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June 3, 2009

Docket Control
Arizona Corporation Commission
1200 West Washington
Phoenix, AZ 85007

RE: INVESTIGATION OF REGULATORY AND RATE INCENTIVES FOR GAS & ELECTRIC UTILITIES
DOCKET NOS. E-00000J-08-0314 and G-00000C-08-0314

Attached please find Arizona Public Service Company's proposed comments and Energy Efficiency Rules.

If you have any questions or concerns, please call Jeff Johnson at 602-250-2661.

Sincerely,

Leland R. Snook

Attachment

LRS/dst

Cc: Ernest Johnson
Brian Bozzo
Terri Ford
Barbara Keene
Julie McNeely

Arizona Public Service Company's
Proposed Energy Efficiency Rules
Docket Nos. E-00000J-08-0314 & G-00000C-08-0314
June 3, 2009

BACKGROUND

On June 19, 2008, the Arizona Corporation Commission ("Commission") opened Docket Nos. E-00000J-08-0314 & G-00000C-08-0314 for the Investigation of Regulatory and Rate Incentives for Gas and Electric Utilities to develop Commission policy goals on the matter of energy efficiency. On January 1, 2009, Chairman Mayes issued a letter recommending that a workshop be established to explore how best to expand energy efficiency efforts, taking the needs of consumers and utilities into consideration. During the months of March, April and May 2009, Staff held a series of workshops and technical working group meetings to develop Energy Efficiency Rules (the "Rules"). Staff requested that interested parties submit draft rules by June 3, 2009, for their consideration. Also, at the May 29, 2009 technical working group meeting, Staff requested that interested parties file comments on the energy efficiency provisions of Section 532 of the federal Energy Independence and Security Act of 2007 ("EISA"). Staff intends to present an energy efficiency rulemaking package to the Commission by early July.

The following comments and proposed rules are provided by Arizona Public Service Company ("APS" or "Company") in response to Staff's request. In developing its proposed rules ("APS Proposed Rules"), the Company primarily considered Staff's First Draft of Proposed DSM Rules, which was docketed April 15, 2005,[1] the Commission's Renewable Energy Standard Rules,[2] and the New Mexico proposals to amend the New Mexico Energy Efficiency Rule.[3] Relevant portions of those documents have been incorporated into the APS Proposed Rules.

Introduction

APS is the leading provider of Demand-Side Management ("DSM") programs in Arizona. Its current portfolio of nine energy efficiency programs has been very successful.[4] In addition, APS has identified DSM as a key component to provide for customers' future energy needs in the Resource Plan filed earlier this year.[5] In fact, a recent study by the American Council for an

[1] Docket No. RE-00000C-05-0230.
[2] A.A.C. R14-2-1801 through 1816.
[3] *In the Matter of a Rulemaking to Revise NMPRC Rule 17.7.2 NMAC to Implement the Efficient Use of Energy Act*, Amended Notice of Proposed Rulemaking issued March 12, 2009, New Mexico Public Regulation Commission, Case No. 08-00024-UT
[4] Customers are expected to benefit by $500 million in estimated savings on participating customer bills over the expected life of all energy efficiency measures; a cumulative annual 565,000 megawatt hour ("MWh") savings, which is the equivalent to the electricity used by more than 40,000 average households for a year; approximately 80 megawatts ("MW") of peak demand was saved; and over two million tons of carbon dioxide ("CO_2") emissions are anticipated to be reduced. For the past three years, APS has received several national awards for excellence in energy efficiency program delivery. Figures are as of the end of 2008.
[5] The APS Resource Plan calls for twice the energy savings by 2025 than would be achieved with APS's current funding levels. As part of its resource planning process, APS analyzed several energy efficiency scenarios as documented in the "2009 Resource Plan Report", which was filed on January 29, 2009 (Docket No. E-01345A-09-

Energy Efficient Economy ("ACEEE")[6] puts APS's existing DSM program achievements in context. The ACEEE study analyzed the 14 leading states in energy efficiency and their level of DSM savings as a percent of retail sales. The study found that the median achievement among these top states was an annual savings level equal to 0.7% of retail energy sales – less than the level currently being achieved by APS. In fact, the level of energy efficiency that APS achieved in 2008 is equal to 0.8% of retail energy sales, which places APS's current achievements above the median level of the leading states in energy efficiency. APS's level of savings, if achieved statewide, would tie Arizona for sixth on the ACEEE list of leading states.

The Company recognizes the positive impacts of energy efficiency, including reduction in fuel costs and carbon emissions, as well as the potential to defer certain investments in generation and transmission infrastructure over the long-term. However, the full value of these benefits will be difficult to realize if the interests of customers and utilities in implementing DSM are not aligned. Regulatory actions that address and minimize the financial disincentives are essential if utilities are to increase their investments in energy efficiency programs.

APS supports the development of a state-wide energy efficiency standard ("Energy Efficiency Standard" or "Standard"), as long as it is carefully developed with provisions to provide adequate and timely funding to achieve the Standard; that it accounts for a number of factors outside of the utility's control that can affect the ability to achieve the Standard through utility programs; and that it removes the utility's regulatory disincentives to implement a Standard.

APS is concerned about the uncertainty of costs related to an aggressive Energy Efficiency Standard, and the impact these costs may have on customers' rates. For example, APS is currently projecting program costs ranging from approximately $40 million in 2010 to over $300 million in 2020, for a total cost of over $2 billion during that 11-year term of the Standard.

Additionally, it should also be noted that the level of the Energy Efficiency Standard goals currently being contemplated is quite aggressive, as illustrated by the lower goals adopted in neighboring states, such as New Mexico, Colorado, and the recent ACEEE study cited above. The ACEEE study concluded that "[w]ith one exception (Vermont), no states are yet reporting energy efficiency savings at the higher levels being called for in a number of recent state policy decisions (i.e., in the range of 1.5% to 2.0-% per year)." Whether this level of savings can be achieved in Arizona over a sustained period is unknown at this point.

APS's current estimate of program costs is based on the Market Potential Study that was completed by ICF International in 2007.[7] The Market Potential Study estimated future energy efficiency potential and the costs for the twenty-year period from 2005 through 2025. The study

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0037). The energy efficiency scenarios were based on APS's Market Potential Study. The scenarios in the Resource Plan ranged from 4% to 15% of load by 2025, and were compared with the long term economics of conventional generation resources in a consistent manner. These were further evaluated under a variety of scenarios relating to natural gas prices, carbon legislation, and the cost of implementing energy efficiency measures. Under the baseline conditions, the "optimum" amount of energy efficiency was found to be about 7% of load by 2025. Under high gas price, high carbon price, or low cost of energy efficiency measure scenarios, it was found that up to 15% of load by 2025 may be economically justified.

[6] *Meeting Aggressive New State Goals for Utility Sector Energy Efficiency* (March 2009).

[7] This study was filed on September 12, 2007 (Docket No. E-01345A-05-0182).

made a "point in time" estimate of market potential because of the difficulty in predicting future technologies and market conditions. A wide variety of energy efficiency technologies for all common end uses and customer segments were examined in this comprehensive study. The Market Potential Study is the most recent assessment that has been done specifically for the Arizona market and climate. The program cost estimates from this study, while realistic, are also highly uncertain. Actual program costs for each year of implementation will provide the best experience to inform whether these program costs estimates are too high or too low.

The Energy Efficiency Standard must be carefully developed, as it has unique planning challenges. Customer involvement is critical to the success of DSM – if customers do not participate, the Standard will not be met. Even demand response programs will falter without customer participation. Therefore, in establishing an Energy Efficiency Standard, outside factors, such as the current economic downturn which can impact customer participation, must be taken into consideration. APS Proposed Rules include an annual implementation plan process which would allow the Commission to adjust for these outside factors.

Section 532(a)(16) of the EISA provides that each electric utility shall integrate energy efficiency resources into utility, state, and regional plans, and adopt policies establishing cost-effective energy efficiency as a priority resource. Section 532(a)(17) also states that the rates allowed to be charged by any electric utility shall align utility incentives with the delivery of cost-effective energy efficiency, and promote energy efficiency investments. APS Proposed Rules are consistent with and conform to the federal energy efficiency laws. If the Commission adopts APS Proposed Rules and subsequently removes the regulatory disincentives in future rate cases, APS believes that the factors that each state regulatory authority must consider (in Section 532(a)(17)(B) of EISA) regarding rate design modifications to promote energy efficiency investments will be satisfied. Accordingly, APS recommends that the Commission adopt the amended PURPA standards in the EISA.

The Rules must provide for customer incentives and rebates that are sufficient to motivate customers to participate; provide flexibility necessary to adapt to market and economic conditions; provide utilities with full and timely cost recovery for DSM programs; provide for the removal of regulatory disincentives for utilities; and allow the Commission the ability to take into consideration these and other relevant factors on a year-by-year basis. The APS Proposed Rules address these issues.

OVERVIEW

The Energy Efficiency Standard

APS recommends that the Commission set an Energy Efficiency Standard, as outlined in these comments, that represents an 18% reduction in retail energy sales by the year 2020 through a combination of utility programs and energy efficiency building codes and appliance standards. Under the APS Proposed Rules, the Energy Efficiency Standard from utility activities would be a 15% reduction in retail energy sales by the year 2020 with 3% reduction coming from building codes and appliance standards. Demand response may comprise up to 3% (3 percentage points) of the 15% utility program standard. For purposes of compliance with the Standard, APS

proposes that the peak load reduction capability from demand response would be converted to an annual energy equivalent, based on an assumed 50% annual load factor. A utility's energy reductions from DSM programs beginning in January 2005 would be counted towards the Standard.

If the Commission desires a higher Standard, then APS recommends that the Standard be based on the reduction in retail energy sales compared with retail energy sales in 2005 – the first year that DSM energy reductions count towards meeting the Standard, similar to the New Mexico approach.

APS is proposing that annual guidelines be established to provide a benchmark to compare each utility's progress toward meeting the 2020 Energy Efficiency Standard. To allow for flexibility to respond to economic and market conditions, the actual performance in a given year may be above or below the guideline. The annual guidelines, expressed as a percent reduction in retail sales, are proposed as follows:

Year	Cumulative Annual Energy Guideline % Retail Sales
2010	1.00%
2011	2.25%
2012	3.75%
2013	5.00%
2014	6.50%
2015	8.00%
2016	9.50%
2017	10.75%
2018	12.00%
2019	13.50%
2020	15.00%

The savings from DSM measures that are installed during the years applicable to the Standard would be presumed to persist through the entire term of the Standard. Measures that expire before 2020 would be assumed to be replaced at similar or better efficiencies.

Cost Recovery

- **Program Costs**

Under the APS Proposed Rules, program costs and the performance incentive would be recovered concurrently with the program implementation. Utilities could recover the program costs and performance incentive associated with the Energy Efficiency Standard through an adjustor mechanism or a base rate component supplemented by an adjustor mechanism.

Program costs may be either expensed or deferred and amortized (capitalized) over time at the utility's election, as expressed in an annual implementation filing. If amortized, the annual

revenue requirements will be based on an interest rate equal to the utility's weighted average cost of capital and will be recovered over a period not to exceed five years. The annual revenue requirements will be recovered through an adjustor mechanism. If expensed, the total annual costs will be recovered through an adjustor mechanism based on the projected costs over the annual recovery period, subject to a true-up with interest in the subsequent period.

- **Aligning Customer and Utility Interests**

APS believes that it is essential that the Commission address the rate making and regulatory disincentives that are presented by the implementation of an Energy Efficiency Standard. These regulatory disincentives are related to the recovery of fixed costs of providing service to customers (wires, transformers, other transmission and distribution delivery costs, and other fixed costs). The utility incurs these costs whenever a customer is provided service through the utility's electric systems, regardless of the amount of energy that customer uses. Under traditional ratemaking principles, these fixed costs are primarily collected through a usage charge, which is based on the energy that the customer uses in any given month. In a rate case, the usage charge is typically based on assumptions of higher customer usage that do not reflect the impact of energy efficiency programs. However, between rate cases, if customer usage is reduced due to an expanded level of DSM, a portion of these fixed costs would be unrecovered.

If an Energy Efficiency Standard is adopted and usage is significantly reduced, ratemaking approaches must be modified to assure that utilities recover the fixed costs of serving their customers. A number of proposals have been discussed during the Commission's workshops, although there has been no consensus on the best way to resolve this issue. In order to meet the Commission's accelerated schedule and appropriately address this fundamental ratemaking issue, APS is proposing that the Commission adopt rate design and ratemaking methods that eliminate regulatory disincentives or barriers to utility implementation of energy efficiency programs. This is similar to that proposed in New Mexico's rulemaking docket. The APS Proposed Rules specify that the Commission would issue a final order removing regulatory disincentives or barriers no later than each utility's next rate case after the approval of the Energy Efficiency Standard.

The foregoing suggested language would merely be a statement of Commission policy no different than the other portions of the Rules. Although subject to modification by future Commission rulemaking, again just as would be all other aspects of the Rules, the requested language would represent a clear recognition by this Commission of the challenge created by regulatory disincentives and represent a present commitment to address and remove the disincentives at the earliest opportunity. This is not only consistent with, but APS would suggest a vital part of the overall intent of the Rules, which is to make Arizona a national leader in all aspects of energy efficiency. In fact, most of the leading states in energy efficiency already have effectively addressed these disincentives.[8] A secondary benefit of providing a direct tie between

[8] For example, California has for years had decoupling or similar programs in place for its gas and electric utilities. Decision 07-09-043 in Rulemaking 06-04-010 dated 4/13/2006, Decision 08-09-040 in Rulemaking 08-07-011, dated 9/18/2008. Massachusetts provides "lost base revenue" recovery currently, but is moving to full decoupling. D.P.U. Order 07-50-A, dated July 16, 2008. Connecticut implemented decoupling as of January 1, 2009. Decision in Docket No. 07-10-03 dated 6/19/08; Decision in Docket No. 08-07-04 dated 2/4/2009. Vermont uses

the Rules and future ratemaking actions would be to strengthen the argument that the Rules are themselves incident to the Commission's Constitutional ratemaking authority, and thus less susceptible to any potential legal challenge.

To help alleviate a portion of the rate making disincentives before they are addressed as described above, an initial recovery mechanism will be implemented for each year based upon the energy savings achieved by the utility multiplied by a per kWh incentive. This mechanism will equal the lifetime energy savings for measures installed in that year times $0.0025 per kWh. The equivalent energy from demand response programs will not be applicable to this mechanism.

- **Adjustor Mechanism**

The APS Proposed Rules include an adjustor mechanism, which would be adjusted annually as part of the implementation process. The adjustor would be based on the projected program costs, performance incentive, and unrecovered fixed costs (if applicable) over the annual recovery period, subject to a true-up with interest in the subsequent period.

Performance Incentive

APS is proposing an annual performance incentive for energy efficiency, which would be tiered as a percent of net benefits, and capped at a tiered percent of program costs. The chart below depicts the Company's proposal. The annual performance incentive would be based on the achieved annual energy reduction relative to an annual guideline, which would be established in the utility's implementation plan. While the equivalent energy savings from demand response programs would be counted toward the annual guideline, the net benefits from demand response would not be included in the performance incentive.

Achievement Relative to MWh Guideline	Incentive as a Percent of Net Benefits	Capped at a percent of Program Costs
Less than 85%	0%	0%
85% to 95%	6%	12%
96% to 105%	7%	14%
106% to 115%	8%	16%
116% to 125%	9%	18%
Greater than 125%	10%	20%

"Alternative Rate Plans" that adjust base rates annually using forecasted sales volumes to address ratemaking disincentives. Order in Docket Nos. 7175 and 7176, dated 12/22/2006. Wisconsin has approved a pilot "revenue-sales" decoupling program. Final Decision in 6690-UR-119 dated 12/30/2008. New York has historically provided net lost revenue recovery in rate cases, but is now requiring utilities to propose decoupling mechanisms. Order in Case 07-M-0548 dated 6/23/2008. Oregon has approved decoupling and lost revenue recovery for Portland General Electric. Order No. 09-020 in Docket UE 197, dated 1/22/2009. Minnesota has determined that decoupling will be adopted to encourage energy efficiency. MSA § 216B.2401, 2412. *See also* EISA Section 532(a)(16) and (17).

PROCESS

APS believes that the process for implementation under the Renewable Energy Standard Rules is effective, and for consistency, should be adopted for an Energy Efficiency Standard. Under the APS Proposed Rules, within sixty days of the effective date of Energy Efficiency Rules, utilities would apply for a new tariff or changes to an existing adjustor mechanism for recovering the reasonable and prudent costs of complying with the Rules. Beginning June 1, 2010, and every June 1st thereafter, electric utilities would file an annual implementation plan for Commission review and approval. The implementation plan would include a description of the utility's compliance with the requirements of the Energy Efficiency Rules for the previous calendar year, and a plan that describes how the utility intends to comply with the Rules for the next calendar year, including any necessary adjustments to the Energy Efficiency adjustor mechanism. As part of that process, the Commission would adopt modifications to the utility's energy efficiency adjustor mechanism that would become effective on January 1st of the following year.[9] APS proposes that the implementation plan and compliance reporting described above replace the current reporting requirements.

CONCLUSION

APS supports the development of state-wide Energy Efficiency Rules for all jurisdictional utilities that are consistent with the energy efficiency provisions of EISA. In its consideration of such Rules, the Commission should be cognizant of the potential cost of attaining targeted levels of energy efficiency, and the impact of such costs on utility customers. And to be effective at any level, but especially the aggressive levels of energy efficiency being considered in this proceeding, the Energy Efficiency Standard must include provisions for adequate and timely funding to achieve the Standard and address removal of the regulatory disincentives to achievement. Finally, the Standard should acknowledge that there are numerous factors outside the utility's control that can affect the ability to achieve the Standard through utility activities alone.

[9] If having all utilities on the same schedule proves to be overly burdensome to the Commission, the Rules could be modified to allow staggered filings using non-calendar program years for some utilities.

ARIZONA PUBLIC SERVICE COMPANY'S
PROPOSED ENERGY EFFICIENCY RULES

ARTICLE ___. ENERGY EFFICIENCY STANDARD

APPLICABILITY

These rules shall govern the advancement and implementation of cost-effective and prudent demand-side management initiatives for all electric and natural gas utilities subject to the jurisdiction of the Commission.

R14-2-_____. Definitions

A. "Achievable" means those energy efficiency or load management resources available to the utility using its best efforts and considering a reasonable level of customer participation.

B. "Adjustor Mechanism" means a rate schedule which can be changed periodically outside of a general rate case to reflect changes in specific costs incurred by a utility, performance incentives earned by the utility, and other items allowed for recovery.

C. "Affected Utility" means a public service corporation serving retail electric or natural gas load in Arizona.

D. "Annual Energy Efficiency Guideline" means the cumulative annual kWh energy reduction from approved Demand-Side Management programs expressed as a percent of actual retail kWh sales, which is used to track progress towards the Energy Efficiency Standard.

E. "Commission" means the Arizona Corporation Commission.

F. "Customer" means an Affected Utility customer at a single, contiguous field, location or facility, regardless of the number of meters at that field, location or facility.

G. "Demand Savings" means the load reduction occurring during the relevant peak period(s) as a direct result of Energy Efficiency and Demand Response programs.

H. "Demand-Side Management ("DSM")" means the planning, implementation, and evaluation of programs to shift peak load to off-peak hours, to reduce peak demand ("kW"), and/or to reduce energy consumption ("kWh" or "therms") in a cost-effective manner. DSM may include energy efficiency, load management, and demand response.

I. "Demand Response" means all intentional modifications to electric and natural gas consumption patterns of customers affecting the timing or quantity of customer demand and usage. Demand response programs are used to reduce customer energy usage in response to prices, market conditions, or threats to system reliability. Demand response programs may include, but are not limited to price-responsive demand bidding, contractually obligated curtailment, voluntary curtailment, direct load control/cycling and pricing options, such as time-of-use, critical peak pricing, peak time rebates, and real-time pricing.

J. "Energy Efficiency" means products, services, practices and educational programs aimed at saving energy in end-use applications generally by substituting technically more advanced (compared to what is presently used in a specific situation) equipment or practices or targeting customer behavior to produce the same or an improved level of end-use service with less energy use.

K. "Energy Efficiency Standard" means the overall goal for energy reduction from approved Demand-Side Management programs expressed as the cumulative annual energy reduction as a percent of actual retail kWh sales in some future year.

L. "Energy Savings" means the reduction in a customer's consumption of energy as a direct result of a DSM measure or program.

M. "Incremental Benefits" include, but are not limited to, avoided environmental impacts and the avoided fuel cost, purchased power cost, new capacity cost, transmission cost, and/or distribution cost.

N. "Incremental Costs" means the additional cost of DSM programs and measures relative to baseline cost.

O. "Measure Life" means the expected useful life of the energy efficiency measure being deployed.

P. "Market Transformation" means strategic efforts to induce lasting structural or behavioral changes in the market that result in increased adoption of DSM technologies, services, practices, and customer behaviors.

Q. "Measures" means the components of a public utility program, and includes any material, device, technology, educational program, pricing option, practice or facility alteration that makes it possible to deliver a comparable level and quality of end-use energy service while using less energy than would otherwise be required.

R. "Net Benefits" means incremental benefits resulting from DSM minus the incremental costs of DSM.

S. "Program" means one or more measures provided as part of a single offering to customers.

T. "Program Costs" are the costs incurred by an Affected Utility as a result of developing, marketing, implementing, administering, and evaluating approved DSM measures and programs.

U. "Retail Energy Sales" is the Affected Utility's actual measured kWh sales to jurisdictional retail customers.

V. "Self-direction" means an option made available to qualifying customers of sufficient size, in which a portion of the amount of money paid by each qualifying customer toward a DSM adjustor is tracked for an individual customer and is made available for use by the customer for DSM investments upon application by the customer.

W. "Tariff" means a Commission-approved rate designed to recover an Affected Utility's reasonable and prudent costs of complying with these rules.

X. "Unrecovered Fixed Costs" result when fixed costs, such as a utility's investment in distribution and transmission infrastructure, which are recovered through volumetric charges, are not recovered because a customer's kWh monthly consumption is reduced from DSM programs.

R14-2-_____. Objectives

A. The following objectives shall be considered in the advancement and implementation of cost-effective, achievable and prudent DSM initiatives:

1. Achieve cost-effective energy savings and peak demand reductions.

2. Advance market transformation to achieve cost-effective DSM benefits through approaches that achieve sustainable savings and reduce the need for future market interventions.
3. Ensure timely recovery of program costs and performance incentives and provide adequate program funding to achieve the DSM targets.
4. Align utility and customer interests by removing financial disincentives to the utility from implementing DSM programs.
5. Implement DSM programs that provide an opportunity for all Affected Utility customer segments to participate, including low-income customers.

R14-2-_____. Energy Efficiency Standard and Annual Energy Efficiency Guideline

A. The Energy Efficiency Standard is a reduction of retail energy sales by 18% by the year 2020 through a combination of utility activities and energy efficiency building codes and appliance standards.

B. The Commission recognizes that building codes, appliance efficiency standards, shared savings legislation, and actions in other forums are an important part of advancing the goals for increased DSM. Therefore, the Energy Efficiency Standard shall include an expected reduction of retail energy sales by 3% by the year 2020 from energy efficiency building codes and appliance standards.

C. The Affected Utility shall reduce Retail Energy Sales by fifteen percent (15%) by the year 2020 from utility activities.

D. The Affected Utility's sales reductions from DSM programs beginning in January 2005 will be counted toward the Energy Efficiency Standard.

E. Demand response may comprise up to 3% (3 percentage points) of the 15% utility program standard. For purposes of compliance with the Standard, the peak load reduction capability from demand response will be converted to an annual energy equivalent, based on an assumed 50% annual load factor.

F. Energy savings from efficiency improvements to the delivery system will count toward meeting the Energy Efficiency Standard from utility activities.

G. The Energy Efficiency Standard allows for self-direction for large customers and the resulting MWh saved will be counted toward the utility portion of the Energy Efficiency Standard.

H. The savings from DSM measures that are installed during the years applicable to the Energy Efficiency Standard will be presumed to persist through the entire term of the Energy Efficiency Standard. Measures that expire before 2020 will be assumed to be replaced at similar or better efficiencies.

I. Annual Energy Efficiency Guidelines are established to provide a benchmark to compare the Affected Utility's progress toward meeting the 2020 Energy Efficiency Standard. The Annual Energy Efficiency Guidelines expressed as a percent reduction in retail sales are provided as follows:

YEAR	Annual Energy Efficiency Guideline % Retail Sales
2010	1.00 %

2011	2.25 %
2012	3.75 %
2013	5.00 %
2014	6.50 %
2015	8.00 %
2016	9.50 %
2017	10.75 %
2018	12.00 %
2019	13.50 %
2020	15.00 %

The increase in the annual percentage for each Affected Utility will be prorated based on when the Affected Utility's funding mechanism is approved.

R14-2-_____. Tariff

A. Within 60 days of the effective date of these rules, each Affected Utility shall file with the Commission a Tariff that proposes methods for recovering the reasonable and prudent costs of complying with these rules.

B. The Affected Utility's Tariff filing shall provide the following information:
   1. Financial information and supporting data sufficient to allow the Commission to determine the Affected Utility's fair value for purposes of evaluating the Affected Utility's proposed Tariff. Information required under R14-2-____ will be the minimum information necessary for filing a Tariff application, but Commission Staff may request additional information depending upon the type of Tariff filing that is submitted;
   2. Data to support the level of costs that the Affected Utility contends will be incurred in order to comply with these rules; and
   3. Any other information that the Commission believes will be relevant to the Commission's consideration of the Tariff filing.

C. The Commission will approve, modify, or deny a Tariff proposed pursuant to subsection (A) within 180 days after the Tariff has been filed. The Commission may suspend this deadline or adopt an alternative procedural schedule for good cause.

D. If an Affected Utility has an Adjustor Mechanism for the recovery of costs related to Annual Energy Efficiency Guideline, the Affected Utility may file a request to modify and reset its Adjustor Mechanism in lieu of a Tariff pursuant to subsection (A). The Affected Utility's filing shall provide all the information required by subsection (B), except that it may omit information specifically related to the fair value determination.

R14-2-_____. Implementation Plan and Compliance Reporting

A. Beginning June 1, 2010, and every June 1st thereafter, each Affected Utility shall file with Docket Control for Commission review and approval a plan that describes its accomplishments for the prior year and how it intends to meet the Energy Efficiency Guideline for the next calendar year.

B. The implementation plan (first example of Implementation Plan not capitalized, even though it is in the Comments document) shall include the following information:
   1. A description of the Affected Utility's compliance with the requirements of these rules for the previous calendar year;
   2. A plan that describes how the utility intends to comply with the rules for the next calendar year, including any necessary adjustments to the Adjustor Mechanism;
   3. A description of the DSM Programs and kWh and kW projected to be obtained from each of those Programs; and
   4. The estimated cost and cost per kWh of each DSM Program.

C. The Commission may hold a hearing to determine whether an Affected Utility's implementation plan satisfies the requirements of these rules.

D. The Affected Utility will provide quarterly updates that include annual kWh savings and spending by program during that quarter.

E. The implementation plan and compliance reporting described herein shall replace and supersede those in effect prior to the adoptions of these rules.

R14-2-_____. Cost Recovery

A. Program Costs
   1. Utilities shall recover their costs to plan, design, implement, and evaluate DSM programs. In order to qualify for cost recovery, each program must be approved prior to implementation.
   2. Program costs and performance incentives shall be recovered concurrently with the program implementation. The Affected Utility may recover the program costs and performance incentive associated with the Energy Efficiency Standard through base rates and/or an Adjustor Mechanism.
   3. Program costs may be either expensed or deferred and amortized over time at the Affected Utility's election, as established in an annual implementation plan filing.
      a. If amortized, the annual revenue requirements will be based on an interest rate equal to the Affected Utility's weighted average cost of capital and will be recovered over a period not to exceed five years. The annual revenue requirements will be recovered through an Adjustor Mechanism.
      b. If expensed, the total annual costs not recovered through base rates will be recovered through an Adjustor Mechanism pursuant to R14-2-_____.
   4. DSM funds may be used for market studies, consortium membership, labor costs for portfolio development, and other items for which the costs are difficult to allocate to individual DSM programs.

B. Unrecovered Fixed Costs
   1. The Commission will develop rate design and ratemaking methods that resolve regulatory disincentives or barriers to public utilities to achieve energy efficiency savings. The Commission will issue a final order removing regulatory disincentives or barriers to utilities to achieve energy efficiency savings by adopting appropriate rate design or ratemaking methods, by no later than the Affected Utility's next rate case subsequent to the approval of the Rules.
   2. To better align the energy efficiency interests of customers and the Affected Utility, each Affected Utility shall file a proposal for rate making methodologies to remove

regulatory disincentives. These methods may include one or more of the following: (1) modifying monthly customer charges to recover a higher portion of fixed costs from fixed charges and a lower portion from variable charges; (2) reflecting the projected reduction in kWh sales from programs in the billing determinants during a rate case; (3) using a future test year; (4) attrition adjustments; (5) reflecting unrecovered fixed costs through a proforma revenue adjustment in a rate case; or (6) decoupling mechanisms and other mechanisms designed to address this issue.

3. To help alleviate a portion of the rate making disincentives before they are addressed as described above, an initial recovery mechanism will be implemented for each year based upon the energy savings achieved by the Affected Utility multiplied by a per kWh incentive. This mechanism will equal the lifetime kWh energy savings times $0.0025 per kWh. The kWh from demand response programs will not be applicable to this mechanism.

C. Adjustor Mechanism

1. The Adjustor Mechanism, which will be adjusted annually as part of the implementation plan as established in R14-2-____, will be based on the projected relevant revenue requirements, such as program costs, performance incentive, and unrecovered fixed costs (if applicable), over the annual recovery period, subject to a true-up with interest in the subsequent period.

R14-2-_____. Performance Incentive

A. Performance incentive for Energy Efficiency Programs shall be tiered as a percent of net benefits, capped at a tiered percent of Program Costs. Performance incentives shall be recovered through the energy efficiency Adjustor Mechanism.

B. The performance incentive will be based on the achieved annual energy reduction relative to an annual guideline, which is established in the implementation plan. While the equivalent energy savings from DR programs will be counted towards the annual guideline, the net benefits from DR will not be included in the performance incentive.

C. The performance incentive schedule is as follows:

Achievement Relative to MWh Guideline	Incentive as a Percent of Net Benefits	Capped at a percent of Program Costs
Less than 85%	0%	0%
85% to 95%	6%	12%
96% to 105%	7%	14%
106% to 115%	8%	16%
116% to 125%	9%	18%
Greater than 125%	10%	20%

R14-2-_____. Cost-Effectiveness

A. The incremental benefits of the overall DSM portfolio shall exceed the incremental costs. The incremental benefits of the individual DSM programs shall also exceed the incremental costs.

B. Cost-effectiveness may be determined by a variety of methods. Each program should pass a cost-effectiveness test. However, each measure included in a program does not have to individually be determined to be cost effective. In addition to the cost-effectiveness test, the Affected Utility should consider the impact on rates, economic development, customer costs, and other economic impacts.

C. The avoided costs used in the cost-effectiveness tests should be consistent with the Affected Utility's integrated resource plan and be based on long-range projected fuel costs over the planning horizon rather than short term annual or quarterly fuel prices.

D. The expected energy and attributed to well-known or commercially available energy efficiency and load management devices or measures may be based on standard engineering calculations, ratings, simulation models or field measurement studies, periodically adjusted as appropriate for Arizona specific data, including building and household characteristics, and climate change conditions in pertinent region(s) within the state.

E. The standard cost-effectiveness analysis may not be appropriate for certain types of DSM programs.

1. Market Transformation Programs: Cost-effectiveness shall be measured by the success of a program in achieving results, such as market effects compared to its costs.
2. Educational Programs: Utilities shall attempt to estimate the energy and peak that result from educational efforts that raise awareness about energy use and opportunities for saving energy.
3. Research & Development and Pilot Programs: Individual research and development and pilot programs do not have to demonstrate cost-effectiveness.
4. Low-Income Programs: Measures included in low-income programs shall be generally deemed cost-effective.

R14-2-_____. Baseline Estimation

A. The baseline for determining the incremental costs and benefits of a DSM program shall be a reasonable estimate of the level of efficiency, costs, and energy consumption patterns that would have occurred in the absence of the DSM program.

B. For Demand Response programs, customer load profile information may be used to verify baseline energy consumption patterns and the peak Demand Savings resulting from demand response actions.

R14-2-_____. Fuel Neutrality

A. DSM shall be developed and implemented in a fuel-neutral manner. For those installations/applications that have multiple fuel choices, the baseline used in the cost effectiveness analysis shall utilize the same fuel source as the installation/application.

B. Electric utility program funds shall be used for electric measures. Natural gas utility program funds shall be used for natural gas measures. However, either natural gas utilities or electric utilities may fund thermal envelope improvements.

R14-2-_____. Monitoring, Evaluation, and Research

A. The Affected Utility shall monitor and evaluate all DSM programs to reliably ensure that they are cost-effective. Monitoring and evaluation should:
   1. Determine participation rates, energy savings, and demand reductions;
   2. Assess the utility's program implementation process;
   3. Provide information on whether to continue, modify, or terminate a program; and
   4. Determine the persistence and reliability of DSM.

B. Evaluation and research may also be conducted for program planning, product development, and program improvement. Evaluation and research includes market studies, market research, and other technical research for planning purposes.

R14-2-_____. Waiver from the Provisions of this Article

A. The Commission may waive compliance with any provision of this Article for good cause.

B. Any Affected Utility may petition the Commission to waive its compliance with any provision of this Article for good cause.

C. A petition filed pursuant to these rules shall have priority over other matters filed at the Commission.