



0000152213

Memorandum
From the office of
Commissioner Gary Pierce
Arizona Corporation Commission
1200 W. WASHINGTON
PHOENIX, ARIZONA
(602) 542-3933

ORIGINAL

Arizona Corporation Commission
DOCKETED

APR 02 2014



TO: Docket Control
DATE: April 1, 2014
FROM: Commissioner Gary Pierce
SUBJECT: Energy Efficiency & Integrated Resource Planning
Docket # E-00000XX-13-0214

The agenda and presentations from the March 31, 2014 Energy Efficiency & Integrated Resource Planning workshop have been docketed. If interested in participating or presenting at the April 17th EE & IRP workshop please contact my office.

RECEIVED
2014 APR - 2 A 9:07
AZ CORP COMMISSION
DOCKET CONTROL

**NOTICE
SPECIAL OPEN MEETING
OF THE ARIZONA CORPORATION COMMISSION**

**Energy Efficiency & Integrated Resource Planning
RE-00000C-09-0427 & E-00000XX-13-0214**

DATE: Monday, March 31, 2014

START TIME: 9:00 a.m.

**Arizona Corporation Commission
Hearing Room One
1200 W. Washington Street
Phoenix, Arizona 85007**

This shall serve as notice of a special open meeting of the Arizona Corporation Commission at the above location for consideration, discussion, and possible vote of the items on the following agenda and other matters related thereto. Please be advised that the Commissioners may use this open meeting to ask questions about the matters on the agenda; therefore, the parties to the matters to be discussed or their legal representatives are requested, though not required, to attend. The Commissioners may move to executive session, which will not be open to the public, for the purpose of legal advice pursuant to A.R.S. §§ 38-431.03.A.2, 3 and/or 4 on the matters noticed herein. The Commissioners may also move to executive session, which will not be open to the public, for other purposes specified in A.R.S. §§ 38-431.03, including discussions, consultations or considerations of Commission personnel and salary matters, on matters noticed herein.

The Arizona Corporation Commission does not discriminate on the basis of disability in admission to its public meetings. Persons with a disability may request a reasonable accommodation, such as a sign language interpreter, as well as request this document in an alternative format, by contacting Shaylin A. Bernal, phone number (602) 542-3931, E-mail sabernal@azcc.gov. Requests should be made as early as possible to allow time to arrange the accommodations.

**Jodi Jerich
Executive Director**

Workshop #2 Cost Recovery – March 31, 2014

Includes discussion of:

- 1.) EE cost recovery mechanisms (including base rate recovery of expenses, surcharge based on anticipated spending, surcharge to recover deferred costs, and treating EE as a resource).
- 2.) Methods for utility recovery of authorized non-EE fixed costs (including revenue decoupling, straight fixed variable rates, lost revenue adjustment mechanism, and cost shifting).
- 3.) Utility incentives (including performance incentives and rate of return incentives).

NO VOTES ON SUBSTANTIVE MATTERS WILL BE TAKEN AT THIS MEETING.

Energy Efficiency (EE) Cost Recovery



Jeff Schlegel & Ellen Zuckerman
Southwest Energy Efficiency Project (SWEEP)

March 31, 2014

Outline

- EE and the Public Interest
- Cost Recovery & Incentives for Supply- and Customer-Side Investments
 - Two Main Ways to Pay for EE
 - Objectives and Types of EE Performance Incentives
- Recovery of Authorized Fixed Costs
- Designing Programs to Maximize Benefits & Reach

CUSTOMERS

Lowers Bills Now & in the Future

Improves Comfort, Health & Safety

Gives More Control & Understanding

ECONOMY

Creates Local Jobs

Gives Businesses a Competitive Edge

Redirects Bill Savings to the Local Economy

EE: Good for Customers, the Economy, the Utility System, & the Environment

UTILITY SYSTEM

Grid Made Less Vulnerable To:

Terrorist Attacks, Natural Disasters,
Economic Changes, Unexpected
Weather, & Central Power Plant Outage

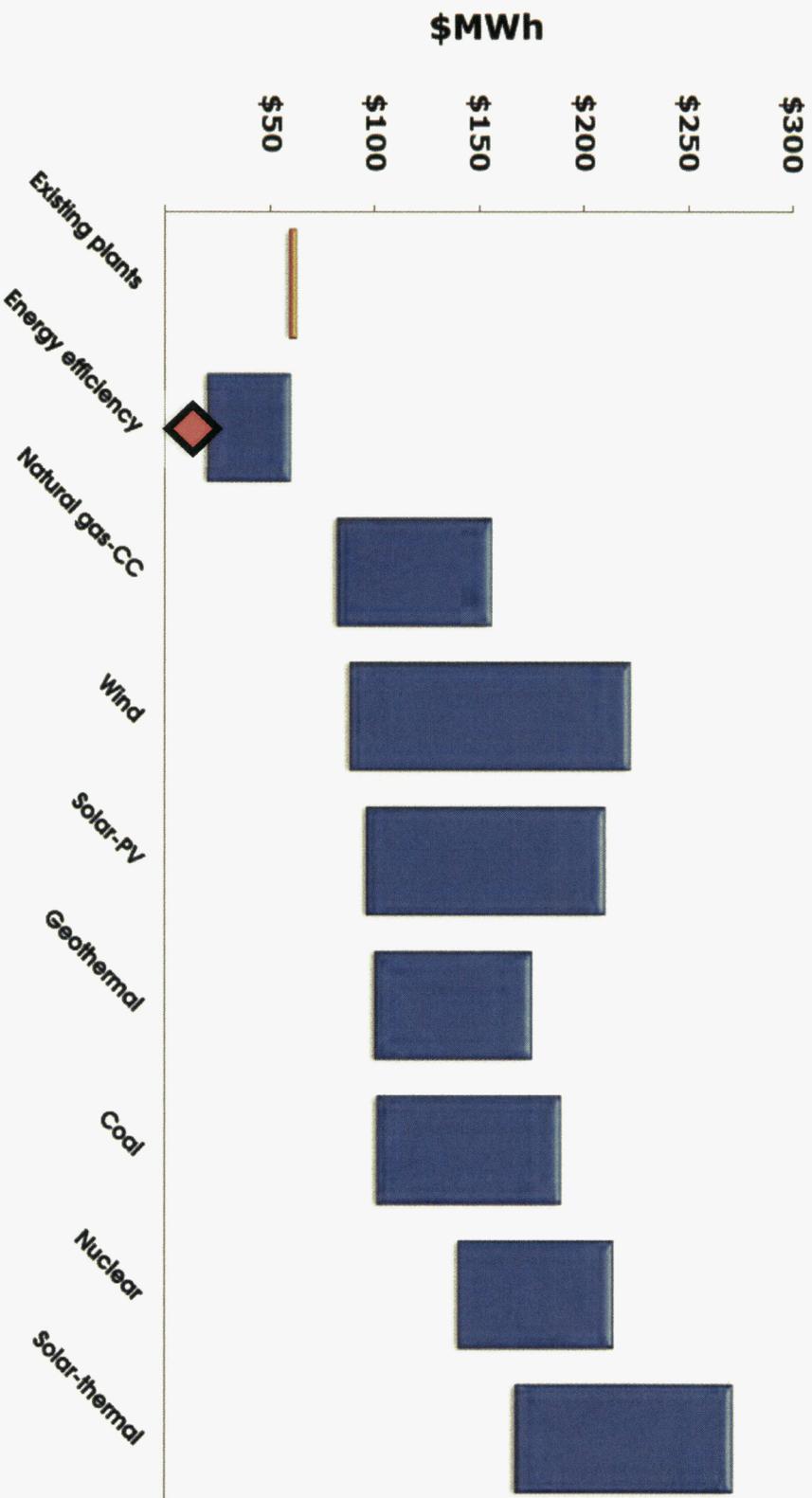
ENVIRONMENT

Reduces Water Use

Reduces Air Pollution

EE: The Least Expensive Resource

APS New Resource Costs (\$/MWh, 2015)



◆ ACTUAL 2012 COST OF EE

Source: Arizona Public Service Company, 2011.

Utility Options for Meeting Customer Needs

Supply-Side Investments

1. Opportunity to **recover costs** of supply-side investments
2. Opportunity to **earn a return** for making supply-side investments

Customer-Side EE Investments

1. Opportunity to **recover costs** of EE programs
2. Opportunity to **earn a performance incentive** for delivering EE



Two Main Ways to Pay for EE

1. Treat EE as an expense
2. Treat EE like a capital investment (amortization)

EE as an Expense

- Pay costs as they are incurred
- Can include **performance incentive**
- **Less expensive** for ratepayers
- **Higher** near-term rate impact, but lower total cost to ratepayers
- **Does not create** a regulatory asset
- Most common approach

EE as a Capital Investment

- Pay incurred costs **over time** (like a mortgage)
- Includes authorized **rate of return**
- **More expensive** for ratepayers
- **Lower** near-term rate impact, but higher total cost to ratepayers
- **Creates** a regulatory asset
- Uncommon

EE Performance Incentives Should:

- ❑ Encourage cost-effective EE resources
- ❑ Encourage cost-efficient EE program delivery
- ❑ Avoid perverse incentives
- ❑ Be based on clearly-defined goals and activities that are monitored, quantified, and verified.
- ❑ Be available only for activities for which the utility plays a distinct and clear role in bringing about the outcome
- ❑ Be kept as low as possible while balancing and meeting the above objectives

Types of EE Performance Incentives

- Shared benefits or net benefits
 - Allows utility to earn a portion of the monetary benefits the EE program or portfolio delivers
 - Example: Utility allowed to receive X% of delivered net benefits
- Performance targets
 - Allows utility to earn an incentive based on achieving a goal or target
 - Example: Utility allowed to receive incentive for meeting a target of X% energy savings as a percent of retail sales
- Rate of Return
 - Allows utility to earn a rate of return based on EE spending or savings
 - Example: Utility can receive X% return-on-equity for applicable, approved DSM costs

Recovery of Authorized Fixed Costs

- Fixed costs are utility supply-side investments (e.g. power plants, transmission and distribution lines) that have been authorized for recovery by the Commission
- ***Fixed costs are Commission-authorized costs – they exist regardless of EE or how much EE is implemented***
- ***Fixed costs are paid by customers***
- Fixed costs are recovered in two ways:
 - Volumetric charges (\$ per kWh sold)
 - Fixed charges (\$ per month)

EE Does Not Cause Fixed Costs to Increase – They are *Not* a Cost of EE

- Fixed costs are Commission-authorized costs
- EE does not increase the amount of fixed costs to be recovered from customers – the Commission decides how much in fixed costs the customers pay
- EE reduces the volume of energy sales over which fixed costs are recovered, thereby increasing the portion of costs recovered in each remaining unit of energy sales
- Fixed costs are not recovered when:
 - Actual sales < projected sales in the test year
- BUT the *total amount* customers pay remains the same

Utility Options for Meeting Customer Needs

Supply-Side Investments

- ❑ Much higher costs for future resources
- ❑ Without EE, all customers pay much higher costs, including higher fixed costs
- ❑ Rates and bills increase for customers

Customer-Side EE Investments

- ❑ Defer or avoid supply investments to keep costs lower (don't allow fixed costs to increase so much in the first place)
- ❑ Bills are lower but rates increase slightly to recover fixed costs
- ❑ Longer term, bills and rates are lower

Volumetric Rates Send a Price Signal

- Volumetric rates are crucial for sending a strong price signal, to maximize customer participation in EE
- Need strong price signal to encourage many customers to take action, thereby achieving even more cost-effective savings, and avoiding the need to build or buy more expensive resources
- Need to motivate customers to take action
- An increase in customer fixed charges will dampen the price signal and be a disincentive to action

Designing EE Programs to Maximize Customer Benefits & Reach

- Develop and implement programs that are accessible, reach all customer segments, & target hard-to-reach segments
 - Example: APS 2012 EE programs: ~ 400,000 customers participated
- Spend EE program dollars on the customers from whom money was collected
 - Example: EE program costs recovered by residential sector are spent on residential customers

Thank you!

□ Jeff Schlegel

schlegelj@aol.com

520-797-4392

□ Ellen Zuckerman

ezuckerman@swenergy.org

602-466-1513

**Energy Efficiency
Cost Recovery**

Arizona Public Service

ACC Workshop

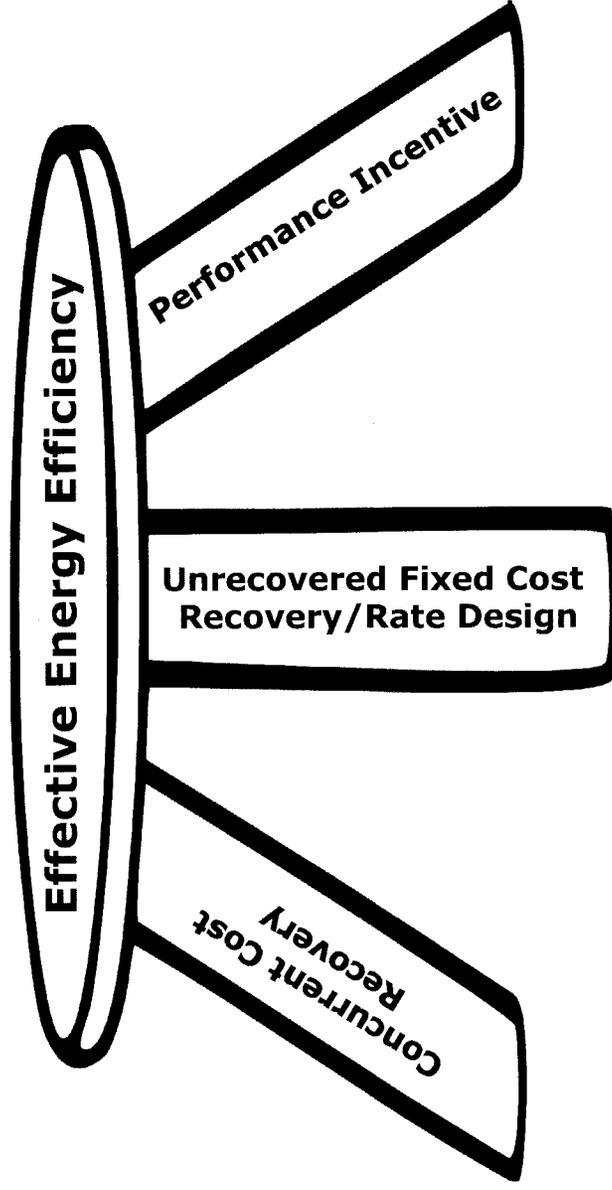
Energy Efficiency Cost Recovery

March 31, 2014



Energy Efficiency and Utility Business Model

- EE is different than traditional resources, so it requires a different cost recovery model
- What is important?



Fixed Cost Recovery

CURRENT

Lost Fixed Cost Recovery
Adjustment Mechanism

- Approved in APS's 2011 rate case
- Recovers a portion of transmission and distribution lost fixed costs

FUTURE

Rate Design Can Be
Updated to Improve Fixed
Cost Recovery

- Accurate price signals
- Address potential cost shift
- Modernize rates

Thank You

APS Performance Incentive Structure

- Based on a % of net benefits, capped at a maximum amount per kWh saved

% of Goal Achieved	% of EE Net Benefits	Cap
<85%	0%	Performance
85% to 95%	6%	Incentive capped at no more than
96% to 105%	7%	\$0.0125 per kWh.
>105%	8%	

- Incentive based on actual performance and only collected if program generates net benefits for customers
 - Maximize energy savings while minimizing costs
 - Not tied to program spending



Utility Fixed Cost Recovery Full Revenue Decoupling

March 31, 2014



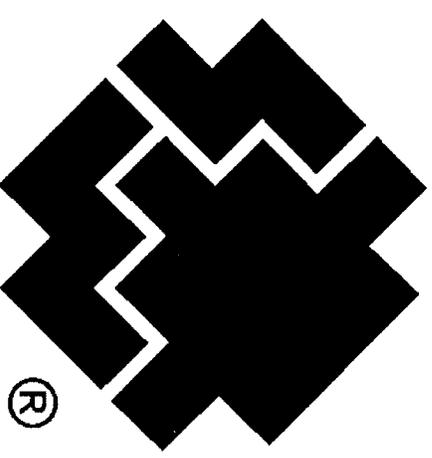
SOUTHWEST ENERGY SERVICES



Delivering
SOLUTIONS
FOR
ENERGY SERVICE
REGULATORY

Decoupling History

- Approved as part of 2010 Rate Case
 - Effective January 1, 2012
- Two components of decoupling mechanism
 - Annual Margin per Customer True-up
 - Monthly Weather Adjustor
- Reporting Requirements
 - Quarterly
 - Annually



Decoupling History

Annual Reporting

- First annual report for year ended 12/31/12 included a refund to customers of \$1.9M
 - Commission Staff concluded:
 - “the revenue decoupling mechanism has accomplished its objectives, including both enhanced revenue stability for the Company and bill stabilization for consumers, as well as removal of disincentives to energy efficiency.”*
 - Unanimously approved by Commission in December 2013
 - Approved as part of ACC Consent Agenda

Benefits of Full Decoupling

- **Improved credit rating – resulting in lower debt costs**
 - 2004 Rate Case decision initiated a subsequent Moody's rating downgrade from Baa2 to Baa3

“...due to the absence of mechanisms which mitigate the impact of weather, . . . rate design that is solely based on gas throughput . . . approval of a decoupling mechanism is key to the improvement in Arizona’s overall regulatory environment...”
Standard & Poor’s 2009

Benefits of Full Decoupling

➤ Decoupling is now a credit rating positive factor

“In our opinion, regulation in Arizona (historically considered one of the less credit-supportive jurisdictions) has improved substantially, as the ACC approved a decoupled rate design in Southwest Gas’s latest rate case; this mechanism can significantly mitigate cash flow volatility.” Standard & Poor’s 2013

“The company now has some form of de-coupling and gas purchase adjustment mechanism in all three of its service territories, which will contribute towards sustained financial performances over the next several years.” Moody’s 2014

Benefits of Full Decoupling

- **Improved credit rating – resulting in lower debt costs**
 - Provides for greater stability of earnings and cash flow that positively contributed to improved credit ratings
 - Resulting in lower long term cost of debt for our customers

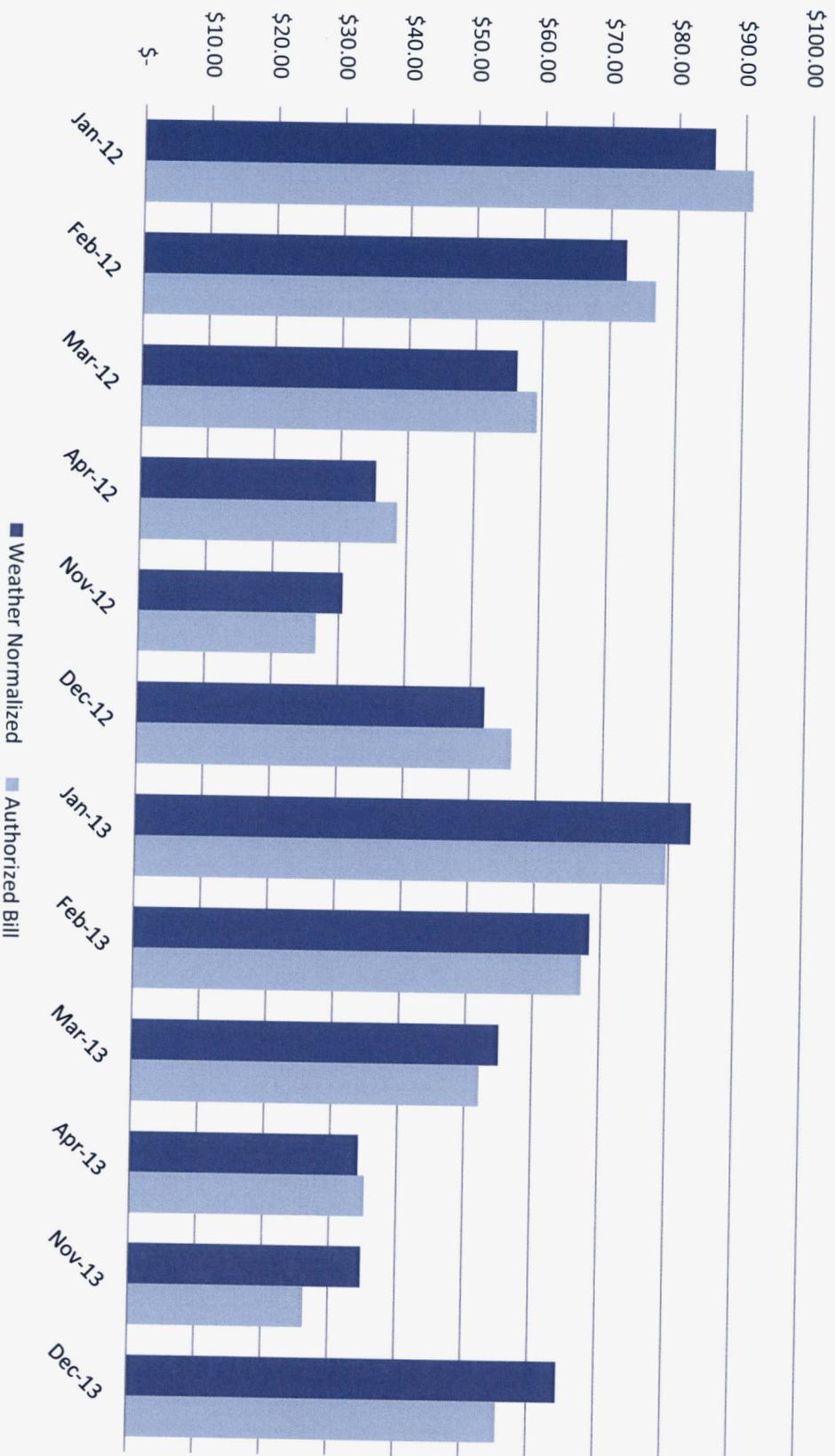
	Standard & Poor's	Moody's	Fitch
2011	BBB+	Baa2	BBB+
Today	A-	A3	A

Benefits of Full Decoupling

- Improved credit rating – resulting in lower debt costs
- **Customer Protections**
 - Protects customers from high winter bills
 - Ensures customers pay no more than Commission authorized costs
 - Limiting utility profit from increased sales
 - Enhancing utility focus on cost control
 - Allows both upward and downward rate adjustments
 - Decreases frequency of general rate cases

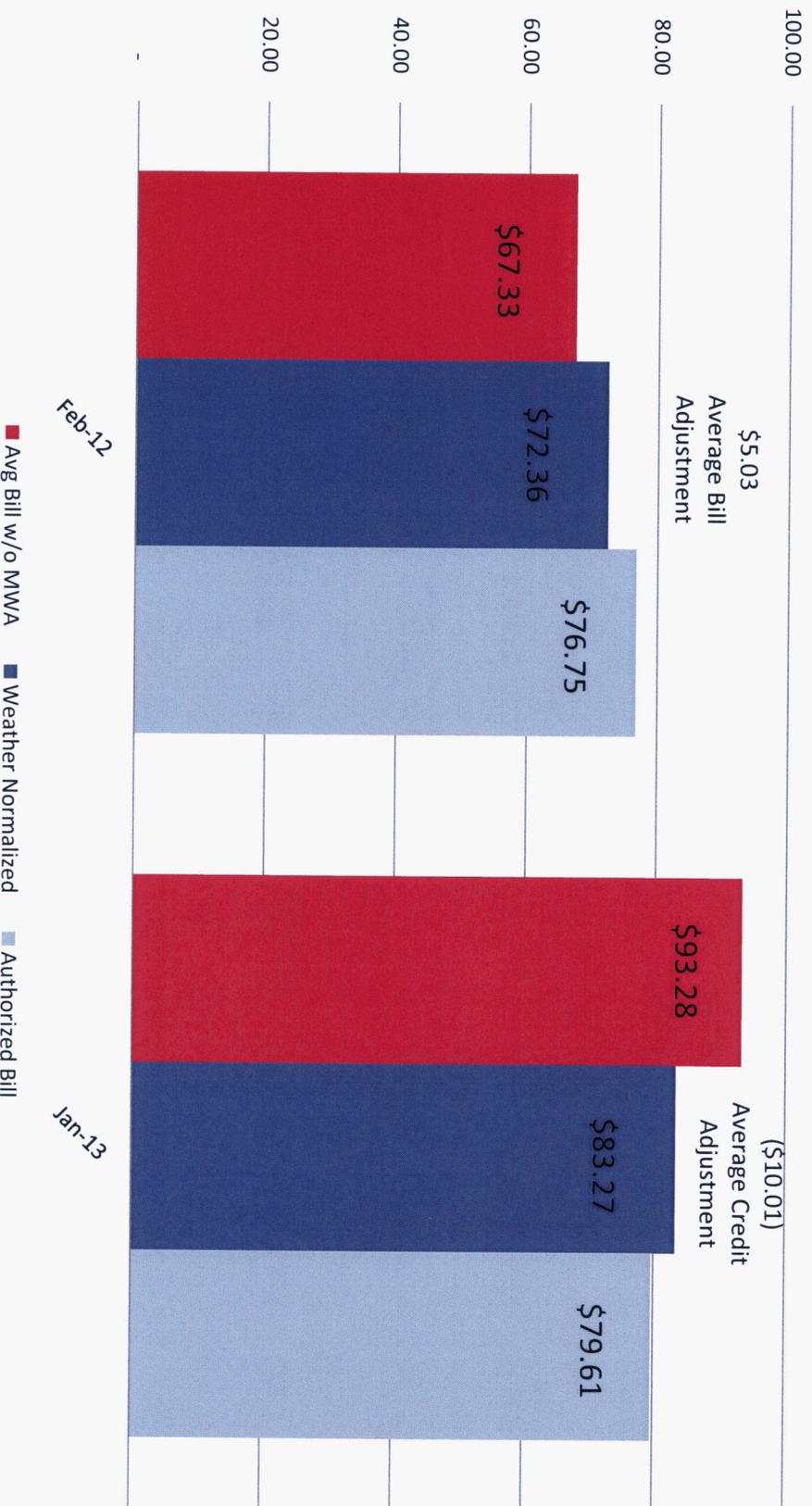
Benefits of Full Decoupling

Average Residential Bills



Benefits of Full Decoupling

Residential Weather Adjustments

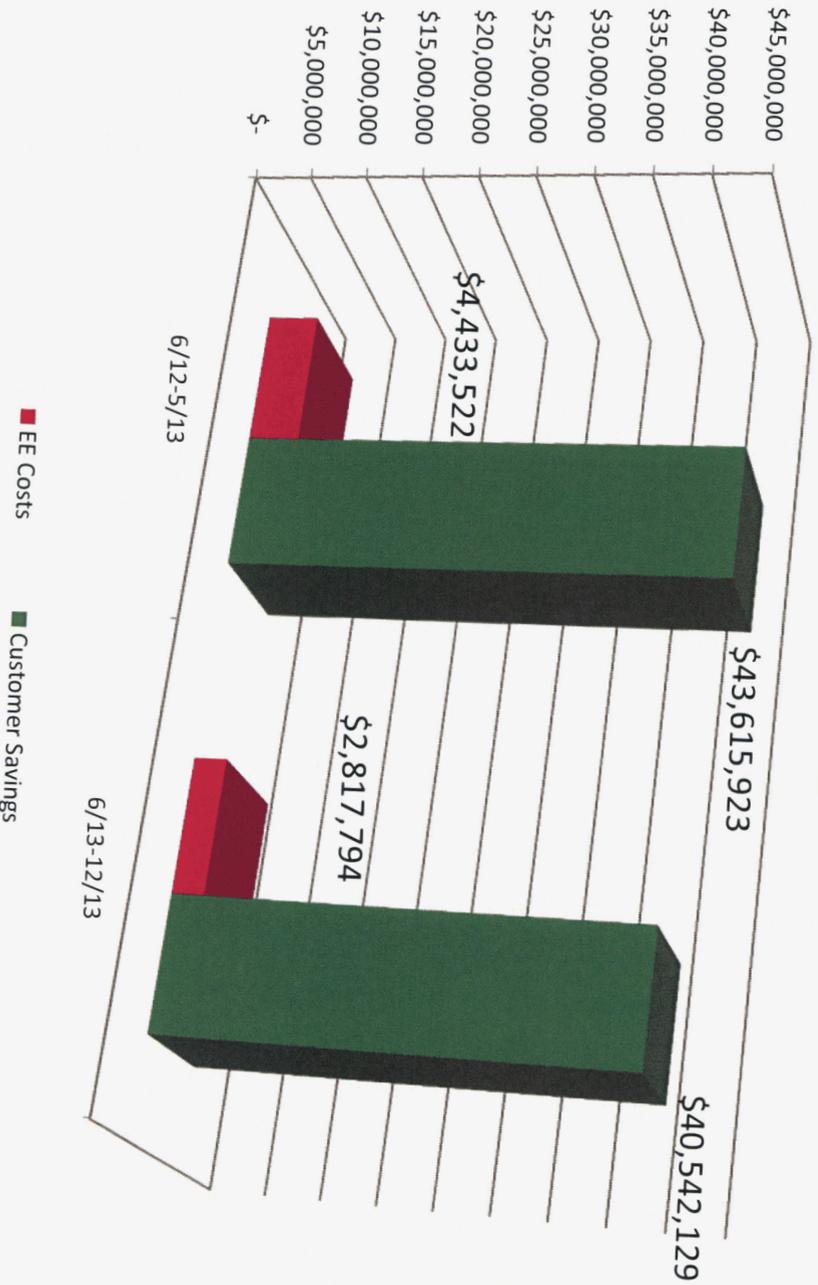


Benefits of Full Decoupling

- **Improved credit rating – resulting in lower debt costs**
- **Customer Protections**
 - Protects customers from high winter bills
 - Ensures customers pay no more than Commission authorized costs
 - Limiting utility profit from increased sales
 - Enhancing utility focus on cost control
 - Allows both upward and downward rate adjustments
 - Decreases frequency of general rate cases
- **Maximizes customer savings opportunities**
 - By fully aligning company and customer interest in promoting energy efficiency

Benefits of Full Decoupling

Energy Efficiency Savings
Over Life of EE Measures



Summary

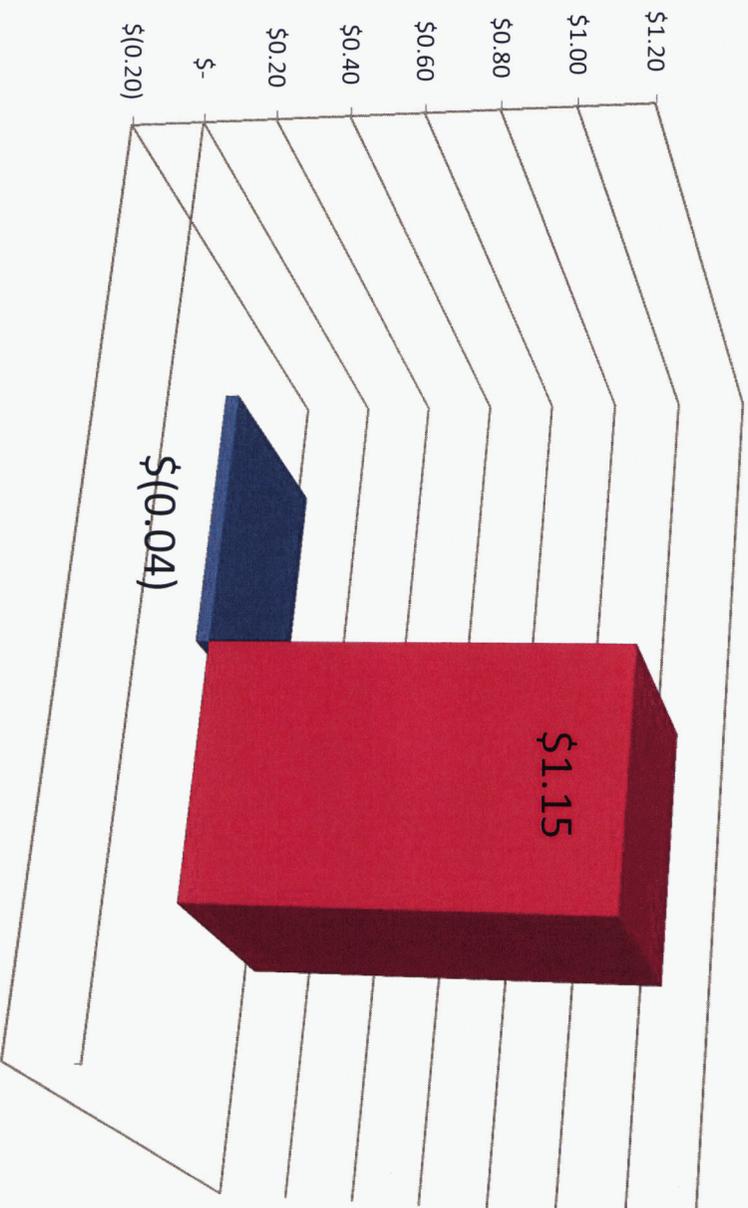
- **Improved credit ratings – resulting in lower debt costs**
 - Stabilizes cash flow and stabilizes customer bills

	Standard & Poor's	Moody's	Fitch
2011	BBB+	Baa2	BBB+
Today	A-	A3	A

- **Customer Protections**
 - High winter bills and symmetrical adjustments
 - Customers pay no more than Commission authorized
 - Decreases the frequency of general rate cases
- **Vital to the success of Energy Efficiency programs**
 - Removes utility throughput incentive
 - Cumulative Southwest Gas customer savings of \$84M

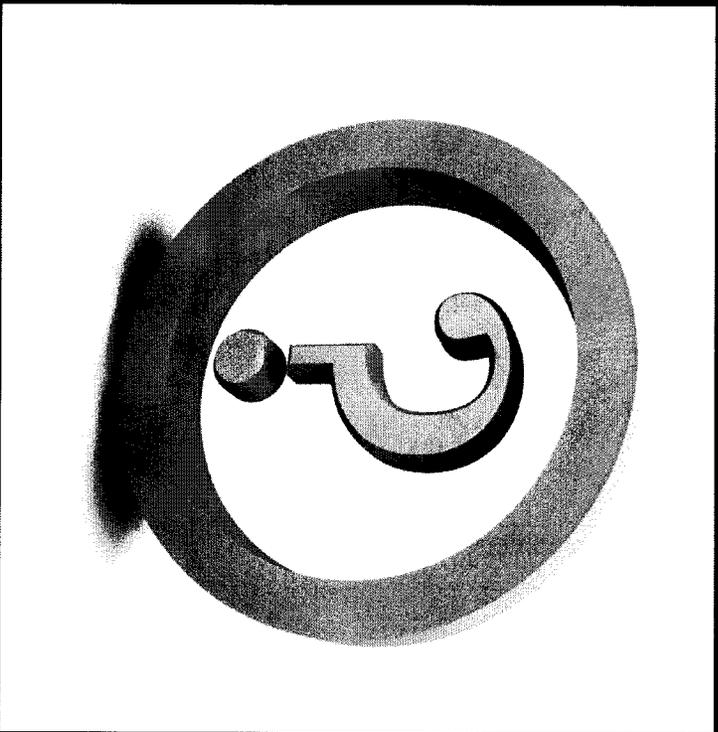
Benefits of Full Decoupling

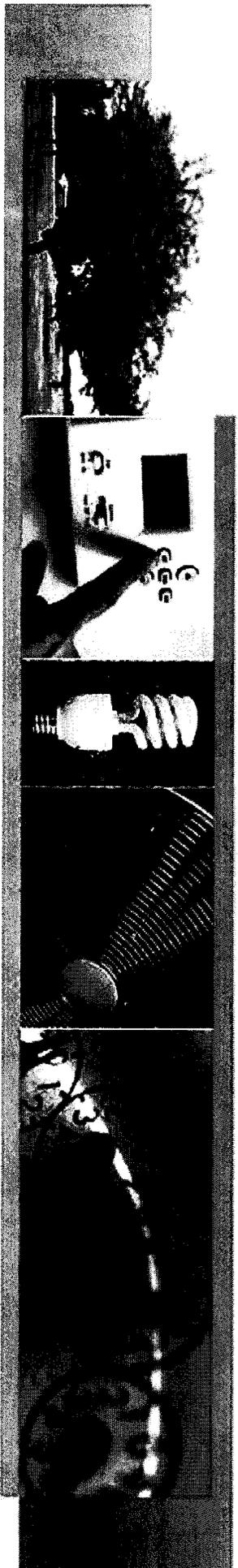
Minimize Residential Bill Impact



■ Decoupling Adjustment ■ BSC Increase

Questions





Energy Efficiency and Integrated Resource Planning

Cost Recovery Workshop

March 31, 2014



Tucson Electric Power



Today's Discussion Items

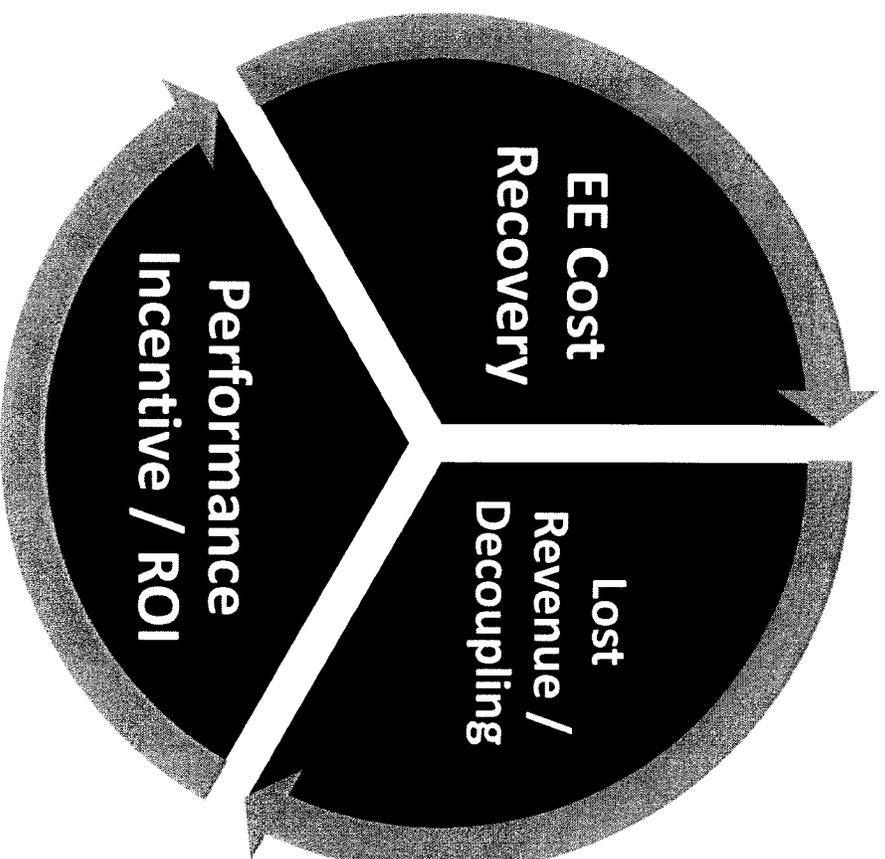
- EE Cost Recovery Mechanisms
- Utility Incentives
- Methods for utility recovery of authorized non-EE fixed costs



Tucson Electric Power



Three Paths to Cost Recovery



EE Cost Recovery

- Recovery of direct program expenses:
 - Rebates
 - Marketing
 - Program Administration
- Mechanisms
 - Contemporaneous recovery in a surcharge
 - Rate Base investment



Tucson Electric Power

Utility Incentives

- Performance incentives allow the utility to earn a return – same as supply side investments
- Properly designed performance incentives can ensure cost-effective EE investments



Tucson Electric Power

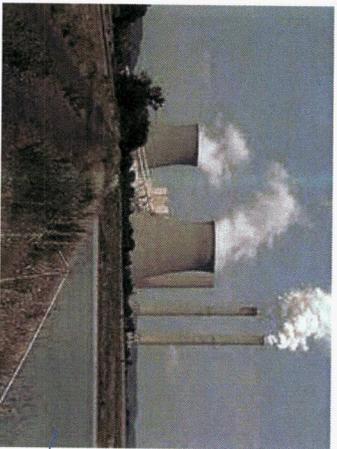
Recovery of Authorized Fixed Costs

- Primary goal: Fairness and equity
 - More cost-based rate design
 - Full decoupling
 - Partial decoupling (LFQR – current model)



Tucson Electric Power

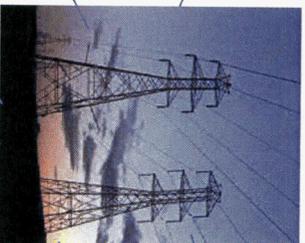
Residential Cost of Utility Service



Generation: \$145 Million



Distribution: \$43 Million



Transmission: \$56 Million




Tucson Electric Power

Costs from TEP 2012 Rate Case


UniSourceEnergy
SERVICES

Current Method: Volumetric recovery

	 House A	 House B	 House C	 House D	
<u>Cost of energy</u>	835	835	835	835	3,340
Fixed cost	\$55.00	\$55.00	\$55.00	\$55.00	\$220.00
Fuel cost	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$110.22</u>
Total bill	\$82.56	\$82.56	\$82.56	\$82.56	\$330.22

	<u>Cost of energy if House D uses 20% less</u>				
	835	835	835	668	3,173
Fixed cost	\$57.90	\$57.90	\$57.90	\$46.30	\$220.00
Fuel cost	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$22.03</u>	<u>\$104.70</u>
Total bill	\$85.46	\$85.46	\$85.46	\$68.33	\$324.70

<u>Change in bill to customer</u>					
	\$2.90	\$2.90	\$2.90	(\$14.22)	(\$5.52)



Tucson Electric Power



Preferred: Fixed Recovery of Fixed Costs

	 House A	 House B	 House C	 House D	
<u>Cost of energy</u>					
Fixed cost	835	835	835	835	3,340
Fuel cost	\$55.00	\$55.00	\$55.00	\$55.00	\$220.00
Total bill	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$110.22</u>
	\$82.56	\$82.56	\$82.56	\$82.56	\$330.22

	kWh				
<u>Cost of energy if House D uses 20% less</u>					
Fixed cost	835	835	835	668	3,173
Fuel cost	\$55.00	\$55.00	\$55.00	\$55.00	\$220.00
Total bill	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$27.56</u>	<u>\$22.03</u>	<u>\$104.70</u>
	\$82.56	\$82.56	\$82.56	\$77.03	\$324.70

<u>Customer bill impact</u>				
	\$0.00	\$0.00	\$0.00	(\$5.52)
				(\$5.52)

Fixed Cost Recovery

- Cost recovery consistent with how costs are incurred
 - Customer charges
 - Access charges
 - Demand charges
 - ???



Tucson Electric Power

Questions?