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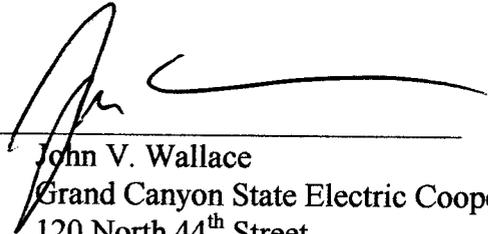
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IN THE MATTER OF THE NOTICE OF INQUIRY) DOCKET NO. E-00000J-08-0314
REGARDING UTILITY DISINCENTIVES AND) DOCKET NO. G-00000C-08-0314
POTENTIAL DECOUPLING FOR UTILITIES)
) **ELECTRIC COOPERATIVES'**
) **COMMENTS ON NOI REGARDING**
) **DECOUPLING**

On February 24, 2010, Chairman Mayes filed a Notice of Inquiry ("NOI") regarding utility disincentives and potential decoupling for utilities that asked interested parties to file information in these dockets in response to questions contained in the NOI. The following comments in response to the NOI are provided by Duncan Valley Electric Cooperative, Inc. ("Duncan"), Graham County Electric Cooperative, Inc. ("Graham"), Mohave Electric Cooperative, Inc. ("Mohave"), Navopache Electric Cooperative, Inc. ("Navopache"), Trico Electric Cooperative, Inc. ("Trico") and Sulphur Springs Valley Electric Cooperative, Inc. ("Sulphur") (collectively the "Cooperatives").¹

¹ The Cooperatives reserve the right, individually and collectively, to provide additional or different comments and positions on any of these issues in the future. The Cooperatives, individually and collectively, also reserve the right to modify the opinions expressed below as new information and input becomes available.

1 RESPECTFULLY SUBMITTED this 26th day of March, 2010.
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5 By: 

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11 Original and thirteen copies of the foregoing
12 filed this 26th day of March, 2010, with:

13 Docket Control
14 Arizona Corporation Commission
15 1200 West Washington Street
16 Phoenix, Arizona 85007
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ELECTRIC COOPERATIVE COMMENTS
ON NOTICE OF INQUIRY REGARDING UTILITY DISINCENTIVES AND
POTENTIAL DECOUPLING FOR UTILITIES
(DOCKET NOS. E-00000J-08-0314 & G-00000C-08-0314)

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Introduction

On February 24, 2010, Chairman Mayes filed a Notice of Inquiry (“NOI”) regarding utility disincentives and potential decoupling for utilities that asked interested parties to file information in these dockets in response to questions contained in the NOI.

The following comments in response to the NOI are provided by Duncan Valley Electric Cooperative, Inc. (“Duncan”); Graham County Electric Cooperative, Inc. (“Graham”); Graham County Utilities (“Graham Utilities”); Mohave Electric Cooperative, Inc. (“Mohave”); Navopache Electric Cooperative, Inc. (“Navopache”); Trico Electric Cooperative, Inc. (“Trico”); and Sulphur Springs Valley Electric Cooperative, Inc. (“Sulphur”) (collectively, “Cooperatives”).

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- 1. What financial disincentives are created by the implementation of energy efficiency measures?**

Cooperatives' Response: Revenue and margin erosion is a true concern and will occur to some degree with the implementation of EE programs. Cooperatives use margins to pay loan payments, invest in plant improvements, etc. Unlike the integrated IOU utilities, the benefits from EE savings in the form of lower energy costs and delayed capacity additions must be shared by the distribution cooperative's customers and generation and transmission cooperative or power supplier which are all separate entities.

Only a small portion of the fixed, distribution-related expenses are currently recovered from customers through the monthly fixed charge with a majority being collected through the per kWh charge. Consequently, for each kWh that a customer saves through EE, the distribution cooperative loses a portion of its margin and fixed cost recovery. In addition to the costs of EE programs discussed above, each cooperative would need to determine the amount of fixed cost including margin recovery that is necessary to remain whole financially.

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- 2. Should the Commission consider decoupling or decoupling like mechanism that would allow Companies to recover weather-adjusted fixed costs that are lost as a part of energy efficiency programs that drive conservation? If so, why?**

Cooperatives' Response: The Cooperatives support a straight fixed-variable rate structure or fixed cost recovery mechanism. A straight fixed-variable rate structure would allow the Cooperatives to increase fixed customer charges to the appropriate level demonstrated by a cost of service study and decrease per kWh rates. With the appropriate level of fixed customer charges, the Cooperatives earnings will stabilize and be less susceptible to large revenue swings due to weather and other variables.

The Cooperatives currently have not reviewed studies or have an opinion on weather-adjusted fixed cost recovery. The Cooperatives believe that as more factors are considered in the calculation of the lost fixed costs, the complexity and cost of such a calculation increases significantly. From an administrative and cost perspective, a simpler calculation that accounts for a major portion of the fixed costs may be preferential for the Cooperatives than a more complex formula that attempts to account for all variables such as weather.

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- 3. If you believe the Commission should adopt such a mechanism, how should it be structured? Should certain customer classifications be exempt?**

Cooperatives' Response: As mentioned above, the Cooperatives believe a simpler mechanism would be more appropriate under their circumstances. The Cooperatives would prefer a straight fixed-variable rate design to Decoupling Trackers, Lost Revenue Adjustment Clauses, Revenue Caps and Utility Retention of Cost Reductions because the majority of the Cooperative's distribution costs are fixed, earnings tend to be more stable and ease of calculation and explanation.

However, if a straight fixed-variable rate structure will not be adopted by the Commission, then the Cooperatives would propose that a fixed revenue by customer calculation (total revenue requirement per class minus fuel and purchased power expense per class divided by number of customers in each class for base time period). Allowed recovery is calculated by multiplying the fixed revenue by customer by the number of customers in a future time period.

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Since all customer classifications can potentially benefit from EE programs, all customer classifications should be subject to a fixed cost recovery mechanism.

- 4. How should weather-related changes in customer usage be treated? Should they be excluded and if so, how?**

Cooperatives' Response: The Cooperatives support a straight fixed-variable rate structure or if the Commission will not adopt such, a less complex fixed revenue per customer recovery mechanism. They currently have not reviewed studies or have an opinion on how weather-related changes in customer usage should be treated other than a more complex formula will be more expensive, controversial and time consuming.

- 5. What mechanism should be used for the recovery of unrecovered fixed costs associated with energy efficiency? What are your views of utilizing a deferral mechanism but requiring that accumulated costs be amortized of a several year period if deferrals are large?**

Cooperatives' Response: As stated above, the Cooperatives would prefer a straight fixed-variable rate design to Decoupling Trackers, Lost Revenue Adjustment Clauses, Revenue Caps and Utility Retention of Cost Reductions because the majority of the

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Cooperative's distribution costs are fixed, earnings tend to be more stable and ease of calculation and explanation. The Commission could accomplish this by allowing the Cooperatives to file an application for revenue neutral adjustments to rates that would allow the Cooperatives to increase fixed customer charges to the appropriate level demonstrated by a cost of service study and to decrease to the per kWh charges.

Since this application would be revenue neutral, the Cooperatives could file such an application without filing a rate case application.

If the Commission does not adopt a straight fixed-variable rate structure, then the Cooperatives would support a fixed revenue by customer calculation (total revenue requirement per class minus fuel and purchased power per class divided by number of customers in each class for base time period). Allowed recovery is calculated by multiplying the fixed revenue by customer by the number of customers in a future time period.

Concerning the use of a deferral account, the Cooperatives would only support this cost recovery method if immediate recovery is not an option. Recovery through a deferral account with an interest component is more expensive to member/customers and also more complex and less certain for utilities. In order to maintain their

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financial ratios such as equity ratio and Times Interest Earned Ratio (TIER), the Cooperatives would prefer a short deferral period such as 6 months. This deferral period is similar to fuel and purchased power pass through mechanisms currently adopted in many cooperative rate structures. Fixed cost recovery could be calculated for the previous 6 months and an adjustor could be implemented every April and October to keep the Cooperatives whole financially.

- a. If the Commission was to adopt decoupling and use a deferral mechanism, how should usage related to new customer additions be treated during the deferral period, i.e. should it be included or excluded?**

Cooperatives' Response: Usage related to new customer additions should be included in the calculation of the fixed cost recovery mechanism to reduce the overall collection of fixed costs.

- b. Should both programmatic and non-programmatic energy savings be included in the deferrals? If so, how should non-programmatic energy savings be measured and verified?**

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Cooperatives' Response: The programmatic and non-programmatic energy savings should be included in deferrals. Attempting to separate the two will be complex, time consuming and expensive.

6. What features can be adopted as a part of a decoupling proposal that would prevent the Company from over-earning, and address the concerns that decoupling mechanisms necessarily mean deviating from the matching principle?

Cooperatives' Response: When earnings are higher than authorized, there is no over-earning for cooperatives from the perspective that there is a third-party investor who benefits. The member-customers are also the owners of the cooperative. Since cooperatives are member-owned and non-profit entities, all margins that are earned are allocated to members in the form of capital credits and either refunded to members when retired or used to fund operations and construction thereby offsetting future rate increases. That being said, the straight fixed-variable rate design mitigates revenue fluctuations and ensures that the Cooperatives will only collect their authorized revenue requirement versus the current rate design that relies heavily on the kWh rate to collect fixed costs.

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- a. Should the Commission consider a “cap on earnings” as a part of its decoupling plan?*

Cooperatives’ Response: For the reasons stated above, this is not necessary for the Cooperatives. However, the Cooperatives do not have an objection to such a proposal as long as it is structured equitably to allow the Cooperatives to maintain their financial ratios and recover their fixed costs.

- b. Should a lower Return on Equity be adopted when considering rate cases for decoupled Companies to recognize that such companies may incur less risk than non-decoupled companies?*

Cooperatives’ Response: Return on Equity (“ROE”) is not used for setting the Cooperatives’ rates and therefore would not be applicable to the Cooperatives. Cooperatives rates are set on the basis of the financial ratios known as Times Interest Earned Ratio (“TIER”) and Debt Service Coverage Ratios (“DSC”). The Commission has historically set the Cooperatives’ rates on the basis of TIER and DSC because the Cooperatives’ lenders typically have requirements that certain TIER and DSC ratios be maintained. In addition, such adjustments are not necessary for the reasons stated above in response to question no. 6.

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c. Should the Commission require that Companies' decoupling mechanisms and deferrals be reviewed after some period of time, i.e. after three years of operation unless a company comes in for a rate case sooner?

Cooperatives' Response: The Cooperatives do not have an objection to a three year review period absent a rate filing as long as such a review is structured equitably to allow the Cooperatives to maintain their financial ratios and recover their fixed costs.

7. Please state whether the information provided in the Revenue Decoupling Data Report filed in compliance with Decision 70655 supports or argues against revenue decoupling in the case of natural gas utilities.

Cooperatives' Response: The Cooperatives do not have an opinion on whether the information provided in the Revenue Decoupling Data Report filed in compliance with Decision 70655 supports or argues against revenue decoupling in the case of natural gas utilities.

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8. What disincentives to customer conservation may be caused by virtue of the adoption of decoupling or decoupling like mechanisms?

Cooperatives' Response: If a straight fixed-variable rate design is adopted, then customer fixed charges will rise and kWh charges will decrease, thereby reducing but not eliminating the impact of conservation on a customer's bill. A fixed revenue per customer mechanism will have a similar impact but to a lesser extent. If necessary, the Cooperatives believe there is a balance that can be achieved using both mechanisms.

9. Are price signals skewed by decoupling and if so, how?

Cooperatives' Response: If a straight fixed-variable rate design is adopted, customer fixed charges will rise as they should be based on a cost of service study. This increase in fixed charges will send a more accurate price signal given that the majority of a distribution cooperative's costs are fixed in nature and not skewed price signal. A fixed revenue per customer mechanism will have a similar impact. Again, the Cooperatives believe there can be a balance in sending a price signal versus adequate fixed cost recovery that can be achieved using both mechanisms.

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10. What type of revenue decoupling mechanism is appropriate for Arizona or does it vary by company and with different facts?

- a. Revenue per Customer**
- b. Sales margin per Customer**
- c. Total margin revenue**
- d. Total class revenue**
- e. Usage per Customer**

Cooperatives' Response: If a straight fixed-variable rate design is adopted, customer fixed charges will rise as they should based on a cost of service study making the revenue decoupling mechanism less important. While all of the above could serve as the basis for a revenue decoupling mechanism, a fixed revenue per customer calculation is more relevant to a cooperative's bottom line and maintaining the TIER and DSC financial ratios discussed above absent a fixed-variable rate design. A fixed revenue per customer calculation will also require the lowest level of detail for the calculation.

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11. Should the Commission impose penalties for failure to meet specific designated DSM goals?

a. Should the opportunity to have periodic rate adjustments be tied to meeting specific energy efficiency requirements?

Cooperatives' Response: The Commission should not impose penalties for failure to meet specific designated DSM Goals for the simple fact that the adoption of DSM/EE measures is completely voluntary for customers and the Cooperatives have no control over the amount and type of DSM/EE programs that their customers will adopt. In addition, the Cooperatives have stated on numerous occasions that they do not believe that the 22% EE Rules Standard is realistic or achievable for various reasons.

Periodic rate adjustments can and should only be tied to a cooperative's TIER and DSC ratios to maintain the financial health and viability of the cooperative. Meeting specific EE requirements should only be a small part of a rate case analysis and the revenue requirement determination for the reasons stated above and given the Commission's purpose as stated in the Arizona Constitution.

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12. What means should be employed to track conservation associated with specific DSM programs for the purposes of evaluating the success of decoupling?

Cooperatives' Response: The EE Rules contain reporting requirements on the success, cost and benefits of specific DSM programs. The Cooperatives would propose to report the amount of fixed cost recovery associated with the approved fixed-variable rate design or decoupling mechanism. This fixed cost recovery would be identified within this report and could be compared with benefits realized and the amount of DSM/EE achieved.

13. What mechanisms are needed to assure data quality and accuracy of forecasting customers, usage and utility driven energy efficiency savings?

Cooperatives' Response: No forecasts are necessary for the adoption of a straight fixed-variable rate design. Any necessary standardization in forecasting methods and data quality associated with other decoupling mechanisms can be determined and developed as a part of the decoupling workshops. The EE Rules contain reporting requirements on the success, cost and benefits of specific DSM programs. From these reports and implementation plans, the Commission will be able to determine the quality of forecasting from year to year.

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14. Should decoupling mechanisms include a low income component?

Cooperatives' Response: The Cooperatives would consider low income rate components. However, unlike any other class, the EE Rules state that low income customers are already guaranteed a certain percentage of funds collected through the DSM/EE surcharge for low income EE programs.

a. Should utility energy-efficiency programs be structured to align costs and benefits among rate classifications?

Cooperatives' Response: EE programs need to be designed to maximize participation and the amount of EE. Limitations such as aligning costs and benefits among rate classifications could impair the Cooperatives' ability to accomplish this.

15. What additional issues should the Commission consider when addressing utility disincentives to implementing its Energy Efficiency requirements?

Cooperatives' Response: The Cooperatives believe that the impact of the implementation of the REST Distributed Generation ("DG") requirements have the same impact on the Cooperatives' collection of fixed cost as the EE programs. As customers install DG systems, the Cooperatives will be selling fewer kWh to such customers and

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thereby experience a decrease in their fixed cost recovery from these customers. Net metered customers with DG systems receive a full retail credit for any energy produced and avoid all fixed costs included in the kWh charge for the energy produced by a DG system. Consequently, the Commission should allow the fixed cost recovery mechanism to account for the decrease in the fixed cost recovery associated with the energy generated from customers' DG systems.

Another important factor besides decoupling, is to continue to explore DSM and retail rate structures that incent customers to use less energy during peak cost periods, while keeping the utility whole in terms of cost recovery. The Cooperatives intend to continue to explore these methods to reduce energy consumption at peak times.

Finally, the Cooperatives have a limited ability to meet the EE goals given that their customer base is approximately 95% residential. Small electric systems that are mainly residential may need different goals than the current EE standards. The Cooperatives' service territories also have a much lower density level (approximately 10 customers per mile of line) than other larger utilities. Programs that are cost effective in highly dense service territories with a higher percentage of commercial customers may not be cost effective in a small cooperative setting. The Cooperatives' lower density, predominately

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residential service territories could limit the types of programs that produce sufficient results. The Cooperatives believe that the Commission should consider addressing this issue in future workshops.