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IN THE MATTER OF THE APPLICATION OF TUCSON ELECTRIC POWER COMPANY FOR APPROVAL OF ITS 2011-2012 ENERGY EFFICIENCY IMPLEMENTATION PLAN.	DOCKET NO. E-01933A-11-0055 **COMMENTS TO STAFF'S UPDATE ON TUCSON ELECTRIC POWER COMPANY'S ENERGY EFFICIENCY PLAN**

Tucson Electric Power Company ("TEP" or the "Company"), through undersigned counsel, hereby files its comments to Staff's February 28, 2012 Update ("Update") filed in this docket. The Update provides three new alternative proposals. Two of the Staff proposals are directed at Staff's initial Proposed Order filed in this docket on November 16, 2011 ("Proposed Order") and one proposal is directed to TEP's proposed Modified Implementation Plan filed in this docket on January 31, 2012 ("Modified Implementation Plan").

Overview

TEP believes all three Staff proposals are inadequate (for the reasons set forth below) to address the concerns raised by the Company. Accordingly, TEP respectfully requests that the Commission approve the Modified Implementation Plan, which also has the full support of RUCO and SWEEP, and the conceptual support of AECC.[1] In the alternative, TEP requests a waiver of the EE Rules as proposed in TEP's December 2, 2011 Exceptions, with programs and budget as shown in Appendix B of that filing. If neither the Modified Implementation Plan nor TEP's proposed waiver is acceptable, TEP requests an evidentiary hearing on it 2011-2012

[1] In its February 14, 2012 Comments, AECC supported the structure of the Modified Implementation Plan, finding numerous beneficial changes, but urged the Commission to further reduce the cost of the Modified Implementation Plan.

Implementation Plan.

TEP has always been a strong proponent of cost-effective energy efficiency as a means to keep customer rates down, to provide customers with the opportunity to manage their energy needs and to access low-cost energy resources. In fact, the Company was recently recognized as one of fifteen utilities in the United States that are industry leaders for energy efficiency and demand-side management (see Attachment A). Although TEP has proposed a waiver of the EE Rules as an alternative to Staff's Proposed Order, TEP has repeatedly indicated that it preferred the adoption of a robust Implementation Plan that would allow TEP to meet the EE Standard, ***provided that*** the confiscatory impacts of the Plan were suitably ameliorated through appropriate synchronization of compliance with the EE Rules with timely recovery of lost fixed cost revenue.

At the suggestion of this Commission, TEP engaged in a collaborative process with Staff and major stakeholders (RUCO, SWEEP and AECC) and developed a compromise solution to the issues raised in this docket, including the potential confiscatory nature of the initial Proposed Order. This compromise is reflected in the Modified Implementation Plan. Although this compromise is not what TEP would prefer, it is an acceptable resolution to the dilemma facing TEP until it can complete its next rate case.

TEP believes that its Modified Implementation Plan remains superior to Staff's proposals, particularly to Staff's preferred alternative. TEP's proposed DSMS is $0.003806/kWh for residential customers compared to Staff's higher proposed DSMS of $0.003877/kWh. TEP's proposed performance incentive is based on actual program benefits and results, not just the amount of spending as proposed by Staff. Moreover, TEP's proposed Modified Implementation Plan includes elements that ameliorate the confiscatory impact of EE Standard compliance in a manner that provides an acceptable bridge to TEP's next rate case. The Commission should approve the Modified Implementation Plan by adopting the proposed amendment language provided in TEP's January 1, 2012 filing in this docket.

Specific Comments to Staff Proposals

1. Staff Alternative Proposal 1 (Amendments 1 and 2).

This proposal would: (i) increase the DSMS and (ii) authorize TEP to *defer* unrecovered fixed costs associated with energy efficiency savings, using a yet-to-be-determined methodology. This proposal is flawed for several reasons:

a. It does not provide immediate relief for the confiscatory impact of EE Standard compliance

b. It does not provide certainty of any recovery of lost fixed cost revenues attributable to EE Standard compliance. Tellingly, the proposed deferral account amendment does not state that TEP will, indeed, recover the deferred lost fixed cost revenues.

c. It is unknown what type of deferral methodology might be acceptable to Staff, which adds another layer of uncertainty.

d. The alternative proposal only allows calculation of unrecovered fixed costs from the approval date of this order and does not provide for a solution associated to unrecovered fixed costs from January 1, 2012 through the date of this order.

e. It requires TEP to make yet another filing to seek approval of a deferral methodology and the proposal does not offer any deadline for Commission approval or effective date for such methodology. Moreover, if Staff does not agree with TEP's proposed methodology, this could further delay the approval and effective date.

Given these issues, TEP believes the proposed deferral authorization does not adequately address the confiscatory impact of complying with the EE Standard because it does not provide the Company with timely synchronization for recovery of lost fixed cost revenue which is necessary for compliance with the mandates set forth in the Commission's EE Rules.

TEP further notes that this alternative proposes a DSMS that is greater than the surcharge requested by TEP in Modified Implementation Plan. As noted in its January 31, 2012 filing, TEP believes that the Modified Implementation Plan provides it with a reasonable opportunity to meet the EE Standard for 2012 and possibly for 2013, and can do so at a lower cost to ratepayers than proposed by Staff.

For the foregoing reasons, TEP respectfully requests that the Commission reject Staff's Alternative Proposal 1 and approve the Modified Implementation Plan.

2. Staff Alternative Proposal 2 (Amendment 3).

This proposal would waive *only* the 2012 EE Standard (and does not address further waivers necessary until TEP has a lost fixed cost recovery mechanism in place) and sets spending at *no less than* 2010 levels. It also would set TEP's performance incentive on the methodology determined in the last rate case and provide no solution for the recovery of lost fixed cost revenue on a going forward basis.

Staff's new "waiver" proposal creates more problems than it solves and should be rejected. The proposal does not solve the dilemma facing TEP with respect to lost fixed cost revenue; rather it exacerbates it at the expense of improved energy efficiency programs. The proposal also creates the potential for an undue increase to the DSMS in future years as TEP tries to play catch-up to the EE Standard.

First, even if TEP were to return to 2010 spending levels, Staff's proposal provides no solution for the unrecovered fixed costs accumulated from January 2011 through March 2012. TEP increased its energy efficiency efforts in anticipation for the 2011 EE Standard – and in reliance on representations during the EE Rules and Decoupling Policy workshops and proceedings that it would receive lost fixed cost recovery. Staff's proposal also does not address additional unrecovered fixed costs that would continue to accumulate after the date of this order. Mandating 2010 energy efficiency spending levels will result in significant additional lost fixed cost revenues that TEP simply will be unable to recover and is confiscatory.

Second, Staff's recommendation of a waiver from the 2012 EE Standard without a waiver from the cumulative 2020 EE Standard forces TEP to make up for any shortfall sustained in 2012 in subsequent years due to the cumulative nature of the EE Standard. A shortfall in 2012 will require an extensive increase in 2013 program spending, which may require a large upward adjustment in the DSM surcharge. TEP would prefer more gradual surcharge adjustments in the future to avoid customer "rate shock."

Third, Staff's waiver proposal would create further uncertainly by leaving the door open for the Commission to potentially require (in the future) as much as a doubling of what is already an aggressive EE Standard to make up for the 2012 shortfall. This increased demand will result in higher costs to the Company and its customers.

TEP continues to believe that a waiver of the EE Standard should be the last resort. That is why TEP worked diligently with other stakeholders to develop a compromise implementation plan. However, if the Commission is going to waive the EE Rules for TEP, it should do so as proposed in TEP's Exceptions.

For the foregoing reasons, TEP respectfully requests that the Commission reject Staff's Alternative Proposal 2 and approve the Modified Implementation Plan.

Staff Alternative Proposal 3 (Amendment 4).

Staff has provided a number of comments related to TEP's Modified Implementation Plan. However, certain elements in Staff's third proposal undercut the purpose of Modified Implementation Plan, particularly the amelioration of the confiscatory impact of EE Standard compliance.

a. Removal of the Performance Incentive Floor at 80% of goal.

TEP strongly disagrees with Staff's proposal to remove the 80% floor built into the new performance incentive design and to *eliminate* any performance incentive if TEP does not achieve a minimum of 50% of the net benefits goal under the Modified Implementation Plan. This potential lack of *any* recovery does not fairly address the confiscatory impact of complying with the EE standard. Moreover, the uncertainty of recovery creates significant accounting issues for TEP, particularly with respect to TEP's ability to book the performance incentive as revenue.

The performance incentive in the Modified Implementation Plan has been designed through a collaborative process as a compromise solution to assure TEP some level of recovery of lost fixed-cost revenues. The target of $7,246,379 is a lower level of cost recovery than is necessary to make TEP made whole from complying with the EE Standard. TEP's initial 2011-2012 Implementation Plan requested cost recovery of $12,890,443 of Authorized Revenue Requirement True-up plus a performance incentive of $8,577,172 million. The Modified Implementation Plan reflects a compromise under which TEP is willing for forgo both of these in exchange for an interim performance incentive that is only 35% of the amount TEP requested.

The floor of $5,797,103 (80% of the $7,246,379 target performance incentive for 2012) is the minimum amount of cost recovery that TEP is willing to accept. If Staff's statement that *"...there is a risk that the Company could receive a performance incentive that is too high relative to the actual energy savings achieved"* is a concern, TEP could file a report in next DSMS true-up filing that identifies the amount of lost fixed cost revenues. Moreover, if Staff's primary concern is that *"for there to be lost fixed costs associated with energy efficiency, there have to be savings associated with energy efficiency, meanings sales the utility has foregone as a result of the Company's energy efficiency programs,"* TEP would be amenable to a floor equal to the lost fixed costs as calculated by energy efficiency savings multiplied by the non-fuel variable energy rate. However, TEP simply cannot accept a proposal – such as Staff's proposal -- under which TEP receives no performance incentive even though there are energy efficiency savings and lost fixed cost revenues.

b. <u>Calculation of Net Benefits.</u>

Staff's proposed Amendment No. 4 would require the use of Staff's inputs and methodologies to calculate the net benefits of TEP's EE programs used to set the performance incentive. However, TEP has calculated the anticipated $69 Million of net benefits utilizing TEP's own inputs and methodologies. Staff's proposal creates a significant risk due to the differences between the inputs and methodologies used by utilities and the inputs and methodologies used by Staff. Staff's inputs and methodologies could change without notice. That discrepancy and uncertainty undermines the purpose of the interim performance incentive.

If the Company is held to a requirement to calculate net benefits using Staff's *current* inputs and methodology for the societal benefit and societal cost calculations, TEP will likely need to modify the calculation of the 80%, 100% and 120% targets on a much lower basis than $69 Million to reach the $7,246,379 target. TEP anticipates that using Staff's inputs and methodologies to determine net-benefits may reduce its filed benefits by as much as 70 percent. As a result, this element of Staff's third proposal also precludes the Modified Implementation Plan from alleviating the confiscatory impact of compliance with the EE Rules.

For the foregoing reasons, TEP respectfully requests that the Commission reject Staff's Alternative Proposal 3 and approve the Modified Implementation Plan.

Conclusion

Although TEP cannot support Staff's three alternatives set forth in Staff's Update, the Company still desires to move forward with an energy efficiency plan that strives to meet the Commission's EE Rules. TEP supports the Commission's efforts to promote cost effective EE through programs that produce the desired results in a manner that will not harm the Companies' customers or the Company itself.

TEP believes the Modified Implementation Plan filed by the Company (which has the support of RUCO, SWEEP, and AECC, as discussed above) will result in cost effective EE programs and will provide an acceptable resolution to the confiscatory impact of implementing the EE Standard until TEP can complete its next rate case. The Company believes that this approach will strengthen the long-term viability of the EE Rules and are in the public interest. Therefore, TEP respectfully requests that the Commission adopt its Modified Implementation Plan.

However, if the Modified Implementation Plan is not approved, then TEP respectfully requests a waiver of the EE Rules (as set forth in its initial Exceptions) until a lost fixed cost recovery mechanism is adopted.

Finally, if the Commission declines to approve the Modified Implementation Plan or to grant the waiver request, TEP respectfully requests an evidentiary hearing on its 2011 - 2012 EE Plan.

RESPECTFULLY SUBMITTED this 7th.day of March 2012.

Tucson Electric Power Company,

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News release

For immediate release

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Smaller Utilities among Leaders in Sustainable Energy Efficiency & Demand Side Management

EE/DSM Programs earn Utilities Recognition by Target Rock Advisors Sustainability Rankings

Hauppauge, N.Y. (February 28, 2012) - Target Rock Advisors, LLC today released a list of fifteen U.S. utility companies that are industry leaders in energy efficiency and demand side management (DSM).

A disproportionately large number – eleven out of the fifteen – are small and mid capitalization utilities. These include (in alphabetical order) ALLETE, Inc. (NYSE: ALE), Alliant Energy Corporation (NYSE: LNT), Avista Corporation (NYSE: AVA), IDACORP, Inc. (NYSE: IDA), Northeast Utilities (NYSE: NU), Northwestern Corporation (NYSE: NWE), NV Energy, Inc. (NYSE: NVE), Pepco Holdings, Inc. (NYSE: POM), UIL Holdings Corporation (NYSE: UIL), UniSource Energy Corporation (NYSE: UNS) and Unitil Corporation (NYSE: UTL).

The four large capitalization companies on the list are (in alphabetical order): Edison International (NYSE: EIX), NextEra Energy, Inc. (NYSE: EIX), PG&E Corporation (NYSE: PCG) and Xcel Energy Inc. (NYSE: XEL).

Despite the challenges of running a small utility company profitably while also adhering to socially responsible practices, the small and medium size utilities on the Target Rock list have excelled in one of the most important dimensions of sustainable corporate behavior – energy efficiency, conservation and demand side management (collectively, "EE/DSM"). These utilities have provided consistent, exemplary results over the ten years of performance considered by Target Rock in assessing utility sustainability practices.

"One of the most immediate and effective strategies for improving a utility company's sustainability performance, including substantial reductions in fuels use, emissions and water use, is implementing EE/DSM programs," said Richard Rudden, chief executive of Target Rock. "EE/DSM has also been at the forefront of federal, state and local energy policy, as well as a linchpin of many corporate and governmental sustainability programs."

"We are pleased to recognize these small utility companies for their leadership in sustainable practices, specifically EE/DSM," said Rudden. Avista, IDACORP and Unitil were also included in the top echelons of Target Rock's flagship TRA49 rankings, which measures overall sustainability performance.

The TRA49 rankings, released on February 14, 2012, are based on overall sustainability scores assigned by Target Rock to 49 U.S. domiciled energy utilities. These rankings form the basis for Target Rock's family of utility stock indexes. All of the rankings and indexes, including a description of methodology, may be seen at http://www.targetrockadvisors.com.

About Target Rock

Target Rock is dedicated to the rigorous study and implementation of sustainability policies and practices within the utility and financial industries. The Company's mission is to provide data, information, analytical systems and deep sector-specific technical expertise that identifies areas for improved performance and helps utility companies achieve their sustainability objectives with favorable social and economic outcomes. Through its partners and associates, Target Rock has over 250 years of combined experience in sustainability and executive leadership, equities and fixed income analysis, financial management, statistics and econometrics, regulatory policy analysis and management consulting. More information on Target Rock can be found at http://www.targetrockadvisors.com.

Richard J. Rudden, Target Rock's chief executive, has served in analytical, consulting, management and executive positions within the utility, financial and energy industries for over 35 years. As a senior vice president for a multi-billion dollar global consulting and engineering firm, he lead the company's energy sector management and strategy consulting practice, chaired its climate change working group, and was a member of both the Advisory Board and Sustainability Steering Committee. He has published and spoken widely and has testified before state, federal, and provincial regulatory bodies, as well as in bankruptcy and civil court proceedings, on natural gas and electric economic, financial and policy issues. Previously he was the founding CEO of R.J. Rudden Associates, Inc., a strategy and economics consulting firm, and R.J. Rudden Financial, LLC, a FINRA-licensed broker-dealer providing services to the energy industry. Rudden was previously employed in management and executive positions at Con Edison, Stone & Webster (now Shaw) and Black & Veatch. He has also served on the Boards of Directors of the North American Energy Standards Board, a non-regulated retail energy marketer and the Cornell Cooperative Extension, where he is a member of the executive committee. He has also been involved in Cornell's Marine and related environmental programs.

Kyle P. Rudden, Target Rock co-founder and partner, has 15 years of experience in equity and fixed income analysis, with an emphasis on finance and capital markets. Most recently, he was president of R. J. Rudden Financial, LLC, a registered broker-dealer and energy industry advisory boutique. Before co-founding Rudden Financial, Kyle spent nearly a decade at J.P. Morgan Securities as vice president and head of the firm's U.S. Energy and Utilities Equity Research team covering electric and natural gas utilities, pipelines, independent power and new energy technology. While at J.P. Morgan, he was named in both Institutional Investor and the Wall Street Journal annual lists of top analysts and participated in a number of large domestic and international equity and equity derivative underwritings, including initial public offerings, public secondary offerings and private placements. Prior to J.P. Morgan, Kyle was a fixed income analyst at Fitch Ratings, also covering the U.S. electric and natural gas utility industries.

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