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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 **STAFF'S CLOSING BRIEF**

I. INTRODUCTION

On January 23, 2011, Tucson Electric Power Company ("TEP" or "Company") filed its application for approval of its 2011-2012 Energy Efficiency Implementation Plan. Arizona Corporation Commission ("Commission") Utilities Division ("Staff") prepared a Staff Report and Proposed Order ("Staff Proposed Order") that was docketed on November 16, 2011. The Staff Proposed Order was considered by the Commission during the January 10 and 11, 2012 Open Meeting. The Commission did not act on the Staff Proposed Order, but instead directed the parties to further discuss the application among themselves to determine whether a compromise was possible. TEP and all other parties but Staff[1] subsequently agreed to a modified Energy Efficiency Implementation Plan ("TEP Modified Plan") that was docketed on February 1, 2012. In response, Staff prepared a Revised Staff Report that was docketed on February 29, 2012.

At an Open Meeting held March 16, 2012, the Commission considered the Revised Staff Report as well as the TEP Modified Plan. The Commission did not approve an implementation plan at that time, but referred the matter to the Hearing Division for evidentiary proceedings. TEP thereafter produced a further revised "Updated Plan" that was docketed on May 3, 2012. An

[1] In addition to TEP, the parties were the Residential Utility Consumer Office ("RUCO"), Freeport McMoran Copper & Gold, Inc. and Arizonans for Electric Choice and Competition ("AECC"), Western Resource Advocates ("WRA"), and the Southwest Energy Efficiency Project ("SWEEP"). EnerNOC, Inc. was granted intervention on June 20, 2012 and later indicated its agreement with the TEP plans. Collectively, these parties are referred to as "Joint Parties".

evidentiary hearing was held on July 11 and 12, 2012. A Recommended Opinion and Order ("ROO") was docketed by Administrative Law Judge Jane Rodda on August 21, 2012.

On September 27, 2012, a letter from Chairman Pierce was docketed directing the parties to this matter to submit closing and reply briefs discussing various issues relating to the above-captioned matter. Staff provides the following brief to address the legal questions posed by Chairman Pierce's letter.

II. DISCUSSION

A. Question 1: Does the Commission have legal authority to change the formula for calculating TEP's energy efficiency performance incentives outside a rate case?

The method of calculating the energy efficiency performance incentive has a direct impact on the rates charged to ratepayers to fund energy efficiency. As opposed to a simple reset of the adjustor mechanism, which will cause a fluctuation in the total costs recovered due to changes in program budgets from year to year between rate cases, the changes proposed by the Updated Plan would change the structure of the adjustor mechanism itself. In other words, the proposed changes would alter the structure of the rate.

Pursuant to the Arizona Constitution, article 15, section 3, the Commission has exclusive ratemaking authority. Per *Scates*, the Commission must utilize the fair value of a utility's assets to satisfy its constitutional obligations set out by article 15, section 14 and to determine just and reasonable rates. *Scates v. Ariz. Corp. Comm'n*, 118 Ariz. 531, 533-34, 578 P.2d 612, 614-15 (App. 1978). Because the changes to the Performance Incentive structure proposed by TEP are designed to impact earnings erosion caused by energy efficiency programs,[2] these changes will impact TEP's rate of return on fair value rate base. Consequently, the Commission should consider such changes within a rate proceeding, either by reopening TEP's last rate case or considering the proposed changes within TEP's pending rate case.

The Joint Parties suggest that changing the formula for calculating performance incentives outside of a rate case is permissible pursuant to Ariz. Admin. Code § R14-2-2411, which states:

. . .

[2] Evidentiary Hr'g Tr., vol. 2, 394:18 – 395:3, July 11, 2012.

> 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.

However, section R14-2-2411 does not expressly state that the Commission can approve performance incentive changes outside of a rate case. More importantly, the rule cannot trump the constitutional constraints established on the Commission's rate setting authority. To meet the canon of construction that rules and statutes must be read so as to be lawful, the rule must necessarily mean precisely what it says, that a performance incentive may be *proposed* outside of a rate case and that the Commission may consider it in a general rate case.

B. Question 2: If the answer to the first question is yes, must parties to a rate decision, which establishes a performance incentive formula, have notice within the pendency of the rate case that the Commission may change the performance incentive formula outside of either that rate case or a future one?

As Staff has answered no to Question 1, Staff has no additional response to Question 2.

C. Question 3: Decision No. 70628 adopts "the performance incentive for the DSM adjustor mechanism as recommended by Staff in its Direct Rate Design Testimony," which provides TEP the "opportunity to earn up to 10 percent of the measured net benefits from the eligible DSM programs, capped at 10 percent of the actual program spending." May the Commission adopt a new performance incentive that differs from the one adopted in Decision No. 70628? If so, must the Commission utilize either a new rate case or an A.R.S. § 40-252 process to reopen Decision No. 70628?

The Commission may, within the context of a rate case, adopt such adjustor mechanisms as the Commission determines are appropriate in light of the evidence presented. In the present circumstance, the Commission has established, and approved, a DSM adjustor mechanism, which includes a performance incentive, in Decision No. 70628 (December 1, 2008). The Commission can change the adjustor mechanism (including the performance incentive) in a rate proceeding.

Administratively, it is more efficient to institute rate changes in a new rate case rather than by amending a completed case. However, amending a prior rate case pursuant to A.R.S. § 40-252 so as to effect a rate change is within the authority of the Commission. Notwithstanding the Commission's authority in this regard, Staff cautions that amending a prior decision may undermine the concepts of regulatory certainty and finality.

In this matter, it is preferable to implement rate changes (such as changes to the performance incentive) within TEP's pending rate case in Docket No. E-01933A-12-0291. There are potential challenges presented by amending Decision No. 70628 at this point, although they are not insurmountable. First, parties to Decision No. 70628 would have to be noticed and provided with an opportunity to be heard. Should the Commission approve changes that those parties do not support, there could be a renewed opportunity to challenge an otherwise long-resolved Commission Decision. Additionally, because Decision No. 70628 adopted a settlement, any amendments to the decision could raise the potential for claims that the agreement has been materially changed.

Staff notes that TEP has provided notice of the proposed changes to the parties to Decision No. 70628. To date, no other originally settling party has expressed disagreement, aside from Staff. Nonetheless, Staff maintains that deferring consideration of the proposed performance incentive changes to the now-pending TEP rate case is a more straightforward solution.

D. Question 4: Paragraphs 20.12 and 20.13 of the settlement agreement approved by Decision No. 70628 prohibit the signatories to the settlement agreement from "tak[ing], support[ing], or propos[ing] any action that is inconsistent with" the settlement agreement, and require them to actively defend the settlement agreement before the Commission, courts or other regulatory agencies. Is advocating for a change in TEP's performance incentives consistent with the settling parties' obligations under Paragraphs 20.12 and 20.13? Should the A.R.S. § 40-252 process that is recommended in the ROO be broadened to relieve the parties from their obligations under Paragraphs 20.12 and 20.13?

The adoption of Staff's recommendation would not require the Commission to amend Decision No. 70628. Given the timing and complexity of the issues presented by this case, Staff believes that it would be better to evaluate changes to TEP's performance incentives in conjunction with TEP's pending rate case. Such a procedure would provide for a more comprehensive evaluation of TEP's performance incentives than is possible in the current proceeding.

Although Staff opposes amending Decision No. 70628, the Commission is not precluded from doing so. The settlement agreement approved by that Decision includes provisions (¶s 20.12 and 20.13) wherein the *parties* agreed not to undertake action inconsistent with the settlement agreement. These provisions, by their terms, do not apply to the Commission. Furthermore, it is doubtful that the Commission could be precluded from amending its orders in appropriate circumstances. *See* Ariz.

Const. art. XV, § 3 (providing that the Commission may amend or repeal its orders); A.R.S. § 40-252 (same).

In addition, other provisions in the settlement agreement would appear to permit parties to request amendments to Decision No. 70628. For example, while ¶ 10.1 establishes a moratorium (through January 1, 2013) for changes to TEP's *base rates*, ¶s 2.3 and 2.5 appear to *exclude* DSM adjustor revenues from base rates. Paragraphs 10.3, 11.1, and 20.11 also appear to provide (to varying degrees) vehicles by which parties can request changes to the Commission's order.

In summary, Staff opposes amending Decision No. 70628, as the period of time governed by that Decision has nearly concluded and a fresh rate case is available to enable the Commission to consider these matters in a comprehensive manner. On the other hand, the Commission is certainly not precluded from amending its prior orders. And even considering ¶s 20.12 and 20.13, Staff is reluctant to conclude that the parties are completely precluded (as a matter of law) from seeking amendments to the Commission's Decision.

E. Question 5: The rate design advocated by the parties is expected to have a bigger impact on TEP's small businesses than its other customers. Is the rate design inappropriately discriminatory?

Staff's rate design proposal did not have a substantially greater impact on the small business class of customers relative to other customer classes. The ROO adopts a rate design advocated by the Joint Parties which Staff opposes on the grounds that it disproportionately impacts the small business rate class relative to other customer classes. Staff maintains its belief that such rate design inappropriately requires the small business customer class to shoulder a disproportionately higher percentage burden than the other customer classes. This concern is heightened by the fact that the small business customer class already bears the highest proportionate burden of supporting energy efficiency programs, a fact that Mr. Higgins, testifying on behalf of the leading proponent of the Joint Parties' rate design, confirmed in testimony. Evidentiary Hr'g Tr., vol. 1, 201:19 – 202:10, July 11, 2012.

That there were no advocates for the small business customer class among the Joint Parties highlights the concern. As made clear from the testimony of the ratepayer advocates among the Joint

Parties, neither RUCO[3] nor AECC[4] represents small business customers. Although Staff participated in the discussions with the Joint Parties regarding the Updated Plan, Staff does not support the Updated Plan. Staff's recommendations reflect a balance of the interests of all customer classes as well as the utility's interests. In Staff's opinion, the rate design of the Joint Parties suffers from lack of input on the part of the rate class that suffers the most severe rate impact from the proposed changes under the Updated Plan.

In support of the Joint Parties' rate design proposal, Mr. Higgins acknowledged that the rate design proposed in the Updated Plan produces a greater impact on the small commercial rate class. *Id.* at 200:12-18. Moreover, Mr. Higgins further acknowledged that the small commercial rate class is already paying the most for Energy Efficiency under the equal percentage of bill methodology that the Updated Plan uses. *Id.* at 201:19-202:7.

Staff perceives an inherent unfairness occurring under the methodology proposed by the Updated Plan. The rate design of the Updated Plan will "shift per-kWh costs for energy efficiency from large [n]on-residential customers to smaller non-residential customers, a shift which Staff views as inequitable." Evidentiary Hr'g, Ex. S-1, Direct Test. of Julie McNeely-Kirwan, 12:11-13. In conjunction with Mr. Higgins' acknowledgement that energy efficiency measures benefit the entire grid by way of deferring new generation construction and avoiding supplemental power purchases, which all customers pay for through TEP's PPFAC on a per-kWh basis,[5] Staff believes that there is little basis to institute a rate design change with such a disproportionate impact based on the record developed in this matter.

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[3] Evidentiary Hr'g Tr., vol. 1, 225:6-17, July 11, 2012.
[4] *Id.* at 186:13-15.
[5] July 11, 2012 Hearing Tr. at 193:21 – 196:13.

III. CONCLUSION

For all of the reasons stated in closing during the evidentiary hearing and those explained further in this brief, Staff requests that the Commission adopt Staff's Recommendation. In the event that Staff's Recommendation is unacceptable, Staff recommends the adoption of either of Staff's Alternatives 1 or 2 as fair and reasonable resolutions to the matter at hand.

RESPECTFULLY SUBMITTED this 12th day of October, 2012.

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