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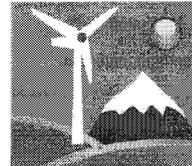


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DATE: August 29, 2008

RE: Comments on Investigation of Regulatory and Rate Incentives for Gas and  
Electric Utilities – **Docket Nos. E-00000J-08-0314 and G-00000C-08-0314**

On August 1, 2008, Staff requested comments to assist it in defining the scope of its inquiry in this docket. This docket represents an opportunity for the Commission to accelerate the adoption of technologies and programs that will result in environmental improvements and long term economic benefits to Arizona ratepayers such as more stable energy prices, lower rates, and lower energy service bills.

Western Resource Advocates (WRA) and Interwest Energy Alliance (Interwest) provide partial answers to the following questions posed by Staff:

1. *What basic incentives and disincentives does today's regulatory structure ... provide to Arizona electric and gas utilities?*
6. *Can the regulatory incentive structure be changed to align a utility's financial incentives with energy efficiency investment?*
8. *Can incentives play a role in Arizona efficiently meeting its future utility infrastructure needs?*
9. *Should the Commission consider "decoupling" mechanisms for electric and gas companies? If so, what type of decoupling?*
12. *What are the best practices across the nation regarding regulatory incentives?*
13. *Are there any other specific topics that should be covered in the inquiry?*

With regard to **Question 1**, the implicit incentive under traditional regulation is to minimize innovation and instead continue with past practices, thereby delaying beneficial investments in clean energy technologies. Examples of potential disincentives are listed below.

- Because utilities expect that they may not recover their costs under traditional ratemaking, they will under-invest in renewable energy resources, including technologies that are commercially available and technologies that are not yet commercially available but which may be beneficial over the long run.
- Utilities often acquire renewable energy through purchased power agreements. Though there may be advantages to doing so, the utility does not receive a return on the capital investment, making renewable energy projects less profitable than utility-owned generation such as gas- or coal-fired power plants.
- Under traditional regulation, utilities incur financial disincentives to large scale energy efficiency programs as they forego revenues with each MWh or therm saved without receiving offsetting income for good performance.

In response to **Questions 8 and 13**, Commission review and pre-approval of new technologies that have long term environmental or economic benefits can be a useful way to remove disincentives to innovation. The Commission does pre-approve energy efficiency programs and approves implementation plans for renewable energy resources under the Renewable Energy Standard. To encourage technological innovation and early adoption of new technologies, we recommend that this docket also address Commission pre-approval of early adoption of new technologies that potentially provide significant long-term environmental or economic benefits. Pre-approval should give utilities assurance of cost recovery for early adoption of new renewable energy and energy efficiency technologies.

With regard to energy efficiency programs (**Questions 6, 9, and 12**), we believe that the Commission should consider performance incentives and other mechanisms to: a) remove financial obstacles to large scale utility efficiency programs, and b) create incentives for utilities to design and implement large scale, cost effective efficiency programs. Crafting new policies requires balancing ratepayer and shareholder interests. WRA anticipates filing a detailed review of these issues and specific recommendations in the current Arizona Public Service Company rate case (Docket No. E-01345A-08-0172).

Lastly, we request that Staff and interested parties discuss how the information gathered in this docket will be used. For example, should the Commission adopt a broad policy to be applied in rate cases? Should the Commission consider adopting a rule to promote utility innovation?

*Original and 15 copies filed with Docket Control, August 29, 2008.*