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BEFORE THE ARIZONA CORPORATION COMMISSION

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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

NOTICE OF FILING REBUTTAL TESTIMONY

Tucson Electric Power Company ("TEP" or "Company"), through undersigned counsel, hereby files the Rebuttal Testimony of David G. Hutchens and Denise A. Smith.

RESPECTFULLY SUBMITTED this 6th day of July 2012.

TUCSON ELECTRIC POWER COMPANY

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Arizona Corporation Commission
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BEFORE THE ARIZONA CORPORATION COMMISSION

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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

Rebuttal Testimony of

David G. Hutchens

on Behalf of

Tucson Electric Power Company

July 6, 2012

TABLE OF CONTENTS

I. INTRODUCTION.

Q. Please state your name and address.

A. My name is David G. Hutchens. My business address is 88 E. Broadway, Tucson, Arizona 85702.

Q. Have you reviewed the Direct Testimonies filed by the Arizona Corporation Commission's Utilities Division ("Staff"), the Residential Utility Consumer Office ("RUCO"), Southwest Energy Efficiency Project ("SWEEP") and Arizonans for Electric Choice and Competition ("AECC")?

A. Yes I have.

Q. Please provide an overview of your rebuttal testimony.

A. My Rebuttal Testimony addresses Staff's recommendations concerning TEP's proposed "bridge" energy efficiency implementation plan ("Updated Plan"). Because both RUCO and AECC have stated their support for the Updated Plan in their respective rebuttal testimonies, I am not commenting on those testimonies. Although SWEEP is also supportive of the Updated Plan as discussed in its rebuttal testimony, SWEEP sets forth a couple of recommendations that TEP does not agree with which I will briefly address.

TEP would like to move forward in efforts to meet the Energy Efficiency Rules ("EE Rules") and provide customers with programs and services that encourage energy savings. As a result of significant time and resources expended by many parties, the Company is proposing the Updated Plan as an interim solution that has been delicately balanced to resolve both practical and legal issues communicated by AECC, RUCO, SWEEP and Staff. The Updated Plan has support from AECC, RUCO, and SWEEP. These same parties understand that the interim plan has been designed to address a unique situation for TEP, created by the adoption of the EE Rules during TEP's rate freeze and rate case moratorium, and that the interim plan will not set precedent for future filings. It is simply a short "bridge" that allows TEP to move forward with EE for its customers until the conclusion of its pending rate case in 2013.[1]

With respect to Staff's recommendations, TEP continues to believe that the Updated Plan presents the most appropriate approach to address the unique interplay of TEP's rate case moratorium with the potentially confiscatory impact of the EE Rules. Staff's recommendations do not provide an acceptable resolution of the unique challenges facing TEP. Staff's proposes a larger EE Plan budget and a higher Demand Side Management Surcharge ("DSMS"). This increases costs to our customers and unnecessarily exacerbates the confiscatory impact of the EE Rules on TEP. Moreover, Staff's proposed deferral account does not provide sufficient protection to the Company against that confiscatory impact. Staff's other proposed modifications to the Updated Plan upset the delicately negotiated balance that made the Updated Plan operationally and economically palatable to TEP, as well as RUCO, AECC and SWEEP. Staff's two alternative proposals also are unacceptable. Alternative 1 results in a confiscatory impact on TEP. Alternative 2 is a full waiver of the EE Rules for a short window of time, which does not timely advance cost-effective EE programs and, which could put TEP in a difficult position to "catch up" to the EE Standard after the short waiver expires.

[1] Docket No. E-01933A-12-0291.

II. RESPONSE TO STAFF.

Q. Does the Company have any concerns with the programs and measures that Staff is recommending for approval.

A. No. The Company agrees with the programs and measures that Staff is recommending. Those programs and measures are the same programs and measures proposed in the Updated Plan.

Q. Does the Company support Staff's proposed budget increase from $18.5 million to $23 million?

A. No, the Company does not support an increase in the budget for the Updated Plan. The budget amount in TEP's Updated Plan is the result of extensive negotiations between the Company, AECC, RUCO, and SWEEP, and provides a solution to concerns raised by each of these stakeholders. By increasing the budget from $18.5 million to $23 million as recommended by Staff, the customer impact resulting from the increased budget will likely disrupt the delicately negotiated balance achieved by the Updated Plan that is supported by RUCO, AECC and SWEEP.

Q. What is TEP's position on Staff's recommendation that TEP not be granted a waiver from either the 2012 or 2013 EE Standard?

A. I believe Staff's position is unreasonable given these unique circumstances and ignores the reality of the situation given the timing. TEP still does not have an approved EE Implementation Plan for 2011 and it is unlikely to have any approved plan until 2012 is almost over. The Commission has stated that TEP's energy efficiency effort is to remain at "status quo" until this evidentiary process is concluded. It is clear that TEP cannot meet the EE Standard for 2012. Further, in order to jump from the status quo to full compliance by 2013 presents numerous operational and financial challenges that I do not believe would be in the best interest of the Company and its customers.

Q. Does the Company support the methodology for calculating the Performance Incentive ("PI") recommended by Staff?

A. No, the Company does not support Staff's recommendation to alter the Interim PI proposed in the Updated Plan. Again, that interim PI is a key element to the compromise developed to: (i) facilitate a more robust EE program, while addressing the issues raised in this docket, including the confiscatory impact of applying the EE Rules at this time (i.e. before TEP's rate case is concluded) and (ii) provide a bridge to the end of the now-pending TEP rate case, where the Commission can approve a more coordinated solution to the issues. TEP witness Denise Smith addresses the Interim PI and Staff's proposals concerning the PI in more detail in her rebuttal testimony.

Q. Staff's recommends that its proposed PI be trued up to actual performance. Would the Company agree to true-up its proposed PI?

A. Yes. TEP's proposal already contemplates that it would be trued-up to actual performance, not projected performance, subject to the floor-to-ceiling range set forth in the Updated Plan. The true-up will take place in the next reset of the DSMS, which will happen either as part of TEP's 2012 rate case or the approval of a subsequent EE Plan, whichever occurs first.

Q. Is the Company amenable to Staff's recommendations that the DSMS should be maintained on a per-kWh basis for all customer classes?

A. No, the Company does not support the recommendation to maintain the DSMS on a per-kWh basis for non-residential customers in this proceeding. The recommended change in the application of the DSMS to a percentage of bill rather than on a per-kWh basis for non-residential customers is the result of discussions with other parties to this application - yet another component of the delicately balanced negotiations for the Updated Plan.

Q. Staff states (at page 14 of Ms. McNeely-Kirwan's testimony) that the Updated Plan expresses concern about LFCR and implies that TEP is attempting to resolve the LFCR issue in this docket. Do you agree?

A. No, the Updated Plan does not address LFCR and the Company does not seek to resolve the issue in this docket. The Updated Plan provides only a compromise position that still provides net-benefits to all customers, provides programs for customers to reduce their electric bill, provides stability to the DSM market place, and provides a bridge mechanism to TEP's next rate case, where lost fixed cost recovery can be synchronized with TEP's future implementation plans.

Q. Assuming the LCFR issue is addressed in this docket, would the Company agree to Staff's recommendation to defer recovery of lost unrecovered fixed costs associated with energy efficiency savings?

A. No. The Company does not support deferred recovery of lost fixed costs or the quarterly reporting requirements recommended by Staff. Staff has not provided any specific guidance or methodology as to how TEP would actually recover those lost fixed costs and there is simply too much uncertainty about the ultimate recovery of those costs. Further, Staff's proposal does not address the following concerns TEP's previously expressed in its Comments filed in this docket on March 7, 2012:

> "*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; and*
>
> e. *It requires TEP to make yet another filing to seek approval of a deferral methodology and quarterly reporting to Commission Staff. 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."*

TEP still has these concerns and believes that the Updated Plan provides the appropriate bridge to the now-pending rate case where LFCR issues can be fully addressed on a going-forward basis.

Q. Would the Company agree to modify the Updated Plan with details provided in either Alternative #1 or Alternative #2 described in Staff's Direct Testimony?

A. No, the Company does not agree to modify the Updated Plan with either of the Alternatives proposed by Staff for the following reasons:

<u>Alternative #1</u>

This alternative does not include the Interim PI and recommends that the DSMS recovery be based on the per-kWh basis for all customers. Both of these elements are key components to the balance struck between the Company, RUCO, AECC, and SWEEP in the Updated Plan. For the reasons I discussed above, the Company cannot agree to their exclusion.

<u>Alternative #2</u>

Staffs "waiver" proposal creates more problems than it solves and should be rejected. The proposal does not solve the dilemma facing TEP and it creates the potential for an undue increase to the DSMS in future years as TEP tries to play "catch-up" to the EE

Standard. As stated in my Direct Testimony: *"TEP would prefer to have a more robust interim EE plan approved by the Commission in this docket rather than to receive a waiver that effectively keeps TEP at spending levels approved in 2010 before the EE Rules were adopted."*

III. RESPONSE TO SWEEP.

Q. Do you have any responses to SWEEP's Direct Testimony?

A. Yes. Generally, SWEEP appears to support the Updated Plan. SWEEP raises concerns about the waiver for 2013 and the bill impacts. I have addressed those issues above and will not repeat them here. SWEEP also suggests that the small commercial customers receive "at least the level of EE program funding collected from small customers." TEP will endeavor to do so provided it comports with the approved budget and results in cost-effective use of the funds. Finally, SWEEP requests that TEP be required to file a 2013 implementation plan. The Updated Plan has been carefully designed to cover the remainder of 2012 and 2013.[2] Moreover, in TEP's pending rate case that will be decided in 2013, the Company is proposing to replace annual EE implementation plan filings with a completely new approach to fund EE. If the Commission approves the Updated Plan, the filing of a 2013 implementation plan is simply unnecessary under the circumstances.

Q. Do you have any concluding remarks?

A. Yes. The financial aspects of the Updated Plan are designed to collect the proposed budget through the DSMS commencing on October 1, 2012. Additionally, as discussed in the direct testimony of Denise Smith, the Company has been awarded a U.S. Department of Energy grant. If TEP does not receive approval of the Updated Plan by October 1, 2012,

[2] *See* TEP's *Request to Accept Proposed Implementation Plan in Pending Energy Efficiency Docket as 2013 Implementation Plan Filing Under A.A.C. R14-2-2405* filed on May 11, 2012, which is incorporated herein by reference.

the Company could be at risk of losing the grant. Accordingly, I would urge the Commission to approve the Updated Plan as expeditiously as possible, but in no later than October 1, 2012 so our customers may once again be able to more fully benefit from the level of EE programs that they expect, as well as the additional funding that the grant will provide.

Q. Does this conclude your Rebuttal Testimony?

A. Yes it does.

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Rebuttal Testimony of

Denise A. Smith

on Behalf of

Tucson Electric Power Company

July 6, 2012

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I. INTRODUCTION.

Q. Please state your name and address.

A. My name is Denise A. Smith. My business address is 88 E. Broadway Blvd., Tucson, Arizona 85702.

Q. Are you the same Denise Smith that previously submitted Direct Testimony on behalf of Tucson Electric Power Company ("TEP" or "Company") in this Docket?

A. Yes.

Q. Have you reviewed the Direct Testimonies filed by the Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission"), the Residential Utility Consumer Office ("RUCO"), Southwest Energy Efficiency Project ("SWEEP") and Arizonans for Electric Choice and Competition ("AECC")?

A. Yes I have.

Q. Please summarize your Rebuttal Testimony.

A. I address concerns raised by Staff about the interim Performance Incentive ("PI") included in the Updated Plan. The Company believes that the Energy Efficiency ("EE") Rules expressly provide that the Commission can and should address and can modify PIs in connection with a proposed EE implementation plan. I also address concerns raised about the requested waiver regarding the filing of TEP's 2013 EE Implementation Plan.

II. PERFORMANCE INCENTIVE.

Q. Staff is concerned that the Updated Plan would change the PI methodology outside of a rate case. Do you share this concern?

A. No. Contrary to Staff's statement, Section R14-2-2411 of the EE Rules specifically provides for a modification of a PI in the annual Implementation Plan to encourage the utility to achieve the targets set by the Commission's approved EE standard:

> *"In the implementation plans required by R14-2-2405, an affected utility may propose for Commission review a performance incentive to assist in achieving the energy efficiency standard set forth in R14-2-2404. The Commission may also consider performance incentives in a general rate case."*

The EE Rules specifically state that it is appropriate for the Commission to review the PI when requested by an affected utility. Further, although the EE Rules acknowledge the PI "*may also*" be addressed in a rate case, the EE Rules do not require it nor provide that it is the only forum in which it can do so. It makes sense for the Commission to consider adjusting the PI in connection with a specific implementation plan especially when the Commission's EE Rules increase annually. In doing so, for example, the Commission can ensure that the PI fits the approved programs thereby assisting the utility in meeting the increasing EE standard. Further, the Commission may want to modify a PI that is not effective or that is incenting the wrong behavior. Staff's position, if accepted, would lead to the odd result that the Commission would have to wait for a rate case to change the PI. Cleary, that is contrary to the intent of A.A.C. R14-2-2411. This case is a good example of why a PI should be adjusted now because the Updated Plan's PI results in a more cost-effective approach that incents actual results and the Commission should not delay such modifications until a future rate case.

Q. Staff also has raised concerns about altering the methodology for calculation of the PI. Please address each concern.

A. Staff has listed four concerns (at page 8 of Ms. McNeely-Kirwan's direct testimony) related to altering the methodology for calculation of the PI.

Staff Concern 1: "The methodology significantly increases the Performance Incentive at the expense of rate payers"

TEP's Updated Plan included the development of an Interim PI structure as a bridge mechanism to the end of the TEP current rate case.[1] Although the Interim PI is higher, the total cost of the Updated Plan is significantly reduced. The Interim PI is based on the Company's performance in delivering cost-effective EE programs to rate payers and includes two separate calculations. This type of structure is beneficial to rate payers as both the tiered payment structure and payment based on net benefits create an atmosphere that encourages the Company to deliver the most cost-effective and highly beneficial programs and measures at the lowest possible cost.

Staff Concern 2: "With respect to Part II (the Other Performance Metrics), the payment associated with Net Benefits per customer dollar spent amounts to a double recovery"

Contrary to Staff's belief, these two performance metrics are entirely different and do not constitute double recovery. The percent of net benefit metric is an incentive for the utility to deliver EE programs that produce greater net-benefits. By comparison, the payment associated with net-benefits per customer dollar spent is a measurement of the efficiency of delivering cost-effective EE programs.

[1] *See* Docket No. E-01933A-12-0291.

Staff is also concerned that the 2/1 ratio of net-benefits to customer dollars spent is too modest. In response, the Company would reiterate that the 2012 Interim PI will not begin until October 2012 and there will be limited time remaining in 2012 for the Company to direct necessary spending to even reach the 2/1 ratio prior to the end of the year.

Staff Concern 3: "Payments associated with the other four performance metrics are not justified by direct, measurable, and verifiable kWh savings."

The whole point to the Part II (the Other Performance Metrics) PI is to incent additional items that are beneficial to the community in ways other than just direct energy savings. The Company, working in collaboration with SWEEP, identified additional performance metrics that would provide these additional benefits.

The Company has proposed a specified number of community weatherization workshops, senior outreach events, contractor training and a 5% increase in weatherized homes from the previous year. Because the 2012 Interim PI is not anticipated to receive approval for implementation until October 2012 and considering the Holiday schedule between the date of approval of this plan and the end of the program year, there will be limited time remaining in 2012 for the Company to schedule and complete all of the events listed. Therefore, the proposed performance metrics constitute a 'stretch' goal and should be approved.

Staff Concern 4: "It would be preferable to review the PI Mechanism in TEP's rate case, where it can be more fully considered in conjunction with related issues."

This issue has already been discussed above. The Company disagrees that it would be preferable to address this matter in the rate case. Further delay of this issue will continue to complicate this matter. Additionally, as previously stated, the Commission's own EE Rules allow for a more timely and cost-effective solution for the adjustment of the PI.

Q. Staff also raises concerns about the proposed floor for the PI. Why is the 80% floor important to the Company?

A. Staff is concerned that the Company could *"receive a performance incentive that is too high relative to the actual energy savings achieved."* It is important to understand that the Company's proposed Interim PI creates significant incentive for the Company to extend efforts to achieve the 'ceiling' level of $3.9 million rather than limiting ourselves to the guaranteed floor of $2.6 million. The floor is an important element of the negotiated bridge mechanism designed to address the unique circumstances facing TEP until a lost fixed cost recovery mechanism can be implemented following the rate case.

Q. Will the Updated Plan be subject to true-up?

A. Yes, the Updated Plan will be subject to true-up in the same manner as previous DSMS resets. This would include a true-up of the Interim PI based on actual performance. This will occur either as part of TEP's 2012 rate case or the approval of a subsequent EE Plan, whichever is first

III. <u>WAIVER OF FILING 2013 EE IMPLEMENTATION PLAN</u>.

Q. In light of SWEEP's recommendation that TEP file a 2013 Implementation Plan, please explain why the Company requested a waiver.

A. The Company requested a waiver of filing the 2013 EE Implementation Plan because of the delay in the timing of the approval of the 2011-2012 EE Implementation Plan and the aggressive cumulative standard set forth in the EE Rules. Any decision in this evidentiary hearing will likely not occur until September, 2012, and therefore the EE programs and measures that can be delivered from the date of that Order through December 2013 will remain identical to those filed on January 31, 2011. As a result, a 2013 EE Implementation Plan would be essentially identical to the Updated Plan as it relates to the already filed 2011-2012 EE Implementation Plan. In addition, TEP has filed in its 2012 rate case, a new proposal for DSM/EE programs that includes a three-year plan. It is anticipated that the rate case decision will occur in 2013 and will supersede any currently approved TEP EE Implementation Plan. Given these facts, the Company believes it is not necessary to file a separate 2013 EE Plan, and also believes that Staff will benefit from a reduction in the administrative burden associated with additional review of another Plan. Finally, the filing of yet another Implementation Plan in such a short period of time will provide even less certainty to customers and other stakeholders as to the status of TEP's EE/DSM program.

Q. Please provide comment to SWEEP's proposal that the Company prepare a filing proposing additional EE programs or program enhancements in a 2013 EE Implementation Plan.

A. The Company appreciates the efforts by SWEEP to accelerate the DSM/EE savings to meet the EE Rules however, the Company has proposed seven new programs and many program enhancements in its 2011-2012 EE Implementation Plan that have not yet been approved. If the Company receives a favorable decision on the Updated Plan in this proceeding, the Company will begin efforts to launch these new programs and enhancements. The necessary infrastructure to deliver both existing and new EE programs has been severely compromised due to the suspension of many of the existing EE programs. The Company will need to rebuild the infrastructure to ramp up new programs. It will take many months for the Company to regain the momentum in order to launch new programs. The Company therefore believes it would be difficult to launch additional programs in 2013. Moreover, the outcome of the new EE funding mechanism set forth in TEP's rate case must also be taken into consideration before TEP proposes new or enhanced programs.

Q. Does this conclude your testimony?

A. Yes it does.