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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF IDAHO POWER COMPANY'S REQUEST TO MODIFY RECOVERY OF INCENTIVES PAID TO SECURE DEMAND-SIDE RESOURCES	))))	CASE NO. IPC-E-10-27

TESTIMONY IN SUPPORT OF THE STIPULATION

NANCY HIRSH

March 4, 2011

Q. Please state your name, affiliation, and reason for this testimony.

A. My name is Nancy Hirsh and I am the Policy Director for the NW Energy Coalition. I have been with NWEC since 1996 and before that spent twelve years in Washington, DC working on national energy policy issues for the Environmental Action Foundation and the National Wildlife Federation. I offer the following testimony in support of the Stipulation filed in this case.

Q. In case IPC-E-09-30, Idaho Power, the staff, and other parties stipulated to a moratorium on filing "a general revenue requirement case which would result in a general rate adjustment becoming effective prior to January 1, 2012." Do you believe this moratorium prohibits the filing of the present case?

A. My attorney advises me that the stipulation in IPC-E-09-30 does not prohibit this filing. Beyond the legal interpretation, the plain language of that stipulation is clear. Paragraph 5.2 expressly allows Idaho Power to file, and this Commission to approve requests to "adjust its revenue requirement and change rates to become effective prior to January 1, 2012" for certain mechanisms including the Annual Power Cost Adjustment and the Energy Efficiency Rider.

The stipulation in the present case falls within these allowable filings. In a broad sense, this stipulation in this case merely changes accounting practices and does not involve a wholly new revenue requirement. This stipulation does not ask the Commission to approve specific expenses as prudent for ratemaking purposes. The Commission will be able to review the prudency of specific expenditures in future cases. For example, the stipulation allows Idaho Power to collect future demand response incentive payments through the Power Cost Adjustment (PCA). During the annual PCA filing, Idaho Power will need to demonstrate that the specific incentive payments were prudent expenses. In short, this stipulation changes the accounting method for certain demand-side management (DSM) programs, it does not change Idaho Power's general revenue requirement.

Q. Why is this stipulation in the public interest?

A. This stipulation provides a critical piece of regulatory support so that Idaho Power has the proper incentives to pursue cost effective DSM. The public will benefit from this stipulation because cost effective demand-side investments will, by definition, defer or avoid investments in more expensive supply-side resources. To ensure on-going aggressive pursuit of demand-side resources they must be financially evaluated on equal footing with supply-side resources. The terms of the stipulation change the funding approach for certain demand-side resource investments to better align their funding with the business interests of the Company and the acquisition of the lowest cost resources. This stipulation bolsters regulatory support for Idaho Power to pursue all cost effective DSM and treats demand response incentives in a manner more consistent with other peak management strategies. In short, it aligns regulatory policy so that Idaho Power continues to spend pennies now to avoid dollars later.

Q. How does this stipulation help align regulatory policy to pursue cost effective DSM?

A. This Commission has steadfastly ordered Idaho utilities to pursue all cost effective DSM. This is a commendable goal and now the regulatory structure must support this goal. Supportive regulatory structure begins with the timely recovery of DSM expenses. The energy efficiency rider is designed to do this. Next, the regulatory structure must remove economic disincentives to invest in DSM. The fixed cost adjustment pilot program accomplishes this by decoupling fixed cost recovery from volumetric sales. Finally, regulators must provide an economic incentive at least equal to that of supply-side resources. When a utility invests capital in a supply-side resource, it has the opportunity to earn a return on that capital. This stipulation provides the third piece of the puzzle; the opportunity to earn a return on prudently invested capital

In the late 1980s and early 1990s, Idaho Power did capitalize some of its energy efficiency program investments. Then most utilities in the region transitioned to expensing DSM

investments via dedicated DSM tariffs. This approach was successful while DSM budgets were modest. Today, DSM budgets are significantly greater and on par with many capital resource investments made by the company. Regulators can no longer expect utilities to pursue DSM as a significant resource to meet loads unless they have an opportunity to earn a return on capital they invest in DSM. This stipulation provides the missing piece of the regulatory support puzzle.

Q. Idaho Power has a suite of DSM programs currently. Based on this, is an incentive mechanism necessary?

A. Yes it absolutely is. Over the past seven years, DSM programs have evolved from a customer service program to a full fledge resource option. During the Integrated Resource Plan (IRP) process, Idaho Power factors savings from DSM programs into its load forecast before considering supply-side resources. However, given all of the regulatory support pieces mentioned above, I believe Idaho Power could achieve substantially greater demand reductions. For example, Idaho Power's *2009 DSM Potential Study* defines three levels of DSM potential: technical, economic, and achievable. The study calculates the economic potential, defined as all cost effective DSM, is roughly 325 GWh by 2028 in the residential class. Meanwhile, the achievable potential, which considers the expected market penetration, is roughly 45 GWh.[1] While this example describes the residential class, the same holds true for the commercial and industrial classes. With an economic incentive, we can expect Idaho Power to redouble its efforts to close the DSM potential gap because this area becomes a profit center instead of a business expense. Without an economic

[1] *See* Attachment 1 *Figure 3.1 Residential Electricity Potential Savings Forecast* (The numbers cited above are rough numbers based on this figure); Figure 4.1 *Commercial Electricity Savings Forecast;* and Figure 5.1 *2009 Industrial Potential GWh Savings and Percent of Total Sales* from Nexant, *Idaho Power Demand Side Management Potential Study,* (August 14, 2009). The entire report was filed with the Commission in Case No. IPC-E-10-09 in the Research and Evaluation portion of Supplement II of the Company's 2009 DSM Annual Report.

incentive to pursue DSM, we cannot expect Idaho Power to close the gap between economic and achievable potential in a timely and cost-effective manner.

Q. Do other states provide economic incentives for DSM?

A. Yes. A recent report by the American Council for an Energy-Efficient Economy *Carrots for Utilities: Providing Financial Returns for Utility Investments in Energy Efficiency* analyzed incentives in 18 states.[2] The report divides incentive mechanisms into three categories: shared benefits, performance targets, and rate of return. Regardless of the specific mechanism, the report explains that financial incentives work hand in hand with decoupling to level the playing field for DSM.

Paragraph 8 of the stipulation in this case describes a rate of return mechanism for the incentive payments made under the Custom Efficiency Program. This is the least common approach outlined in the *Carrots for Utilities* study but the correct mechanism for Idaho. It is the correct mechanism because it is simple, fair, and encourages robust DSM programs.

Q. Can you expand on why the economic incentive in this case is simple, fair, and encourages robust DSM programs?

A. It is simple because unlike the other options it does not rely on estimates of energy savings to determine the benefits to share or whether a target is reached. Instead, Idaho Power chose, and most parties agreed, to select the most robust and verifiable program, Custom Efficiency, and provide the Commission-authorized rate of return that reflects the risk applicable to any other capital investment. It is fair because it places DSM investments on equal footing with supply-side resources. It encourages robust DSM programs because the first program, Custom Efficiency, sets

[2] See ACEEE, *Carrots for Utilities: Providing Financial Returns for Utility Investments in Energy Efficiency*, Report No. U111 (January 2011). Available for free download at: http://www.aceee.org/research-report/u111 (accessed March 1, 2011).

a good standard for potential future programs in that it is measurable, durable, sizable, and cost effective.

This contrasts with Idaho Power's former incentive mechanism tied to the market share of new homes that meet the ENERGYSTAR Homes Northwest standards. After reviewing the history of that mechanism, I believe it did not succeed in part because it was complex, appeared unfair, and did not encourage robust programs. Under the *Carrots for Utilities* framework, this incentive was a performance target, which can be very successful yet is a more complex approach. The mechanism required calculating some level of market share that would trigger an incentive, a difficult calculation to get right particularly in rapidly changing economic conditions. It appeared unfair because the incentive functioned as a bonus payment to Idaho Power shareholders something the public generally perceives as unwarranted. Finally, it did not encourage robust DSM programs because it applied to a very small program and would have been difficult to apply to other parts of the Company's DSM portfolio. Unlike this former incentive, the proposal in this stipulation creates a simple mechanism that encourages Idaho Power to aggressively pursue all the cost effective savings within the Custom Efficiency market.

Another reason why the rate of return mechanism in this stipulation is the right mechanism for Idaho is that it can be incrementally expanded. By adopting a program-by-program approach, beginning with Custom Efficiency, the Commission and other stakeholders can incrementally add programs that meet certain standards. In the end, the incentive mechanism in this stipulation is a careful, measured step towards providing the regulatory carrot that helps fulfill the obligation to pursue all cost effective DSM investments.

Q. Does the rate of return approach encourage the Company to invest money in DSM without regard for savings achieved?

A. No. The program scale and design, including the incentive levels, would still be established under the supervision of the Energy Efficiency Advisory Group. The EEAG also reviews proposed and actual savings levels to ensure cost-effective program implementation. Finally, all stakeholders and the Commission will be able to review the prudency of specific expenses in future rate cases and PCA filings.

Q. In addition to the rate of return mechanism, the stipulation also changes the treatment of demand response incentive payments. Do you agree with this portion of the stipulation?

A. Yes. Paragraph 6 of the stipulation provides that Idaho Power will shift the incentive payments for demand response out of the Energy Efficiency Rider and into the Power Cost Adjustment. This move is appropriate for two reasons. First, payments made to curtail load are akin to payments made to serve load. In both instances, the utility is spending money to meet the power demands of its' entire system. Second, demand response programs are designed to reduce loads during peak periods when power supply is limited and market purchases or other peak generation options are high cost. Incenting customers to reduce their usage during these peak periods can reduce overall peak costs in this timeframe. This provides benefits to all customers who would have to pay for the high cost power. The Power Cost Adjustment was primarily developed to address fluctuations in wholesale power costs driven by peak power conditions. The incentives paid to reduce peak loads are analogous to purchasing power to serve those peak loads and as such should be recovered by the Company in a similar manner.

I do want to address one concern that this part of the stipulation raises. All parties must continue to ensure any demand response incentives are prudent investment for ratemaking purposes. For most ratepayers the Power Cost Adjustment is an opaque black hole into which various buckets of money pour and out of which comes a rate impact. As evidenced by Idaho Power's request to make changes to the Irrigation Load Control program in IPC-E-10-46, demand

response programs are continuing to be refined. As demand response payments move into the complex PCA all parties should be cognizant of the need to continue to review demand response payments for prudency and effectiveness of peak load savings Recovery of the incentive through the PCA should in no way reduce Idaho Power and the EEAG's due diligence in program design and implementation to maximize peak load reductions while maintaining cost-effectiveness in the context of peak power costs.

Q. If this stipulation is approved it will affect the Energy Efficiency Rider by reducing the expenses that it must cover. Should the Rider level be reduced?

A. No. The rider should remain at its current level. While moving demand response and Custom Efficiency payments out of the Energy Efficiency Rider account will reduce the current budget imbalance over time the rider must remain at its current level. Regardless of the need to reduce the imbalance, the two changes proposed in this stipulation are appropriate for the reasons previously stated. They better align the interests of the Company with the interests of their customers. In this same vein, I do not believe the rider percentage should decrease as long as there remain untapped cost-effective energy savings that can be acquired in accordance with Commission orders.

Maintaining the current rider level will ensure the unrecovered back balance is paid down in a timely manner while allowing the Company to continue to pursue all cost effective DSM and the associated administrative obligations to support this effort. For instance, when this Commission approved Idaho Power's 2008-2009 DSM expenses it instructed the company to "take affirmative steps towards achieving measurable improvements in its documentation,

verification, and record-keeping process[.]"[3] These efforts cost money and reducing the Rider amount will only frustrate this task.

In addition, Idaho Power proposed and the Commission approved significantly higher funding for the Northwest Energy Efficiency Alliance (NEEA). NEEA delivers some of the lowest cost energy savings in the region and the Commission was right to approve this in Idaho Power's budget. However, at the time the increased funding for NEEA was not wholly accounted for in the rider and now can be accommodated within the existing tariff level.

Finally, the Idaho Power's *Demand Side Management Potential Study* reveals the substantial gap between the economic potential and achievable potential. Only with adequate funding can we expect Idaho Power to continue to close this gap. This stipulation helps ensure adequate funding by moving some expenses into more appropriate categories, but this will only ensure adequate funding of Idaho Power's overall DSM programs if the rider remains at the current level.

Q. Does this conclude your direct testimony as of March 4, 2011?

A. Yes it does.

[3] See Order No. 32113 at 9, IPC-E-10-09 (November 16, 2010).

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ATTACHMENT 1

Selected figures from Nexant, *Idaho Power Demand Side Management Potential Study – Volume 1*

August 14, 2009

IPC-E-10-27

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Submitted To:

IDAHO POWER
An IDACORP Company

Demand Side Management Potential Study – Volume I

Submitted By:

Nexant

August 14, 2009

3.1 SUMMARY OF RESIDENTIAL POTENTIAL

The residential sector alone accounts for 40% of IPC electricity sales with 5,272,077 MWh billed in 2008 out of a total volume of sales of 14,450,350 MWh. In previous years, IPC has developed a set of seven programs aimed at capturing the large energy efficiency resource of the residential sector. Building on its experience with assessing and managing programs for various electric utilities in the North West, Nexant has developed a thorough assessment of the current programs and an outline for new program developments.

Nexant believes that IPC has the potential to double its energy savings in the next five years. Nexant's DSM model forecasts a potential increase of 14 GWh, from 13 GWh of savings in 2009 to 27 GWh of savings in 2014 and 29 GWh in 2019. Figure 3.1 shows the residential potential savings forecast through 2028. This stream of savings would come at a cost of approximately 1.7 cents per kWh for IPC and 6.7 cents per kWh from a Total Resource perspective. Figure 3.2 shows the evolution of each program share relative to the total energy savings.

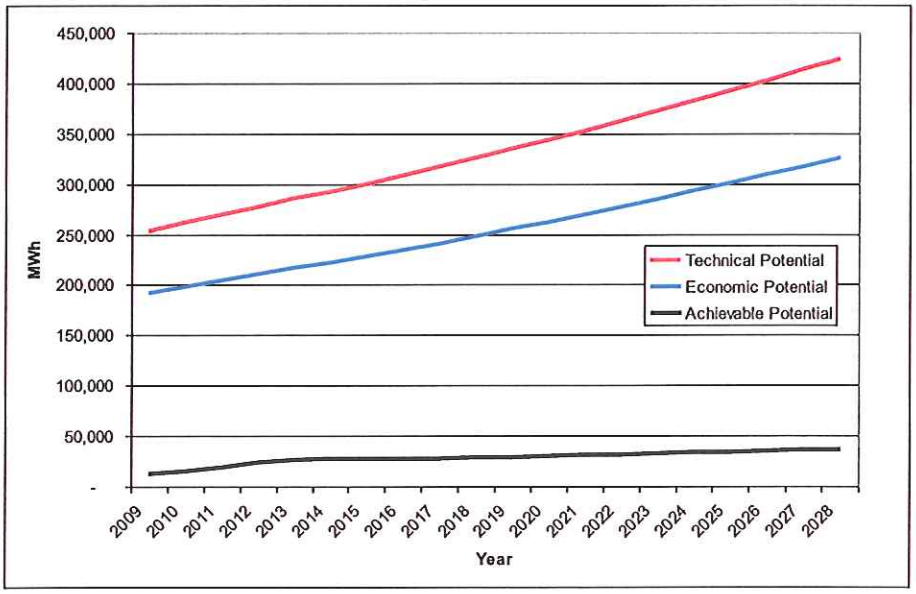

Figure 3.1 Residential Electricity Potential Savings Forecast

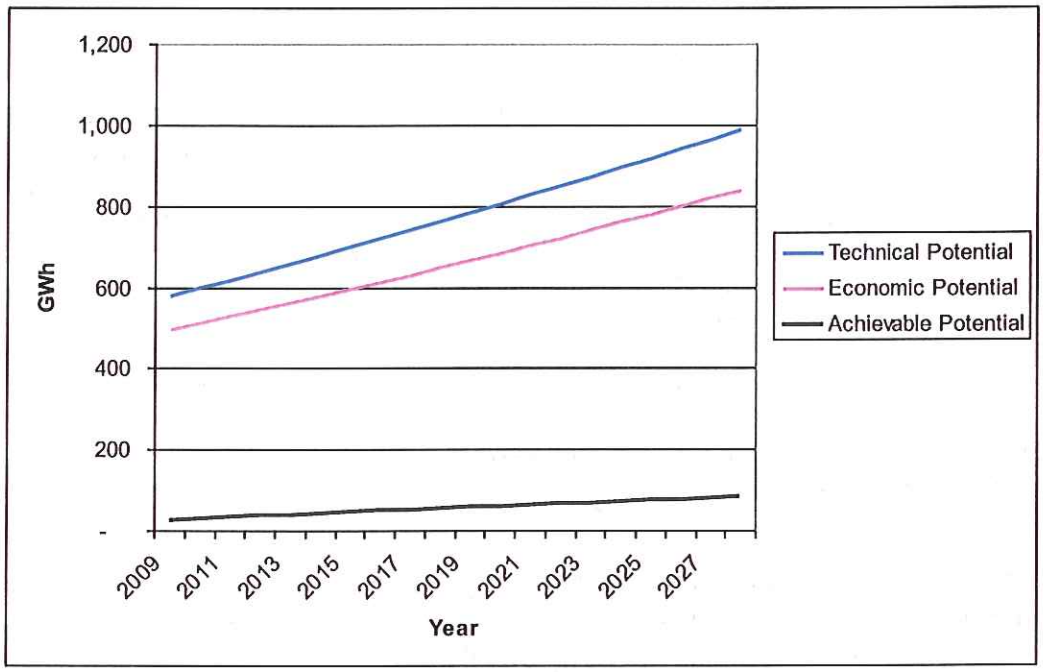

Figure 4.1 Commercial Electricity Savings Forecast

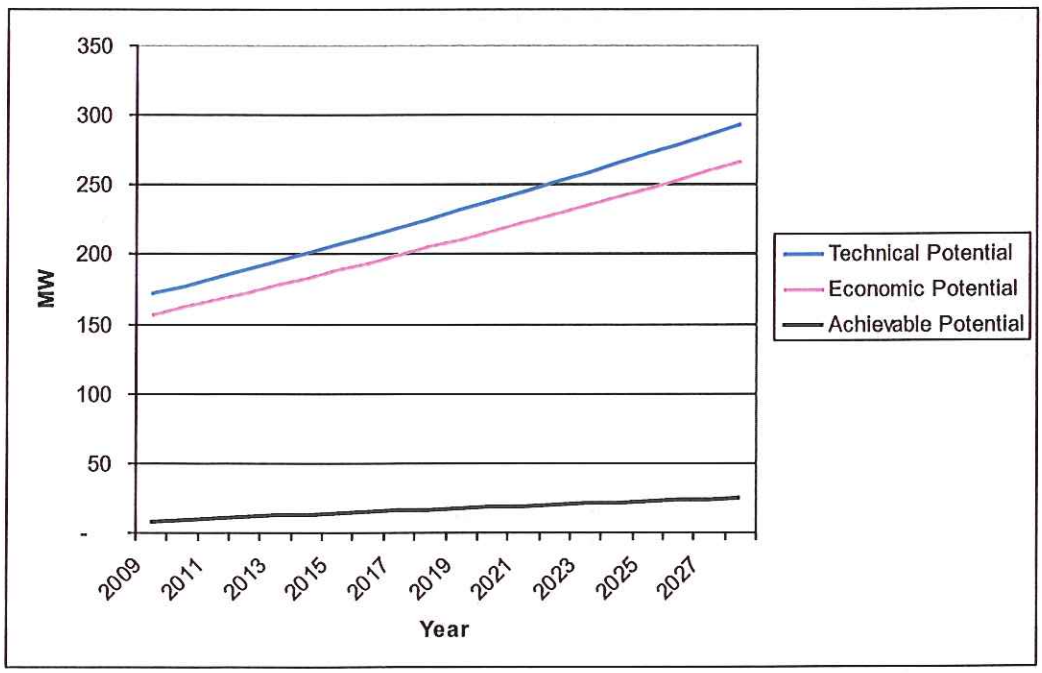

Figure 4.2 Commercial Demand Savings Forecast

5.1 SUMMARY OF INDUSTRIAL POTENTIAL

The industrial sector comprises a total of 17% of IPC's electricity sales and 15% of the total load. While the industrial sector includes a minimal number of customers, the energy intensive processes and high billed demand of each customer allow for a significant amount of DSM potential. At the forefront of electricity consumption is the food processing sector which consumes just over half of the industrial electricity sales. General manufacturing and the electronics industry make up an additional quarter of industrial sales, while the remainder of consumption goes to large commercial customers.

IPC has developed and implemented the Custom Efficiency program for the industrial sector. This program pays customers incentives proportional to the electricity savings from each project. Nexant believes that this type of program is effective in capturing the energy savings from industrial measures which are often to complex or variable to be streamlined into a prescriptive incentive program.

The industrial DSM achievable potential is highly dependant on customer adoption rates which vary directly with the utility incentive offering. Nexant has developed four (4) incentive scenarios to calculate the industrial achievable potential. The scenarios calculate the potential savings from offering a low, moderate, aggressive, or maximum incentive, which represent payment of 25%, 50%, 75%, and 100% of customer costs respectively. Industrial achievable potential energy savings in 2009 range from 33 GWh under a low incentive scenario to 57 GWh with the maximum incentive scenario. Figure 5.1 shows the four achievable potential scenarios relative to the technical and economic potentials calculated for the industrial sector.

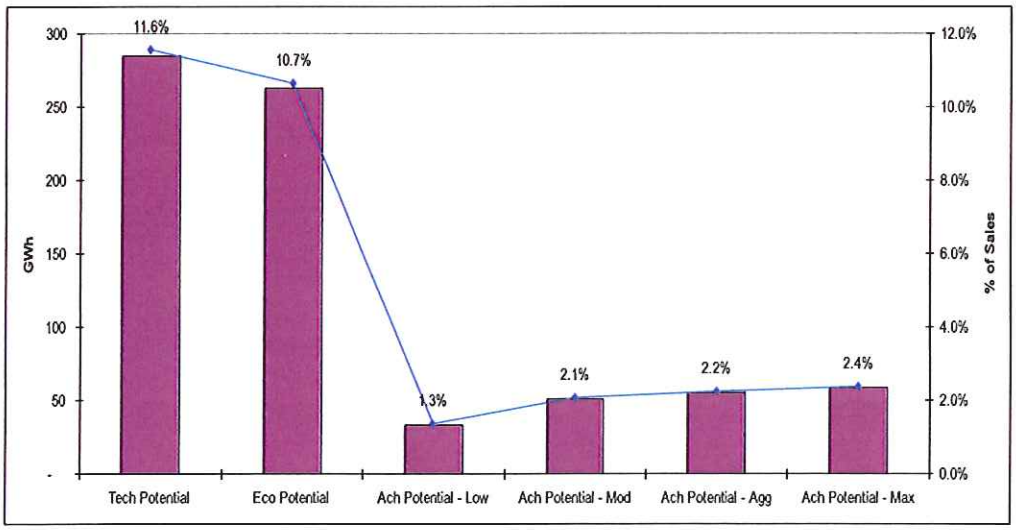

Figure 5.1 2009 Industrial Potential GWh Savings and Percent of Total Sales

The achievable peak demand savings available to IPC in the industrial sector are also calculated based on the incentive offering. Estimates for peak demand savings in 2009 range from 3.5 MW

CERTIFICATE OF SERVICE

I hereby certify that on this 4th day of March, 2011 I delivered true and correct copies of the foregoing TESTIMONY IN SUPPORT OF THE STIPULATION to the following persons via the method of service noted:

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