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2011 JUL 29 P 4: 12

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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-10-0458

Testimony of

Jeff Schlegel

Southwest Energy Efficiency Project (SWEEP)

In Support of the Proposed Settlement Agreement

July 29, 2011

Testimony in Support of the Proposed Settlement Agreement; Jeff Schlegel, SWEEP
Docket No. G-01551A-10-0458

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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), a public interest organization dedicated to advancing energy efficiency as a means of promoting customer benefits, economic prosperity, and environmental protection in Arizona and five other states in the southwest.

Q. Have you filed testimony previously in this proceeding?

A. Yes, I filed direct testimony on June 24, 2011.

Q. What is the purpose of your additional testimony?

A. In this testimony I support the Proposed Settlement Agreement ("Agreement") filed by Staff on July 15, 2011, to which SWEEP was a signatory, and I highlight several important provisions.

Specifically, I support Alternative B (full revenue decoupling) because it results in a lower base rate increase than Alternative A and effectively reduces the utility disincentive to energy efficiency (thereby resulting in more opportunities for customers to reduce their energy bills), which provides customer value in both ways. I also describe how Alternative B is consistent with the Commission-approved Policy Statement on Decoupling.[1] I oppose Alternative A (partial decoupling) and describe why Alternative A is not in the public interest because it results in a higher base rate increase than Alternative B, and almost certainly guarantees future rate increases, yet it does not adequately reduce the utility disincentive to energy efficiency (thereby resulting in fewer opportunities for customers to reduce their energy bills). In addition, I highlight SWEEP's support for the energy efficiency and low income customer provisions in the Agreement. I conclude that the Settlement Agreement is in the public interest, and I urge the Commission to approve the Agreement in its entirety with the selection of Alternative B and the rejection of Alternative A.

[1] Final ACC Policy Statement Regarding Utility Disincentives to Energy Efficiency and Decoupled Rate Structures, Docket Nos. E-00000J-08-0314 and G-00000C-08-0314, p. 30 (Dec. 29, 2010).

Decoupling to Reduce the Financial Disincentive to Natural Gas Utility Support of Energy Efficiency: SWEEP Supports Alternative B and Opposes Alternative A

Q. What is SWEEP's position on the two decoupling alternatives in the Settlement Agreement?

A. SWEEP supports Alternative B (full revenue decoupling) and opposes Alternative A (partial decoupling).

Q. Should Alternative B be implemented to reduce the financial disincentive to utility support of energy efficiency and encourage Southwest Gas to promote additional increases in energy efficiency – through Energy Efficiency (EE) and RET programs, and also from building energy codes, appliance efficiency standards, and state initiatives and legislation?

A. Yes. The financial interest of Southwest Gas should be better aligned with the interests of Southwest Gas customers by reducing financial disincentives to utility support of energy efficiency, thereby resulting in more energy savings and larger reductions in customer energy bills – and Alternative B is designed to achieve this result.

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. The Company addressed SWEEP's premise by proposing the EE and RET programs in its Application, and the Agreement sets for provisions for a Modified EE and RET Plan, both of which are necessary to achieve the Gas Energy Efficiency Standard.

Q. Do you support the full decoupling mechanism in Alternative B?

A. Yes. SWEEP supports the full decoupling mechanism in Alternative B. The decoupling mechanism consists of two parts: (1) customer bills will be adjusted each month (November through April) when actual weather during the billing cycle differs from the average weather used in the calculation of rates; and (2) rates will be adjusted annually to true-up the difference between authorized and experienced non-gas revenues.

The decoupling adjustments could be either up or down, either increases or decreases to customer bills. Analysis of prior experience with decoupling has shown the adjustments to be small, generally less than 3% and typically less than $1.50 per month for residential gas customers.[2] Alternative B also includes a low cap on upwards adjustments (see below).

Q. Is the full decoupling mechanism in Alternative B consistent with the Commission's Decoupling Policy Statement?

A. Yes. The Company's EE and RET Portfolio in concert with its proposed revenue per customer full decoupling mechanism in Alternative B is consistent with the Commission's Decoupling Policy Statement.[3] Alternative B meets the following policies set forth in the Policy Statement:

- "Utilities should pursue all cost-effective energy efficiency and demand side management resources, and should meet Arizona's Electric and Gas Efficiency Standards of at least… 6% gas savings by 2020."
- "Revenue decoupling may offer significant advantages over alternative mechanisms for addressing utility financial disincentives to energy efficiency."
- "While other decoupling models are appropriate in general, non-fuel revenue per customer decoupling may be well suited for Arizona."
- "Adoption of decoupling. . . should not occur as a pilot as this insufficiently supports demand-side management efforts, discourages beneficial changes in rate design, and is unlikely to encourage financial ratings improvements."
- "Full decoupling is preferable to partial decoupling."
- "Decoupling adjustments should occur at least on an annual basis, however, parties may propose more current adjustments as this may provide ratepayers with weather related relief following extreme events."
- "Broad participation in decoupling is preferred; however, the unique characteristics of each utility may merit different treatment of some customer classes."
- "Collars or caps on decoupling adjustments should be designed to encourage gradualism, and to minimize the short-term effects on customers."

Q. Do you support the cap on the decoupling adjustments as set forth in Alternative B (Section 3.29)?

A. Yes. SWEEP supports the cap in Alternative B of 5% of non-gas revenue on any upwards adjustments (increases in customer natural gas bills). Note that this cap is applied to *non*-gas revenue only, and not to the full gas bill, which results in a lower cap than the caps proposed and analyzed during the decoupling workshops and the cap proposed in SWEEP's direct testimony. SWEEP also agrees with Alternative B in that no cap should be applied to any downwards adjustments (i.e., credits on customer bills should not be limited by a cap).

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[2] Pamela Lesh, Rate Impacts and Key Design Elements of Gas and Electric Utility Decoupling: A Comprehensive Review, Electricity Journal (October 2009), p. 67.
[3] Final ACC Policy Statement Regarding Utility Disincentives to Energy Efficiency and Decoupled Rate Structures, Docket Nos. E-00000J-08-0314 and G-00000C-08-0314, p. 30 (Dec. 29, 2010).

Q. Are there reporting and other provisions in Alternative B to enable Commission review of the performance of the decoupling mechanism in the early years of its implementation?

A. Yes. Alternative B includes several provisions including quarterly reports on the performance on the decoupling mechanism, annual reports commencing in April 2013, annual review at Commission Open Meetings, and annual review by Staff with the assistance of an independent consultant – and Southwest Gas will be subject to an annual earnings test (Sections 3.21 through 3.28). Further, Southwest Gas is required to develop and submit a proposed customer outreach/education plan outlining how the Company will explain decoupling to customers (Section 3.31).

Q. Are there other provisions in Alternative B that result in customer value?

A. Yes. Alternative B has the lower revenue requirement of the two alternatives, and therefore results in a lower base rate increase out the gate than Alternative A. And importantly, Alternative B has a stay out provision and moratorium on general rate case applications of over five years (Section 3.30), a provision that applies for Alternative B only.

Q. What is SWEEP's position regarding Alternative A?

A. SWEEP opposes Alternative A (partial decoupling) because Alternative A is not in the public interest. Alternative A:

- Results in a higher base rate increase than Alternative B, and almost certainly guarantees future rate increases due to the lost fixed cost recovery mechanism that is a component of Alternative A only (and in contrast the adjustments under Alternative B could be up or down);
- Allows the recovery of *anticipated* lost-base revenues, thereby paying the Company for lost revenues in advance of actually experiencing such losses;
- Would create perverse incentives;
- Will likely result in contentious and protracted technical proceedings at the Commission (as has been the experience in lost revenue recovery mechanism proceedings in other states);
- Would not encourage the Company to support building energy codes, appliance efficiency standards, and state initiatives and legislation; and
- Does not adequately reduce the utility disincentive to energy efficiency (thereby resulting in fewer opportunities for customers to reduce their energy bills).

Energy Efficiency and Low Income Provisions

Q. What are the opportunities for effective and cost-effective energy efficiency programs and renewable energy programs to benefit Southwest Gas customers, both residential consumers and businesses?

A. 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, the cost-effective programs proposed in the Company's proposed Energy Efficiency (EE) and Renewable Energy Resource Technology (RET) portfolio ("EE and RET Portfolio") Implementation Plan, and the successful natural gas EE/DSM programs in other states.

Importantly, the EE and RET portfolio includes programs that provide opportunities for all customer segments to benefit from the EE and RET programs, including low income customers, residential consumers, small businesses, municipalities and schools, and large commercial and industrial customers.

Q. What are the energy efficiency provisions in the Agreement and why are they important for Southwest Gas customers?

A. The energy efficiency provisions in the Agreement require the Company to provide supplemental energy efficiency information to support a modified energy efficiency and renewable energy technology plan (modified EE & RET Plan). This modified EE & RET Plan will incrementally improve the Company's current customer offerings in terms of both budget and energy savings. The introduction of new, cost-effective energy efficiency opportunities will ensure that customers can achieve greater energy savings and larger reductions in their gas bills. The advent of these offerings will come at an opportune time, as they will help customers to lessen the impact of any bill increases as a result of new rates. Indeed, under the Agreement, Commission Staff has agreed to provide recommendations on as many energy efficiency measures in the modified EE & RET Plan as possible in a report filed prior to the Open Meeting when the Commission intends to vote on the Recommended Opinion and Order approving the Agreement.

While the energy savings proposed by the modified EE & RET Plan may not be sufficient to met the 2011 energy savings requirements established under A.A.C R14-2-2501 et seq. (the Gas Energy Efficiency Rule), the settlement requires the Company to file in a new docket within sixty days of the Agreement filing a new and revised EE & RET Implementation Plan pursuant to the Gas Energy Efficiency Rule. This new and revised Plan will be incremental to the modified EE & RET Plan measures that are being committed by the Company as part of the Agreement.

In the Agreement, the Company has also committed to achieving customer annual energy savings equivalent to the 2011 requirement of the gas energy savings goals within twelve months of Commission approval of the new and revised EE & RET Implementation Plan. In addition, Commission Staff has committed to make its best effort to review the Company's new and revised Plan and file recommendations for Commission approval on a schedule that contributes to the timely implementation of energy savings programs that are necessary to achieve the 2011 energy savings requirement. Finally in 2012 and beyond, the Company has agreed to comply with the cumulative annual energy savings requirements set forth in the Gas Energy Efficiency Rule; to achieve at least seventy-five percent of the cumulative annual energy savings through energy efficiency programs; to file its implementation plans on a schedule consistent with the requirement of the Rule; and to work with SWEEP and Commission Staff to avoid the need to file a request for a waiver during any plan year from 2011 through 2015.

Q. Are there provisions in the Agreement that benefit and protect low income customers?

A. Yes. Under the Agreement, the Company has agreed to enhance and increase funding of the Low Income Energy Conservation (LIEC) weatherization program. In addition, the Company will commit non-ratepayer funding to LIEC each year for the next five years, and this commitment shall result in a contribution equivalent to at least $1 million. The Company has also agreed to meet with Parties to the Docket within forty-five days of the effective date of any order approving the Agreement to develop a plan to enhance customer education and outreach for its LIEC program.

The impacts of new rates to consumers on low-income residential rate schedules will be mitigated through the following:

- The demand-side management adjustor rate for the low-income residential rate schedules will not be increased above the current rate;
- The Customer Owned Yard Line cost recovery mechanism will not apply to the low-income residential rate schedules; and
- The Low-Income Rate Assistance discount will be increased to thirty percent, from the current twenty percent for the first 150 therms in the winter months of November through April.

Conclusion

Q. In sum, what is your conclusion and recommendation for the Commission?

A. I conclude that the Settlement Agreement is in the public interest, and I urge the Commission to approve the Agreement in its entirety with the selection of Alternative B (full revenue decoupling) and the rejection of Alternative A.

Q. Does this conclude your testimony in support of the Proposed Settlement Agreement?

A. Yes.