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10 BEFORE THE ARIZONA CORPORATION COMMISSION

11 MIKE GLEASON, Chairman
12 WILLIAM A. MUNDELL
13 JEFF-HATCH MILLER
14 KRISTIN K. MAYES
15 GARY PIERCE

16 IN THE MATTER OF THE) Docket No. G-01551A-07-0504
17 APPLICATION OF SOUTHWEST GAS)
18 CORPORATION FOR THE) NOTICE OF FILING TESTIMONY
19 ESTABLISHMENT OF JUST AND)
20 REASONABLE RATES AND CHARGES)
21 DESIGNED TO REALIZE A)
22 REASONABLE RATE OF RETURN ON)
23 THE FAIR VALUE OF ITS)
24 PROPERTIES THROUGHOUT)
25 ARIZONA.)

Southwest Energy Efficiency Project ("SWEEP"), through its undersigned
counsel, hereby provides notice that it has this day filed the written direct testimony of
Jeffrey A. Schlegel in connection with the above-captioned matter.

Arizona Corporation Commission
DOCKETED
MAR 28 2008

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DATED this 28th day of March, 2008.

ARIZONA CENTER FOR LAW
IN THE PUBLIC INTEREST

By: 
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ORIGINAL and 13 COPIES of the
Foregoing filed this 28th day of
February, 2008 with:

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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

MIKE GLEASON, CHAIRMAN
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

IN THE MATTER OF THE APPLICATION OF
SOUTHWEST GAS CORPORATION FOR THE
ESTABLISHMENT OF JUST AND
REASONABLE RATES AND CHARGES
DESIGNED TO REALIZE A REASONABLE
RATE OF RETURN ON THE FAIR VALUE OF
ITS PROPERTIES THROUGHOUT ARIZONA.

Docket No. G-01551A-07-0504

Direct Testimony of

Jeff Schlegel

on behalf of

Southwest Energy Efficiency Project (SWEEP)

March 28, 2007

**Direct Testimony of Jeff Schlegel, SWEEP/NRDC
Docket No. G-01551A-07-0504**

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Introduction

Q. Please state your name and business address.

A. My name is Jeff Schlegel. My business address is 1167 W. Samalayuca Drive, Tucson, Arizona 85704-3224.

Q. For whom are you testifying?

A. I am testifying on behalf of the Southwest Energy Efficiency Project (SWEEP).

Q. Please describe the Southwest Energy Efficiency Project (SWEEP).

A. SWEEP is a public interest organization dedicated to advancing energy efficiency as a means of promoting both economic prosperity and environmental protection in the six states of Arizona, Colorado, New Mexico, Nevada, Utah, and Wyoming. SWEEP works on state energy legislation, analysis of energy efficiency opportunities and potential, expansion of state and utility energy efficiency programs as well as the design of these programs, building energy codes and appliance standards, and voluntary partnerships with the private sector to advance energy efficiency. SWEEP is collaborating with utilities, state agencies, environmental groups, universities, and energy specialists in the region. SWEEP is funded primarily by foundations, the U.S. Department of Energy, and the U.S. Environmental Protection Agency. I am the Arizona Representative for SWEEP.

Q. What are your professional qualifications?

A. I am an independent consultant specializing in policy analysis, evaluation and research, planning, and program design for energy efficiency and clean energy resources. I consult for public groups and government agencies, and I have been working in the field for over 20 years. In addition to my responsibilities with SWEEP, I am working or have worked extensively in many of the states that have effective energy efficiency programs, including California, Connecticut, Massachusetts, New Jersey, Vermont, and Wisconsin. In 1997, I received the Outstanding Achievement Award from the International Energy Program Evaluation Conference. I have testified before the Arizona Corporation Commission in many proceedings.

Q. What is the purpose of your testimony?

A. In my testimony I will discuss the public interest in increasing natural gas energy efficiency, summarize the performance of gas energy efficiency programs in other

states, propose an increase in funding for the Demand Side Management (DSM) programs of Southwest Gas, discuss the financial disincentive to natural gas utility support of energy efficiency, discuss decoupling mechanisms, and oppose higher fixed charges for Southwest Gas customers.

The Public Interest in Increasing Natural Gas Energy Efficiency

- Q. What is the public interest in increasing natural gas energy efficiency?
- A. Natural gas DSM energy efficiency programs are in the public interest. Increasing gas energy efficiency will provide significant and cost-effective benefits for Southwest Gas customers, the natural gas and electric utility systems, the economy, and the environment. Increasing natural gas energy efficiency will save consumers and businesses money through lower energy bills, resulting in lower total costs for customers. Natural gas energy efficiency programs will help mitigate fuel price increases and reduce customer vulnerability and exposure to natural gas price volatility. Increasing natural gas energy efficiency will also diversify energy resources, reduce air pollution and carbon emissions, and create jobs and improve the economy. Natural gas energy efficiency is a reliable energy resource that costs less than other resources for meeting the energy needs of customers in the Southwest Gas service territory.

There are many opportunities for cost-effective natural gas energy efficiency in the Southwest Gas service territory in Arizona, as evidenced by the programs Southwest Gas has implemented to date and the gas DSM programs in other states.

The Experience of Natural Gas DSM Programs in Other States

- Q. What is the experience with natural gas DSM programs in other states?
- A. Numerous gas utilities are implementing cost-effective DSM programs to help customers reduce their gas consumption and gas bills. One example is Questar Gas Company in Utah.

Questar began implementing gas DSM programs in Utah in 2007. The first year budget for Questar's programs was \$7.0 million. These programs included free home energy audits, rebates for residential efficiency measures including insulation and high efficiency heating equipment, incentives for construction of Energy Star new homes, a contribution to the state's low-income weatherization program, and consumer education efforts. Questar's DSM programs are cost-effective and were very successful in attracting participation and achieving the first year goals. As a result, Questar proposed expanding the programs in 2008 and proposed adding new programs for promoting more efficient gas use in the commercial sector and in multi-family housing. Questar's total gas DSM budget for 2008, which was approved in full by the Utah Public Service Commission, is \$10.5 million. This is equivalent to

over 1% of Questar's total revenues and about \$12.70 per customer. For reference, Questar serves a total of about 825,000 full service gas customers, fewer than the 945,000 gas customers Southwest Gas serves in Arizona (Southwest Gas, Schedule E-7). Other states where gas utilities are spending well over 1% of total revenues on energy efficiency programs include California, Iowa, and Wisconsin.

Increased DSM Programs and Funding

- Q. Does SWEEP support the current Southwest Gas DSM programs?
- A. Yes. SWEEP supports the natural gas DSM programs proposed in the prior rate case, as modified and approved by the Commission. As Staff analysis has shown, the Commission-approved programs are cost-effective and they are providing value and net benefits to customers. Southwest Gas expects 2008 DSM spending to be about \$2.9 million, which is part of the ramp up to full implementation of the programs, most of which were approved by the Commission in 2007. The 2009 DSM spending is expected to be at the \$4.4 million funding level approved by the Commission in the prior rate case.
- Q. Does SWEEP propose any revisions or increases to the DSM program efforts and funding for the Southwest Gas territory?
- A. Yes. SWEEP proposes that funding for the DSM portfolio of programs should be increased, to at least \$12 million annually, to better address the cost-effective opportunities throughout the Southwest Gas service territory. Additional DSM funding is necessary to capture energy efficiency opportunities and to assist more customers in reducing their energy bills.
- Q. How does the level of DSM effort and funding you propose for Southwest Gas compare to total revenues and DSM spending per customer?
- A. The SWEEP-proposed DSM program portfolio funding level of at least \$12 million is equivalent to 1.2% of total revenues and \$12.70 per customer, similar to the level of effort for Questar.¹ The current Commission-approved DSM program funding of \$4.4 million is equivalent to about 0.4% of total revenues and \$4.70 per customer.²

SWEEP recommends that the additional funding be used to expand existing programs to reach more customers. Also, additional cost-effective DSM programs could be considered for future years, and should be implemented if approved by the Commission in the future.

¹ \$12 million of DSM program portfolio funding divided by \$996.4 million of test year total revenues, per Southwest Gas Schedule E-6.

² \$4.4 million of DSM program portfolio funding divided by \$996.4 million of test year total revenues, per Southwest Gas Schedule E-6.

- Q. Should the collaborative DSM working group review any program revisions or proposals for new programs?
- A. Significant program revisions and proposals for new programs should be reviewed by the collaborative DSM working group. Southwest Gas should be able to expand existing, approved programs without *requiring* review by the collaborative working group, though SWEEP recommends that Southwest Gas consult the working group for ideas on how to reach more customers with the DSM programs.

Financial Disincentive to Natural Gas Utility Support of Energy Efficiency

- Q. Does Southwest Gas experience a financial disincentive to its support of energy efficiency efforts when its customers respond and become more energy efficient?
- A. Yes. Traditional utility regulation links the utility's financial health to the volume of natural gas sold, resulting in a financial disincentive to invest in energy efficiency and other demand-side resources that reduce natural gas sales. For Southwest Gas, energy savings by customers (which are beneficial for customers) result in lower revenues for the company and threaten recovery of utility fixed costs. In general, this financial disincentive can reduce utility support and enthusiasm for cost-effective resources such as energy efficiency programs that minimize the long-term cost of providing service. It also could impede potentially crucial utility support for energy-efficiency standards, building energy codes, and other policies that serve societal interests and reduce energy use without requiring any direct utility investment.

The financial disincentive is particularly strong for natural gas utilities that have experienced an overall trend of declining gas usage per customer, which is the situation for Southwest Gas.

- Q. When should this financial disincentive be addressed?
- A. SWEEP believes that the issue of the financial disincentive to natural gas utility support of energy efficiency should be addressed in Arizona in a timely manner, in this proceeding. We believe this will be necessary if Arizona wants to fully tap the potential for its lowest cost natural gas resource – cost-effective energy efficiency improvements for customers.
- Q. Should a decoupling mechanism for Southwest Gas be implemented to remove the financial disincentive and encourage Southwest Gas to support additional increases in energy efficiency?

A. Yes. SWEEP supports decoupling mechanisms to address issues related to energy efficiency, i.e., when such mechanisms would be effective in substantially increasing customer energy efficiency and reducing the financial disincentive to gas utility support of increased energy efficiency. SWEEP is not in favor of decoupling solely or primarily as a mechanism for the utility to recover authorized fixed costs. Therefore, in SWEEP's view the implementation of decoupling is premised on substantial increases in customer energy efficiency, for which the decoupling mechanism would reduce the financial disincentive to the utility of such increased energy efficiency.

Q. Do you support any of the decoupling mechanisms proposed by Southwest Gas?

A. Yes. SWEEP supports the intent and design of the Revenue Decoupling Adjustment Provision (RDAP) proposed by Southwest Gas. This decoupling mechanism, if approved and implemented, would be effective in meeting the objectives set forth by SWEEP above. It is also similar to the decoupling mechanism approved in Utah for Questar Gas. SWEEP has a few outstanding questions on the specific design and operation of the RDAP mechanism, which SWEEP is addressing through discovery.

Q. Are there other actions that could be taken to ease the transition to the RDAP decoupling mechanism?

A. Yes. SWEEP suggests that the implementation of the RDAP decoupling mechanism could be a three-year pilot, with evaluation and review at the end of the pilot prior to full implementation. Also, to help reduce or address the concerns of other parties, an initial maximum cap could be placed on any revenue or refund from any differences between actual and authorized non-gas revenue, if such a cap would reduce some of the uncertainty regarding the effects of the mechanism.

Q. Is your proposal for increased DSM funding conditioned on approval of the RDAP decoupling mechanism?

A. No. SWEEP recommends the increase in DSM funding with or without approval of a decoupling mechanism. Increasing natural gas energy efficiency will provide significant and cost-effective benefits for Southwest Gas customers, the natural gas and electric utility systems, the economy, and the environment

Fixed Charges

- Q. Should the Commission approve higher fixed charges for Southwest Gas?
- A. No. SWEEP opposes higher fixed charges for natural gas customers because higher fixed charges would mute and reduce the price signal customers would receive when they reduce energy use and become more energy efficient, and therefore would reduce the power they have over their own energy bills.

Conclusion

- Q. Does that conclude your direct testimony?
- A. Yes.