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2 on January 25, 2012, to parties of record

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6 By: /s/Craig A. Marks

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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

GARY PIERCE – Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF
ARIZONA PUBLIC SERVICE COMPANY FOR
A HEARING TO DETERMINE THE FAIR
VALUE OF THE UTILITY PROPERTY OF THE
COMPANY FOR RATEMAKING PURPOSES,
TO FIX A JUST AND REASONABLE RATE OF
RETURN THEREON, TO APPROVE RATE
SCHEDULES DESIGNED TO DEVELOP SUCH
RETURN.

DOCKET NO. E-01345A-11-0224

**REBUTTAL TESTIMONY
OF
NANCY BROCKWAY
ON BEHALF OF AARP
SUPPORTING SETTLEMENT AGREEMENT
JANUARY 25, 2012**

1 **EXECUTIVE SUMMARY**

2 In my Rebuttal Testimony I respond to arguments made by the National Resources Defense Fund
3 (NRDC) and the Southwest Energy Efficiency Project (SWEEP) in opposition to the Settlement
4 Agreement. I recommend that the Commission not adopt these parties' request that LFCR as
5 contained in the Settlement Agreement be rejected. I affirm my recommendation that the
6 Commission adopt the Settlement Agreement as a just and reasonable resolution of the issues in
7 the docket.

8 **Response to SWEEP**

9 The proposed settlement does not limit the Commission's discretion to determine energy
10 efficiency policy. The Commission is not bound to accept the Settlement Agreement. Nor is it
11 bound to implement the December 2010 Policy Statement's preferred decoupling mechanism. If
12 the Commission rejects the Settlement Agreement because it fails to include SWEEP's preferred
13 revenue decoupling mechanism, the Settlement Agreement will lose support and parties will seek
14 to litigate the full range of issues in the case. SWEEP's preferred revenue decoupling
15 mechanism is not necessary to ensure that APS achieves its targets under the Electric Energy
16 Efficiency Standards. Further, it transfers unreasonable levels of risk to consumers. In addition,
17 SWEEP does not propose any adjustment to the agreed return on equity to reflect this reality.
18 The mechanism agreed to by APS and the Signatories in the Settlement Agreement, Lost Fixed
19 Cost Recovery, is a targeted decoupling mechanism that will be effective in removing the
20 financial disincentive for APS to invest in energy efficiency. SWEEP's other proposed
21 adjustments are not contemplated by the Settlement Agreement, and are not reasonable, much
22 less essential.

Response to NRDC

23 The response to SWEEP covers all the issues raised by NRDC in its partial opposition to the
24 Settlement Agreement.

I. INTRODUCTION

1 **Q. ARE YOU THE SAME NANCY BROCKWAY WHO FILED TESTIMONY IN**
2 **THIS DOCKET ON NOVEMBER 18, 2011, DECEMBER 2, 2011, AND JANUARY**
3 **18, 2012?**

4 A. Yes.

5 **Q. WHICH PARTY IS SPONSORING YOUR TESTIMONY?**

6 A. AARP is sponsoring my testimony in this docket.

II. OPPOSITION TO THE SETTLEMENT FROM NRDC AND SWEEP

7 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY FILED TODAY?**

8 A. The purpose of my testimony is to respond to arguments made by the Southwest Energy
9 Efficiency Project (“SWEEP”) and the Natural Resources Defense Council (“NRDC”) in
10 opposition to the Settlement Agreement.

11 **A Response to SWEEP**

12 **Q. PLEASE SUMMARIZE THE ARGUMENTS OF SWEEP WITNESS JEFF**
13 **SCHLEGEL CONCERNING THE SETTLEMENT AGREEMENT.**

14 A. On pages 2 to 3 of his testimony regarding the proposed settlement agreement, Mr.
15 Schlegel argues that

16 1. The proposed Settlement Agreement limits the Commission from fully exploring
17 the full revenue decoupling option for addressing utility disincentives to energy
18 efficiency.

19 2. Full revenue decoupling is a superior option for the treatment of utility
20 disincentives to energy efficiency.

21 3. Rate case stay-out provisions limit the Commission's ability to direct energy
22 policy.

1 4. The Commission should adopt SWEEP's recommended timing, objectives and
2 design criteria for an energy efficiency performance incentive.

3 5. Energy efficiency expenses should be moved from the DSM Adjustor to base
4 rates, and then subject to the DSM adjuster between rate cases.

5 6. The Commission should require that test-year sales be adjusted to reflect
6 efficiency expected to come from Commission-adopted policies.

7 **Q. DOES THE SETTLEMENT LIMIT THE COMMISSION'S DISCRETION?**

8 A. No. The Commission continues to have complete discretion to determine the range of
9 acceptable methods to address the question of utility financial disincentives to invest in
10 energy efficiency. The Commission's action in approving or disapproving this Settlement
11 Agreement is a choice it will make, based on its review of the entirety of the Settlement
12 Agreement and the alternative of continuing litigation of the case. SWEEP did not join
13 the Settlement for the primary reason that the Settlement Agreement if approved would
14 authorize the use of a targeted decoupling mechanism, the Lost Fixed Cost Recovery
15 ("LFCR"), instead of the method SWEEP prefers, full revenue decoupling. If the
16 Commission considers that full revenue decoupling is the only acceptable means of
17 addressing utility financial disincentives to energy efficiency, and determines that full
18 revenue decoupling is a more important policy goal than the other aspects of the
19 Settlement Agreement, it will reject the Settlement Agreement. In such a case, the parties
20 that support the Settlement Agreement would no longer be bound by it and would be free
21 to make whatever arguments they desire. Presumably, the case would return to Hearing
22 Division for further hearings to develop a full record concerning the parties' pre-
23 Settlement Agreement positions. Hearings would be held, briefs filed, and all of the
24 issues in the docket would be before the Commission for determination, subject to any

1 applicable appeals. The Commission is not required to adopt the Settlement Agreement,
2 and is not limited by the Settlement Agreement.

3 **Q. COULD THE COMMISSION KEEP MOST OF THE SETTLEMENT**
4 **AGREEMENT BUT SUBSTITUTE FULL REVENUE DECOUPLING FOR THE**
5 **LFCR DECOUPLING AGREED TO BY THE SIGNATORIES?**

6 A. No. SWEEP and NRDC recommend that the Commission approve all of the Settlement
7 Agreement except the decoupling aspects. With all due respect, this is not an option.

8 Settlements constitute hard-bargained agreements in which typically all signatories give
9 up their position on some issues in exchange for agreement of the parties to live with a
10 particular outcome on issues a party considers more important. Section 20.5 of the
11 Settlement Agreements acknowledges this fundamental fact by reciting that if the
12 Commission rejects any material part of the Settlement Agreement, any signatory may
13 withdraw its agreement. If the Commission believes full revenue decoupling is the *only*
14 valid policy, it could reject the Settlement Agreement in its entirety, and indicate its
15 preferences related to decoupling. Further, the Commission is not bound to approve the
16 Settlement Agreement, as is acknowledged by the Signatory Parties in Section 20.4. But
17 a Commission cannot merely substitute one provision and retain the balance of the
18 Agreement intact.

1 **Q. IF THE COMMISSION WERE TO REJECT THE PROPOSED SETTLEMENT**
2 **AGREEMENT AND INDICATE THAT IT WOULD ACCEPT IT IF THE**
3 **AGREEMENT WERE AMENDED TO ADOPT FULL REVENUE**
4 **DECOUPLING, WHAT WOULD YOU RECOMMEND TO AARP?**

5 A. I would recommend that AARP withdraw from the Settlement Agreement, and proceed
6 to its litigation options. The decoupling issue in this docket is a material issue by any
7 reasonable definition of that term. The risks of full revenue decoupling constituted the
8 bulk of the testimony filed by me on behalf of AARP in this docket. AARP considers
9 full revenue decoupling an unnecessary approach to utility disincentives, and one that
10 transfers risk to consumers without compensating benefits.

11 **Q. IS LOST FIXED COST RECOVERY "CLEARLY INFERIOR" TO FULL**
12 **REVENUE DECOUPLING?**

13 A. No. For the reasons I discussed at length in my earlier testimonies, lost fixed cost
14 recovery is a targeted means to remove the economic disincentive for utilities to engage
15 in efficiency investments. Full decoupling is not necessary to achieve this goal. Further,
16 as I also previously discussed, with Lost Fixed Cost Recovery the Company continues to
17 bear those risks which it is better able to manage, such as weather variations, rather than
18 shifting those risks to consumers. Finally, the Settlement Agreement contains an opt-out
19 provision, allowing customers who prefer to take service under rates designed to recover
20 assigned revenues less on a usage basis than is the case with regular rates subject to the
21 LFCR adjustment. In contrast, full revenue decoupling would presumably apply to all
22 customers.

1 **Q. IS FULL REVENUE DECOUPLING NECESSARY IN ORDER FOR UTILITIES**
2 **TO SUPPORT NON-UTILITY EFFORTS TO SAVE ENERGY?**

3 A. No. The State of Arizona can adopt energy efficiency standards and other non-utility
4 public policies regardless of the indifference, or for that matter the opposition, of utilities.
5 Many states have used lost fixed cost recovery and different efficiency incentive
6 mechanisms with success. For example, when Massachusetts utilities were receiving
7 incentive payments without decoupling, they were already among the national leaders in
8 their commitment to efficiency. APS itself has agreed to the LFCR mechanism, and
9 withdrawn its assertion that it cannot meet its efficiency targets under the Electric Energy
10 Efficiency Standards. Further, any full decoupling imposed to support non-utility energy
11 efficiency policies with "enthusiasm," as requested by SWEEP, must be balanced against
12 the impact of full decoupling on the transfer of risk from the utilities to the consumers.

13 **Q. SWEEP ARGUES THAT USE OF LFCR WILL LEAD TO DISPUTES OVER**
14 **THE EXTENT TO WHICH UTILITY PROGRAMS ACHIEVED THEIR**
15 **EFFICIENCY GOALS. HOW DO YOU RESPOND?**

16 A. I am unaware of extensive litigation on program impacts engendered by LFCR policies in
17 other states. There may from time to time be some disputes concerning whether a utility
18 has achieved its energy-efficiency goals. However, these disputes would demonstrate the
19 fact that the LFCR mechanism will better promote accountability than full revenue
20 decoupling. Eliminating the question of utility performance by adopting full revenue
21 decoupling would mask inferior efficiency production, and remove incentives and
22 opportunities to explore the performance of the utility on its efficiency goals.

1 Further, in his Direct Testimony, Mr. Schlegel states that APS should prepare and file
2 precisely the kinds of information that would be the subject of such disputes. At pages 9-
3 10, Mr. Schlegel asks the Commission to order APS to "document in its filings before the
4 Commission reductions in forecasted or planned costs in meeting the needs of customers
5 and their forecasted loads, including deferral of plant investments and a lower level of
6 plant investments, as a result of energy efficiency expansion as required by the EEES.
7 The Company should also include document such utility system cost reductions as a
8 result of increased energy efficiency and reduced customer loads in its demand side
9 management reports." Such reports cannot be made without reliable estimates of the
10 extent to which APS programs induced particular energy and demand reductions. Unless
11 the proposed reports are intended to be meaningless, it is possible that disputes will arise
12 under the SWEEP proposals in similar fashion to any that would arise under LFCR.

13 **Q. HAS THE COMMISSION RULED THAT FULL REVENUE DECOUPLING IS**
14 **THE ONLY ACCEPTABLE WAY TO ADDRESS UTILITY DISINCENTIVES TO**
15 **EFFICIENCY?**

16 A. Not to my knowledge. The Commission adopted a policy statement favoring full revenue
17 decoupling in December 2010. But that policy statement did not have the force of law.
18 The Commission did not undertake a rulemaking or an adjudication of a contested case.
19 The policy statement provides a snapshot of the Commissioners' position concerning
20 decoupling based on the facts and circumstances as of December 2010. By contrast, in
21 this docket, the parties are actually litigating the issues considered in the Policy
22 Statement. The Commission did not exclude the vigorous exchange of views on utility
23 disincentives in this docket. No party claimed that the parties were "relitigating"

1 decoupling in this docket until after a Settlement Agreement was filed in which a
2 majority of the parties agreed to the LFCR mechanism. Finally, it is inappropriate to
3 claim that the parties are “relitigating” any issues. Again, this is the first time that
4 decoupling has been litigated concerning APS.

5 **Q. DOES SWEEP PROPOSE ANY CHANGE TO THE RATE OF RETURN ON**
6 **EQUITY IN THE SETTLEMENT AGREEMENT TO REFLECT ITS PROPOSED**
7 **EXPANSION OF DECOUPLING TO ALL FACTORS, INCLUDING WEATHER**
8 **AND OTHER NON-EFFICIENCY RISKS?**

9 A. No. If the Commission rejects the Settlement Agreement because the Agreement fails to
10 use SWEEP's preferred decoupling mechanism, the allowed rate of return would be one
11 of the key issues that some or all the Signatories would want to revisit in litigation.

12 **Q. SWEEP ARGUES THAT THE STAY-OUT PROVISION OF THE SETTLEMENT**
13 **AGREEMENT WILL PREVENT THE COMMISSION FROM PURSUING**
14 **POLICY INITIATIVES. DO YOU AGREE?**

15 A. No. Mr. Schlegel appears to assume that the Commission will be barred from initiating a
16 review of the Company's overall rates and revenue requirements if it approves Section
17 2.1. On the face of the Agreement, this conclusion is incorrect. In fact, Section 2.1
18 prevents only APS from filing a rate case before the deadline. As explicitly recognized
19 by Section 19.1, the Settlement Agreement does not limit the Commission's authority to
20 investigate rates and set revenues on its own initiative. Further, even if it were
21 interpreted to limit any investigation of overall rates and revenues as suggested by Mr.
22 Schlegel, this would not deprive the Commission of its authority to investigate demand-
23 side management efforts of the Company. Indeed, the Commission has established a

1 regular process for reviewing utility energy efficiency efforts through the DSM
2 Adjustment Mechanism process.

3 **Q. MR. SCHLEGEL PROPOSES THAT THE COMMISSION SHOULD ADOPT**
4 **SWEEP'S RECOMMENDED TIMING, OBJECTIVES AND DESIGN CRITERIA**
5 **FOR AN ENERGY EFFICIENCY PERFORMANCE INCENTIVE. DO YOU**
6 **AGREE?**

7 A. No. Mr. Schlegel's proposals on the performance incentive are unnecessary to encourage
8 efficiency achievements. APS, whose performance such incentives are intended to
9 promote, has agreed to the incentives proposed in the Settlement Agreement. Also, as
10 noted above, APS has withdrawn the suggestion that it cannot meet its targets under the
11 Electric Energy Efficiency Standards. Further, the Signatories propose a process for
12 exactly the review of performance incentives that SWEEP seeks. What is at stake is a
13 slight timing difference. This difference is reasonable in light of the extent of issues
14 involved, which deserve full discussion by the stakeholders and full review by the
15 Commission.

16 **Q. MR. SCHLEGEL ARGUES THAT ENERGY EFFICIENCY EXPENSES**
17 **SHOULD BE MOVED FROM THE DSM ADJUSTOR TO BASE RATES, AND**
18 **THEN SUBJECT TO THE DSM ADJUSTER BETWEEN RATE CASES, TO**
19 **PROMOTE A STABLE COMMITMENT TO EFFICIENCY INVESTMENTS. DO**
20 **YOU AGREE?**

21 A. I do not think Mr. Schlegel's proposal will have the stabilizing effect he seeks. He agrees
22 that the amount of DSM spending in base rates will be subject to revision up or down in
23 the DSM adjustment process. This means that the DSM expenditures will be as

1 susceptible to variation under the SWEEP proposal as they are today. The difference is
2 cosmetic.

3 **Q. MR. SCHLEGEL ARGUES THAT TEST YEAR SALES REVENUES SHOULD**
4 **BE ADJUSTED TO REFLECT ANTICIPATED ENERGY SAVINGS FROM**
5 **DSM. DO YOU AGREE?**

6 A. No. The Settlement Agreement does not provide for the adjustment proposed by
7 SWEEP. APS has accepted the provisions of the Settlement Agreement as sufficient to
8 protect the utility's ability to earn a reasonable return. The adjustment should not be
9 adopted absent an opportunity for full litigation.

10 **B Response to NRDC**

11 **Q. PLEASE SUMMARIZE THE ARGUMENTS OF NRDC IN OPPOSITION TO**
12 **THE SETTLEMENT, AND TO YOUR TESTIMONY ON EFFICIENCY ISSUES**
13 **IN THIS DOCKET.**

14 A. NRDC witness Ralph Cavanagh summarizes his arguments at pages 1 - 4 of his
15 testimony on the proposed settlement. He argues that:

- 16 1. The Settlement Agreement proposes the use of a "clearly inferior" alternative to
17 full revenue decoupling.
- 18 2. The Settlement Agreement "attempts to prevent the Commission" from choosing
19 the full revenue decoupling mechanism included in the December 2010 Final
20 Policy Statement Regarding Utility Disincentives to Energy Efficiency and
21 Decoupled Rate Structures ("Policy Statement on Utility Disincentives" or
22 "Policy Statement"), and the Commission's order approving the Settlement
23 Agreement in the recent Southwest Gas case.

1 3. I essentially ignored the Commission's Policy Statement on Utility Disincentives
2 and "tried to relitigate issues" that the Policy Statement addressed fully.

3 **Q. IS IT NECESSARY TO FURTHER RESPOND TO NRDC?**

4 A. No. I fully address NRDC's arguments in my response to SWEEP.

5
6 **III. CONCLUSION**

7 **Q. IN LIGHT OF THE SWEEP AND NRDC TESTIMONY, DO YOU CONTINUE**
8 **TO RECOMMEND THAT THE COMMISSION APPROVE THE SETTLEMENT**
9 **AGREEMENT?**

10 A. Yes.

11 **Q. WHY DO YOU STILL RECOMMEND THAT THE COMMISSION APPROVE**
12 **THE SETTLEMENT AGREEMENT?**

13 A. The Settlement Agreement represents a sensible and reasonable resolution of the issues
14 presented in the APS request for a general rate increase. The SWEEP and NRDC
15 testimonies do not persuade me and should not persuade the Commission that full
16 revenue decoupling is necessary or productive in removing incentives for APS to pursue
17 efficiency with vigor. As is the case with all settlements (and for that matter most
18 Commission orders or other dispositions of a rate case), the Settlement Agreement
19 contains some elements that I and AARP would have preferred not to see implemented,
20 and neglects to include some elements that I and AARP would have preferred to see
21 adopted. On balance, however, it resolves the rate case issues in a way that is just and
22 reasonable to all parties. If the SWEEP/NRDC proposals were adopted, the Settlement

1 Agreement would no longer constitute a balanced package that I could recommend that
2 AARP support.

3 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY SUPPORTING THE**
4 **SETTLEMENT AGREEMENT?**

5 A. Yes.