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EXCEPTION
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COMMISSIONERS

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JEFF HATCH-MILLER, Chairman
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AZ CORP COMMISSION
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IN THE MATTER OF THE APPLICATION OF
ARIZONA PUBLIC SERVICE COMPANY FOR
APPROVAL OF ITS DEMAND SIDE
MANAGEMENT PROGRAM PORTFOLIO PLAN
AND RELATED PROGRAMS.

Docket No. E-01345A-05-0477

**RESPONSE TO STAFF'S INTERIM
REPORT AND EXCEPTIONS TO
THE RECOMMENDED OPINION
AND ORDER**

Arizona Public Service Company ("APS" or "Company") hereby submits this response to Commission Staff's ("Staff") Interim Report ("Staff Report"),¹ filed January 17, 2006, which addresses a portion of the Company's Application for Approval of its Demand Side Management ("DSM") Portfolio Plan ("DSM Portfolio Plan"), specifically, the Non-Residential Programs ("Non-Residential Programs").

While the Company is in agreement with much of the Staff Report, the Company requests that the Commission change two of Staff's recommendations. The first recommendation prohibits the Company from recovering its Planning and Administration expenses associated with the DSM Portfolio Plan in a timely manner. The Company has and will continue to incur these additional expenses; yet, Staff's recommendation precludes the Company from even seeking recovery of those prudently incurred costs for another thirteen months. Adopting Staff's recommendation would create an inequitable situation in which the Arizona Corporation Commission ("Commission") would require APS to implement comprehensive DSM programs, while prohibiting the Company from timely recovery of the very costs associated with the Commission's mandate.

¹ Commission Staff filed Staff's Notice of Errata on January 18, 2006 and Staff's Second Notice of Errata on February 3, 2006. References to the "Staff Report" are inclusive of all three filings.

1 Second, APS opposes Staff's recommendation that the Commission only provide
2 "interim" approval of the Non-Residential Programs, at least without clarification. APS
3 believes that an "interim approval" provides little regulatory certainty for the Company or its
4 customers regarding the Non-Residential Programs, because the scope and weight of the
5 "interim approval" recommended by Staff is unclear. Therefore, APS is requesting that the
6 Commission Decision either remove the adjective "interim" or at the very least, clarify that the
7 Company is entitled to recover its prudently incurred costs related to the Non-Residential
8 Programs, whether the approval provided in the Decision is "interim" or "final."

9 **I. Background**

10 Decision No. 67744 (April 7, 2005) adopted a Settlement Agreement, with modifications
11 that resolved the Company's rate request ("2004 Settlement"). In that Decision the Commission
12 ordered APS to spend \$48 million on approved eligible DSM-related items during calendar
13 years 2005 through 2007. Because the success of efficient DSM programs takes research,
14 planning, marketing, incentives, and time (i.e., a start-up phase), timely Commission approval of
15 such programs is essential to allow compliance with this mandate. When the 2004 Settlement
16 was originally developed, APS assumed it would have the full 2005 calendar year to begin
17 planning and implementing the DSM Portfolio Plan. However, by the time Decision No. 67744
18 was issued in April 2005, months of program development time were already lost.

19 To facilitate timely implementation of the new DSM programs, the Company filed the
20 DSM Portfolio Plan on July 1, 2005, more than a month earlier than required by Decision No.
21 67744. In conjunction with its DSM Portfolio Plan, APS also filed for approval of a DSM
22 Baseline Study on March 11, 2005; a DSM Energy Wise Low Income Program on June 6, 2005;
23 and a DSM Consumer Products Program on June 10, 2005.

24 While Staff was reviewing the DSM Portfolio Plan and associated programs, the DSM
25 Collaborative Working Group (consisting of parties to the 2004 Settlement, including Staff,
26 consumer and industry groups) continued to meet, as required by the Decision. Based upon the
27 further input from the DSM Collaborative Working Group, APS submitted a minor change to its
28

1 DSM Portfolio Plan on November 14, 2005. This change, which the DSM Collaborative
2 Working Group believed was necessary and consistent with practices in other states, provided
3 additional specificity to flexible language in the original DSM Portfolio Plan. The revision did
4 not result in any substantial changes to the July 1, 2005 filing; it merely clarified APS' request
5 for flexibility to manage program budgets in response to changing market conditions and
6 customer responses to program offerings. On November 21, 2005, the Company filed the
7 specific pages to be replaced in the DSM Portfolio Plan and related programs.

8 Having undertaken the tasks of planning, reviewing and assessing the feasibility of
9 multiple programs simultaneously, while developing the scope and level of funding for each
10 program and its components, the Company was cognizant of the arduous and time consuming
11 review necessary for approval. With that consideration, the Company took great efforts to
12 submit all of its applications in advance of the date established by the Decision and to respond
13 to discovery requests in a timely manner. In addition, the Company has continued its efforts to
14 meet the Decision's mandate to spend \$48 million to promote and implement cost effective
15 programs by year end 2007.

16 **II. Exceptions:**

17 **A. Recovery of Planning and Administrative Costs**

18 Staff has recommended that APS be prohibited from recovering reasonable and prudent
19 Planning and Administration expenses at this time, suggesting instead that APS could request
20 approval in a future filing. Restricting the recovery of Administrative and Planning costs—
21 costs that are essential for the development and implementation of new DSM programs—is
22 contrary to the terms of the 2004 Settlement and is clearly unfair to the Company.

23 The DSM Portfolio Plan, which was submitted to the Commission in July 2005, is
24 comprised of 10 programs that provide all customers with opportunities to participate in energy
25 efficiency programs. In the Staff Report, Staff acknowledged that the Company's DSM
26 Portfolio Plan was the most comprehensive plan that has been undertaken by APS in recent
27 years, and further recognized that implementing DSM programs of this size and scope is a new
28

1 experience for APS.²

2 It is clear that Staff recognizes the magnitude of the Company's planning and
3 administrative responsibilities in gearing up for the proposed Non-Residential Programs.
4 Indeed, planning is so critical that it was incorporated as part of the definition of "energy-
5 efficiency DSM in the 2004 Settlement."³

6 All of the Non-Residential Programs proposed by APS are new programs which require
7 significant development and planning such as program concepting; meeting with DSM
8 Collaborative Working Group to complete program concepts; engaging in the iterative process
9 of drafting and finalizing program plans; preparation of cost/benefit analyses, energy savings
10 calculations and avoid cost estimates; and working through the review and approval process
11 with Staff and the Commission. These initial costs are absolutely necessary to develop
12 successful programs. In addition, ongoing management and oversight is necessary to administer
13 the programs. In order to successfully comply with the mandates of Decision No. 67744, APS
14 has hired additional staff and consultants⁴ to do the comprehensive planning and to administer
15 these programs.

16 As set forth in the DSM Portfolio Plan, each of the DSM programs has a planning and
17 administration component, which includes the management of program budgets; management of
18 the Request for Proposal ("RFP") bidding process and oversight of the implementation
19 contractors (where applicable); program development and coordination; and general overhead
20 expenses. Another component of Planning and Administration is the facilitation of the DSM
21 Collaborative Working Group, whose purpose is to solicit and facilitate stakeholder input,
22 advise APS on program implementation, develop future DSM programs, and review DSM
23 program performance. The Company believes that all of the planning and administrative
24 responsibilities are essential to ensure the success of the programs. Other than the delay in
25 recovery of costs, Staff has not indicated that it has any concerns with the Company's ultimate
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27 ² Staff Report at 40.

³ Decision No. 67744, Attachment A at 8.

28 ⁴ Since Decision No. 67744, APS has increased its staff dedicated to DSM programs from approximately 1.25 people to 5.15, and has engaged a DSM firm with the expertise necessary to design DSM programs.

1 recovery of such costs.

2 Furthermore, in addition to the planning and administrative duties discussed above, Staff
3 has made a number of recommendations that will require additional administrative resources.

4 Those recommendations include:

- 5
- 6 • APS should refile the Non-Residential portion of its DSM Portfolio Plan within 12 months
7 for final Commission approval. The 13-month refiling should include information on the
8 status of programs and explain changes that were made to budgets, incentive levels, and
9 program implementation. In addition, APS should also file detailed information regarding its
10 Planning and Administration budget and expenses for consideration at that time. The study
11 should include Societal Cost Test analyses utilizing the new baseline data.⁵
 - 12 • APS should provide 13-month refiling information about the level of school participation in
13 all DSM programs in the 13-month refiling recommended by Staff.⁶
 - 14 • APS should track the use of School Program funds by size of school entity and report such
15 findings in its semi-annual DSM reports as well as in the 13-month refiling recommended
16 by Staff.⁷
 - 17 • APS should continually assess opportunities to increase funding levels for schools based on
18 feedback from the DSM collaborative, school representatives and officials, and the results of
19 overall program performance. APS should provide information about its efforts to increase
20 funding for schools in APS' semi-annual reports and the 13-month refiling that is being
21 recommended by Staff.⁸
 - 22 • APS should identify the number of instances that incentives were paid for studies for which
23 associated projects were not completed through the verification process. This information
24 should be provided in APS' semi-annual reports and in the 13-month refiling that Staff is
25 recommending.⁹
 - 26 • Within 90 days after approval, APS must submit a detailed marketing plan for Staff review.
27 The marketing plan should, at a minimum, include all program marketing budget items and
28 their anticipated expenses, details on the divisions of marketing activities between APS and
contractors, and the types of marketing pieces that APS plans to develop to promote the
Non-Residential Programs. Staff further recommends that APS provide copies of all
marketing material for Staff review within 30 days of the development of each piece.¹⁰
 - APS should inform the DSM Collaborative Working Group of progress and significant
changes to budgets and incentives no later than four months after approval of the Non-

26 ⁵ *Id.* at 41.

27 ⁶ *Id.* at 35.

28 ⁷ *Id.*

⁸ *Id.*

⁹ *Id.* at 36.

¹⁰ *Id.* at 37.

1 Residential programs.¹¹

2 Staff's recommendation to delay cost recovery disregards the fact that a significant
3 amount of costs for Planning and Administration have been incurred during the initial planning
4 and development stages, and that, as a result, APS has already incurred approximately \$540,000
5 in costs for 2005.¹² These costs are ongoing and will continue to accumulate.

6 It is simply unfair to assume that the Company should hire the necessary staff and
7 engage outside contractors to implement these programs, without the ability to recover the costs
8 in a timely manner. Staff's recommendation would essentially preclude APS from recovering
9 its costs for at least 22 months (since issuance of Decision No. 67744) after those costs have
10 been reasonably and prudently incurred. APS, therefore, requests that the Commission allow for
11 concurrent recovery of planning and administration expenses.

12 **B. Interim approval**

13 Staff has recommended that the Commission only provide "interim" approval of the
14 Non-Residential Programs because they are new programs and additional information regarding
15 the programs will be available in the future. The Staff has further recommended that the
16 Company be ordered to refile the non-residential portion of the DSM Portfolio Plan, with 12
17 months of actual data for final Commission approval. It is unclear why an "interim" process is
18 recommended in this situation, when Commission has historically approved new programs, and
19 has simply required the company to file future reports for Staff review. The Commission
20 always has the prerogative to take further action.

21 Nonetheless, Staff has recommended an interim approval, which in the Company's
22 opinions creates uncertainty as to the final outcome of the proposed Non-Residential Programs.
23 Furthermore, the uncertainty caused by an "interim" approval may result in the reluctance on the
24 part of trade allies (contractors, builders, etc.) and customers to participate in programs they
25 believe may be temporary. This uncertainty affects the ability for APS customers to do long-

26 ¹¹ *Id.* at 40.

27 ¹² Such recommendation is contrary to Staff's own position in its February 7, 2005 Staff Report on Demand Side
28 Management Policy, which states, "to effectively implement programs, cost recovery shall be concurrent (on an
annual basis) with DSM spending." Staff Report on Demand Side Management Policy, issued February 7, 2005, at
12.

1 term planning for energy efficiency.

2 Therefore, the Company requests that the Commission grant final approval of its Non-
3 Residential Programs. In the alternative, the Company requests that the Commission clarify that
4 regardless whether the approval is "interim" or "final", that the Company is entitled to recover
5 prudently incurred costs related to the Non-Residential Programs.

6 **Conclusion:**

7 For all the reasons set forth above, APS requests that:

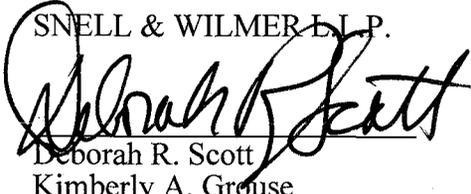
8 1) the Commission reject Staff's recommendations related to the delayed recovery of
9 Planning and Administrative costs and allow APS to immediately recover those prudently
10 incurred costs; and

11 2) the Commission give its "final" approval to the DSM Non-Residential Programs.

12 RESPECTFULLY submitted this 10th day of February, 2006.

13 SNELL & WILMER L.L.P.

14
15 By:


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19 Original and 14 copies filed this
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