Agenda Date: September 27, 2012
Item Number: A2

Docket: UG-121119
Company: Avista Corporation

Staff: Eric Russell, Regulatory Analyst
EJ Keating, Regulatory Analyst

Recommendation

Take no action, thereby allowing the tariff revision filing made by Avista Corporation, in Docket UG-121119 to take effect October 1, 2012, by operation of law.

Background

On June 29, 2012, Avista Corporation (Avista or company) filed with the commission a request to revise Tariff WN U-29, which proposes revisions to Schedule 190, "Natural Gas Efficiency Programs." The purpose of the tariff revision is to temporarily discontinue the company's natural gas demand side (DSM) programs due to new natural gas avoided costs that have been released as part of Avista's Integrated Resource Plan (IRP) process.

As part of its annual DSM Business Planning process last fall, Avista identified the need to monitor natural gas avoided costs to optimize, and maintain the cost effectiveness of its natural gas DSM portfolio.[1] This optimization was further analyzed and discussed in a report entitled "Review of Prospects and Strategies for the 2012 Avista Regular Income Natural Gas DSM Portfolio," filed with the commission on February 29, 2012.[2]

The updated analysis was based on future natural gas avoided costs that were expected to be 25 percent lower than existing avoided costs. Further, this analysis concluded that a smaller portfolio of natural gas programs could and would be offered later in 2012. This changed, however, with the June 9, 2012, release of natural gas avoided costs that are now approximately 50 percent lower than the avoided costs from those in November 2011. Avista's natural gas IRP was released on August 31, 2012,[3] and confirmed these lower avoided costs.

Related filings include UG-120788, Avista's current natural gas DSM tariff rider, currently suspended with rates temporarily in effect, subject to revision, and UG-121416, natural gas decoupling rate adjustment, scheduled for the October 25, 2012, open meeting. Additionally, UG-060518, Avista's natural gas decoupling mechanism is tied to the natural gas DSM portfolio.

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[1] UE-111882, Annual DSM Business Plan, filed November 1, 2011.
[2] UE-111882.
[3] UG-111588 Natural Gas Integrated Resource Plan.

Discussion

Staff believes that one of the major determining factors for evaluating this proposed tariff revision is evaluating the cost effectiveness of the company's natural gas DSM portfolio, which is directly related to the avoided cost of gas. Other factors contributing to staff's recommendation include the slower evolution and more limited nature of natural gas DSM technologies, the absence of generation infrastructure, as well as the ability to store fuel, all of which make providing cost-effective natural gas DSM significantly more difficult than electric DSM.

The recent reduction in natural gas commodity prices is almost solely responsible for the approximate 50 percent decrease in the avoided cost of natural gas. Furthermore, the estimates show that a 91 percent increase (over the June 9, 2012 value) in avoided cost of gas is necessary for the programs to be cost effective. The estimated increased avoided cost would result in a TRC ratio of 1.0, as compiled by the company. The tests conducted by the company are discussed below.

Staff thoroughly reviewed Avista's cost effectiveness calculations including its attempts to construct a more cost-effective natural gas DSM portfolio under the reduced avoided costs. Even under multiple and varied calculation methodologies used in an attempt to retain its natural gas DSM programs, the company was unable to generate a Total Resource Cost (TRC) portfolio ratio greater than 0.70. This ratio is based on a net to gross ratio of 100 percent for all programs across the portfolio. A portfolio ratio of 1.0 or greater is the threshold at which programs are deemed to be cost effective.

Scenarios considered by the company included:

- The addition of a carbon cost adder for 2013-2019, above and beyond the carbon cost that is incorporated into the avoided cost itself for 2020 and beyond.
- The inclusion of a natural gas distribution capacity cost value.
- The use of an interpretation of the TRC test on a gross (including all program participants) rather than a net (based upon those participants who adopted the measure due to utility intervention) basis.
- Various alternative categorizations of net to gross ratios and realization rates by programs.
- Different means of allocating non-incentive utility costs across programs.

Staff agrees that the dramatic reduction in natural gas avoided costs prevents Avista's natural gas DSM portfolio from passing the TRC. Staff also looked at the company's evaluation of the portfolio under the Program Administrator Cost Test (PAC). However, evaluating programs under the PAC does not take into account the impact of the programs and measures on the ratepayer, but measures the benefits and costs to the utility. Staff's analysis shows the results of the PAC test resulted in a ratio of 0.99, which is slightly under the cost effectiveness threshold.

Similar to the TRC calculation, this ratio is based on a net to gross ratio of 100 percent for all programs in the portfolio.

Staff also looked at the possibility of keeping two programs (non-residential windows/insulation and non-residential heating and cooling), but these programs are small, are projected to be marginally cost effective, and would not be cost effective if the fixed natural gas DSM administrative expenses were borne only by these two programs rather than being spread over the larger portfolio of programs currently offered.

Further, staff anticipates that customer demand for natural gas DSM programs will decrease as retail gas prices fall and customer bills become more affordable. Expiring federal tax credits and rebates for energy efficiency offered through the American Reinvestment and Recovery Act of 2009 are also expected to decrease future participation because many customers purchased energy efficiency measures sooner than they would have without the federal incentives. Lower program participation reduces cost effectiveness by spreading fixed overhead expenses over fewer saved therms.

Suspending DSM programs during periods of reduced avoided costs may increase the expense of re-starting the program infrastructure in the future if or when natural gas avoided costs increase again. If reduced avoided costs were only expected in the short term, staff would consider recommending maintaining the programs if the increased expense of rebuilding them exceeded the cost savings of a temporary suspension. However, this does not appear to be the case. Industry forecasts indicate that the wholesale price of gas, which is closely tied to Avista's avoided cost, will remain low for the foreseeable future. Under these conditions, it is more beneficial to suspend a cost-ineffective portfolio until avoided costs substantially increase.

During similar circumstances in 1997, Avista received commission approval to suspend its natural gas DSM programs when avoided costs declined.[4] Avista successfully revived its gas programs four years later when gas prices rose dramatically.[5] Staff believes that since the company has experienced staff who work on both natural gas and electric DSM, this existing company infrastructure will allow the reinstatement of programs in a rapid fashion if and when the program can again be shown cost effective.

The following breakout represents Avista's plan and schedule to ramp down its natural gas DSM programs:

<u>Site Specific Programs</u>:
Avista will honor all terms and conditions of contracts and agreements that are fully executed prior to October 1, 2012. Natural gas energy efficiency projects, known to Avista prior to

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[4] UG-961310.
[5] UG-010029.

October 1, 2012, but without fully executed contracts, will be honored if Avista has already conducted an analysis of a proposed natural gas energy efficiency measure. If the company has not already conducted an analysis of a proposed natural gas energy efficiency measure, customers seeking incentive funding must have submitted an overview of the proposed natural gas energy efficiency project to the company in writing or via email by October 1, 2012. Projects must have material documentation by November 15, 2012 and an energy efficiency agreement must be signed by January 15, 2013.

Residential and Non-Residential Prescriptive Rebate Programs:
Qualifying customers in the company's Residential and Non-Residential Prescriptive Rebate Programs must send to Avista all required rebate forms and other required documentation postmarked by November 1, 2012, to be eligible for payment. Any requests postmarked after November 1, 2012, will be denied payment.

Limited Income Programs:
All existing 2012 Community Action Partnership contracts with natural gas incentives will be honored. No additional natural gas measures will be funded effective January 1, 2013.

At this time, there is an active rulemaking on natural gas conservation programs, under Docket UG-121207, opened on July 20, 2012. Interested parties were given an initial opportunity to file comments on August 31, 2012. All four natural gas providers regulated by the commission, as well as other parties, filed comments on or before that date. A second opportunity to file comments will close on October 5, 2012. A workshop will then be conducted on October 19, 2012. Two specific questions are being asked in that docket:

1. What are the appropriate assumptions or factors to include in natural gas avoided cost calculations?
2. Should companies use a combination of cost tests in evaluating the cost-effectiveness of natural gas conservation programs?

The outcome of this rulemaking docket may have ramifications on the way natural gas conservation programs are evaluated.

Avista has stated they will remain committed to a continual re-evaluation of the prospects for the natural gas DSM portfolio. Should natural gas costs, technologies or delivery methods change in such a manner to allow for cost-effective opportunities in the future, the company will move to return all or portions of the natural gas DSM portfolio to the company's overall energy efficiency strategy.

Staff recommends that Avista informally provide staff with quarterly updates to the avoided cost analysis to re-evaluate the ongoing cost effectiveness status of this portfolio. Should the avoided costs rise to the point where a TRC result above 1.0 is reached, then the company will file a tariff revision to reinstate their natural gas DSM programs.

Conclusion

Take no action, thereby allowing the tariff revision filing made by Avista Corporation, in Docket UG-121119 to take effect October 1, 2012, by operation of law.