of the Joint Industrial Customer's concerns is the subsidy nature – its existence and its current magnitude – inherent in the PILOT program. In 2010 some 509 water utilities employed

¹ Water acquired from non-municipal sources typically is returned to the environment cleaner than when it entered the paper making process.

the PILOT program to collect more than \$87.3 million from customers. Last year, the total increased to more than \$92.8 million.² The water utilities' average PILOT payments amounted to close to 15% of the total revenue requirement in 2010 and 2011 – this is a significant deviation from the actual cost of water service.³

Further, it is not clear why the percentage ranges are so large and varied. As an extreme case, there are some water utilities where PILOTs are in excess of 40%.⁴ While it's not apparent what criteria water utilities used to determine these payments, it is very clear that these payments are not for water service.

These high percentages are problematic as they deviate significantly from the cost to provide water service, create over-pricing of the commodity, and send distorted price signals. Municipalities apparently subsidize local services or amenities – of their choosing, at their discretion – by charging water rates that are unsupportable by cost-of-service analyses or studies.

Regardless of the rationale for subsidies, this is contrary to regulatory principles established decades ago, and adhered to today: customers should receive accurate price signals – bills for service – that reflect, to the greatest extent possible, the actual cost to serve them. The service is water procurement and delivery; street maintenance or snow removal is not part of water service.

Generating double-digit percentage subsidies via water rates sends erroneous information to industrial personnel who attempt to mitigate, control or reduce costs in order to maintain their company's competitive abilities. Prices above cost whether for raw material, labor, debt service, equipment and infrastructure – or utilities such as

² Table 1, Page 5, Staff Report

³ Table 2, Page 7, Staff Report

⁴ See PSCW Draft Appendices

water service – promote erroneous decision making. That is a significant concern as these are important decisions that affect all facets of the firm: (a) how many men and women it can afford to employ, (b) whether it can afford to upgrade its equipment to improve productivity, conserve resources or improve its competitive abilities, (c) whether it can afford to engage in research and development, (d) whether it can expand its operations (thus expanding its contributions – for example, through tax payments and purchases of goods and services – that benefit the quality of life and socio-economics at the state, county and municipal levels), (e) indeed, whether it can afford to continue in business in any particular Wisconsin municipality.

Simply stated, payments in lieu of taxes may be perceived as valuable (albeit additive) contributions to municipal managers' budgets – but the “rest of the story” is that they distort the cost of water to companies that are dependent on water for their existence.

The situation is all the more pernicious as, speaking generally, customers do not have supplier choice if they are reliant on municipal water; there is one supplier of municipal water in the municipality.

In mentioning customer choice, please understand that the Joint Industrial Customers are not suggesting or flirting with deregulation of municipal water utilities in Wisconsin. But water rates, inflated by PILOT programs, do risk industrial customers considering what options they have in order to reduce or sever their dependence on municipal water. And that raises the specter of municipal utilities being forced to cover fixed costs while their customer base and sales decrease.

The multi-million dollar subsidies generated by PILOT programs would be a regulatory policy concern in any economic environment. But they become even greater concerns as Wisconsin businesses struggle to cope, to survive, in challenging economic times. The unprecedented slow recovery, from what is being termed the Great Recession, exacerbates the tax challenges being borne by Wisconsin businesses.

Thus a 15 percent PILOT component – or larger – in a water-dependent company's water bill can be a heavy counterweight impeding economic recovery progress and the economic growth so sought by the nation, the state and its municipalities.

IV. Subsidies are Counter-Productive to Rebuilding Water Utility Infrastructure

The Joint Industrial Customers are also concerned about the practical impact of inflated water rates on the ability of those municipalities that are facing costly projects to replace and/or upgrade aging infrastructure. The Joint Industrial Customers are concerned that municipalities succumbing to the use of water service as a means to subsidize other services hobbles their ability to budget responsibly for the future needs of their water utilities. Thus, we agree with Commission staff's concern that because water utilities are capital-intensive, the current method for calculating PILOTs may be a disincentive to replacing aging infrastructure and making improvements necessary to ensure adequate service.

A reflective observer may understand the path that has led Wisconsin municipalities to develop significant subsidization in their water rates and the attendant distortion of price signals to water customers. The Joint Industrial Customers believe

that a reflective person will come to the conclusion that now is the time to address the situation.

**V.
Recommendations of the Joint Industrial Customer**

The reality of distorted water rates used to subsidize services by Wisconsin's municipalities clearly is wide spread. It has harmful impacts on those Wisconsin businesses that rely the most on municipal water service.

Identification of equitable solutions requires prompt attention and an encompassing initiative. This is the bottom line "take away" message the Joint Industrial Customers submits to the PSCW.

The nascent thoughts of the Joint Industrial Customers regarding solutions include (a) termination of the PILOT program over a certain number of years to permit an orderly transition into a better regulatory mode, or (b) caps on PILOT levels.

However, the Joint Industrial Customers recognize this is a complex, multi-faceted issue. Thus, we respectfully urge the Public Service Commission to make a determination now that this is a serious issue which requires a concerted effort in order to identify – and implement – reforms. This is crucial to our members that are dependent on municipal water supplies.

It would be a short-sighted public policy response were Wisconsin to shirk or postpone this opportunity to correct a problem that is hampering important segments of its economy and business community.

Maintaining the status quo is not acceptable public policy; a commitment to identify and implement reform is essential.

The Joint Industrial Customers are ready to work with the Public Service Commission, government at all levels, and other stakeholders, to seek a responsible resolution. Thank you for focusing on this issue and for providing this opportunity for public comment.

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