

BEFORE THE CORPORATION COMMISSION OF OKLAHOMA

IN THE MATTER OF THE APPLICATION)
OF PUBLIC UTILITY DIVISION SEEKING)
DETERMINATION OF THE CALCULATION)
OF LOST NET REVENUES AND SHARED)
SAVINGS PURSUANT TO THE DEMAND)
PROGRAM RIDER OF OKLAHOMA GAS)
AND ELECTRIC COMPANY)

CAUSE NO. PUD 201500153

FILED
JUN 02 2015

COURT CLERK'S OFFICE - OKC
CORPORATION COMMISSION
OF OKLAHOMA

REBUTTAL TESTIMONY

OF

EDWIN C. FARRAR

ON BEHALF OF

OKLAHOMA ATTORNEY GENERAL

June 2, 2015

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INTRODUCTION

1

2 **Q: Please state your name.**

3 A: My name is Edwin Farrar.

4 **Q: By whom are you employed and what is your business address?**

5 A: I am employed by the Office of the Attorney General of Oklahoma. My business address
6 is 313 NE 21st Street, Room 3073, Oklahoma City, Oklahoma 73105.

7 **Q: What is your educational and professional background?**

8 A: I graduated from Cameron University with a Bachelor of Science degree in Business
9 Administration. I am also a Certified Public Accountant in the State of Oklahoma. I am
10 a member of the American Institute of Certified Public Accountants and the Oklahoma
11 Society of Certified Accountants. I was employed by the Public Utility Division of the
12 Corporation Commission from April 1985 through December 31, 2006 in various analyst
13 and audit positions. From January 2007 until May 2011 I worked as an independent
14 consultant on utility rate cases. I began employment with the Office of the Attorney
15 General in May of 2011 as an auditor in the Public Utility Unit.

16 **Q: Have you testified before this Commission before and have your credentials been**
17 **accepted?**

18 A: Yes. I have previously testified before this Commission and my credentials have been
19 accepted.

1 **PURPOSE**

2 **Q: What is the purpose of your testimony in PUD Cause No. 201200134, in the matter**
3 **of the application of Public Utility Division (“PUD”) or (“Staff”) seeking**
4 **determination of the calculation of lost net revenues and shared savings pursuant to**
5 **the demand program rider of Oklahoma Gas and Electric Company’s (“OG&E”) or**
6 **(“Company”)?**

7 **A:** I am providing testimony to discuss the definition of Lost Net Revenue (“LNR”) in the
8 Commission’s rules and the prospective changes to that definition. I will also discuss the
9 need to interpret OG&E’s Smart Hours tariff under the rules existing at the time the order
10 was issued in CN PUD 201200134. I will also recommend that the Commission support
11 OG&E’s very effective Smart Hours demand side management program by recognizing
12 that the intent of the stipulation and order approving the program was for the recovery of
13 all net revenues forgone by the Company through the implementation of the program.

14 **STAFF’S APPLICATION**

15 **Q: Have you reviewed PUD’s request for a determination of the calculation of LNR**
16 **and shared savings and its recommendation that LNR be limited under a strict**
17 **interpretation of the tariff?**

18 **A:** Yes, I have. Staff witness Kathy Champion pre-filed direct testimony contending that
19 OG&E was over recovering LNR related to its Smart Hours tariff under their Demand
20 Program Rider (“DPR”) tariff. Ms. Champion is recommending that the LNR under the
21 DPR tariff be narrowly interpreted to include only revenue lost from reduced kWh sales

1 and that it exclude revenue lost from the lower rates offered under the Smart Hours
2 tariff.^{1,2} Ms. Champion further recommends that limiting the LNR calculation to only the
3 residential class of customers is inappropriate because it fails to consider possible
4 increases in sales to other classes of customers.³

5 **Q: Does OG&E agree with Ms. Champion's discussion and recommendations?**

6 A: No. OG&E pre-filed responsive testimony disagreeing with Ms. Champion's
7 recommendations. OG&E argued that the Company properly calculated the LNR as
8 allowed by the order setting the DPR tariff and under the conventional definition used in
9 Cause Number PUD 201200134, the Commission definition of LNR, and industry best
10 practices.⁴ Simply put, OG&E recognizes LNR as revenue lost by the Smart Hours
11 program as a whole, while Staff believes that only the revenues lost within the Smart
12 Hours tariff itself should be recovered from DPR tariff revenue.

13 **Q: How is LNR from the Smart Hours program different from the LNR from the**
14 **operation of the Smart Hours tariff?**

15 A: The LNR from the Smart Hours program includes the difference between the revenue
16 that would have been received under the original residential tariff and the revenue that
17 was received under the Smart Hours tariff. It consists of the difference in consumption
18 and the difference in pricing under the two tariffs. The LNR that Staff identified from the
19 operation of the Smart Hours tariff is the reduction in consumption that is priced at the

¹ Direct testimony of Kathy Champion, page 6, lines 15-18.

² Direct testimony of Kathy Champion, page 10, line 16 through page 11, line 1.

³ Direct testimony of Kathy Champion, page 12, lines 17-20.

⁴ Direct testimony of Donald R. Rowlett, page 9, lines 6-8.

1 Embedded Fixed Cost (“EFC”) rate.⁵ This is consistent with the testimony of Philip R.
2 Bartholomew in OG&E’s most recent DPR case where describes the calculation of the
3 net lost revenue related to avoided energy sales.⁶ The revenues lost from the
4 implementation of the Smart Hours tariff compared to the standard residential tariff were
5 not addressed in the testimony filed in that case.

6 **Q: Why was the revenue lost from the pricing difference between the Smart Hours**
7 **tariff and the standard residential tariff not addressed in the DPR case?**

8 A: In my opinion it was not addressed then because the Smart Hours program is an
9 innovative program that uses pricing as a major tool to attract participants and it was
10 highly successful because OG&E heavily promoted it. We simply did not have
11 experience with this type of program and the impact that the pricing aspect would have.
12 The Company has offered load shifting programs for industrial customers in the past in
13 conjunction with rate cases where the revenue recovery could be addressed. When the
14 DPR case was filed three years ago no one anticipated the success that OG&E would
15 have with the Smart Hours program. However, we did know that LNR would result from
16 the program and did make a provision in the settlement for the recovery of 100% of the
17 lost net revenue.⁷

18 **LOST NET REVENUES DEFINED**

19 **Q: How is LNR defined in the Commission’s demand program rules?**

⁵ Direct testimony of Kathy Champion, page 7, lines 14-16.

⁶ See the direct testimony of Philip R. Bartholomew in CN PUD 201200134, page 4, lines 3–22.

⁷ Joint Stipulation and Settlement Agreement, Cause No. PUD 201200134, page 2, III. at 3.

1 A: The Commission's rules at OAC 165:35-41-3 define lost net revenue as:

2 "Lost net revenue" means income from the retail sale of electricity forgone by a
3 utility directly resulting from the success of its demand portfolio, less expenses
4 the utility was not required to pay by forgoing the sales.

5 Lost net revenues were not otherwise defined in the joint stipulation and settlement
6 agreement in CN PUD 201200134 or in the resulting DPR tariff. The reading of the
7 definition in the rule currently in effect clearly supports the recovery of net revenue lost
8 from both the implementation of the Smart Hours tariff and the reduction of energy sales.

9 **APPROPRIATE REGULATORY POLICY**

10 **Q: What are the appropriate recovery provisions for LNR?**

11 A: Generally, a utility should be made whole for all net revenue lost through the
12 implementation of a demand response or conservation program. A utility's officers have
13 a duty to provide a reasonable level of earnings for shareholders by fulfilling the
14 company's public responsibilities. This means that demand and efficiency programs
15 have to be as profitable as investments in utility assets for them to be most effective on a
16 long-term basis. That is because a failure to allow a utility to recover all of the earnings
17 lost from those programs would force the utility to limit its offerings to less detrimental
18 programs. In OG&E's case they have developed a very effective demand reduction
19 program and have achieved an outstanding participation rate through a very aggressive
20 pricing and marketing program. Critical to the success of the Smart Hours program are
21 the savings realized by participating customers from the reduced tariff rates in all years
22 and not just years when we have record breaking heat. OG&E did experience lost

1 revenue from the implementation of the tariff and it is reasonable that they should be
2 allowed to recover those lost revenues to ensure the sustainable success of the program.

3 **Q: What has been Staff's past position on the recovery of lost revenue from demand**
4 **and efficiency programs?**

5 A: Staff has supported the recovery of lost revenue in the past. In CN PUD 200900200
6 David W. Smith testified:

7 "Despite the issues mentioned above, utilities cover a portion of fixed cost
8 through volumetric rates priced per kilowatt-hour (kWh) that are related to sales
9 volumes. Any gains in energy efficiency savings would lower sales, but fixed
10 costs remain. Uncompensated, this would detract the utility from investments in
11 energy efficiency programs. If revenues drop, then an impact on earnings could
12 hinder the financial performance of the utility. For these reasons, it is Staff's
13 opinion that lost revenue recovery for this cause is an important element for
14 financial health of the utility. A lack of revenue recovery would dissuade the
15 utility from investing in energy efficiency."⁸

16 **Q: Did you provide testimony in OG&E's recent DPR case that addressed the issue of**
17 **LNR?**

18 A: I did pre-file responsive testimony in CN PUD 201200134 that supported OG&E's
19 demand programs but I did not specifically address the definition of LNR. I assumed
20 then and continue to assume that it included all revenue lost from the implementation of
21 the program consistent with the definition of income forgone by the utility.

22 **Q: What would likely be the impact of limiting OG&E's LNR to the reduced sales**
23 **under the Smart Hours tariff?**

⁸ CN PUD 200900200, the direct testimony of David W Smith, page 23, lines 10-19.

1 A: OG&E would be reluctant to promote this type of program going forward. It would also
2 discourage other utilities from adopting product pricing as a demand response tool
3 because their earnings would be at risk.

4 **THE FUTURE OF DEMAND RESPONSE IN OKLAHOMA**

5 **Q: Are there any recent developments that could impact OG&E's demand response**
6 **programs in the future?**

7 A: Yes. The definition of LNR has been changed effective January 1, 2016. The new
8 definition reads:

9 "Lost net revenue" means income from the retail sale of electricity forgone by a
10 utility directly resulting from the success of its demand portfolio, less expenses
11 the utility was not required to pay by forgoing the sales. Lost net revenue shall be
12 calculated using verified savings, shall exclude customer service charge revenues
13 (non-volumetric revenues), and shall exclude revenues collected from riders with
14 annual true-ups.

15 The Commission also modified the definition of inducement to read:

16 "Inducement" means anything of value offered by a utility to encourage an
17 electricity user or trade ally to engage in Demand Programs approved pursuant to
18 this subchapter. While inducements can include a variety of costs, direct
19 payments to customers or trade allies on behalf of customers shall make up the
20 majority of total inducement costs.

21 The Commission should expressly state in their order that the utility is to recover the
22 revenue lost as a result of tariff pricing differences from customer participation in the
23 programs in addition to the volumetric revenue lost from customer load reduction efforts,
24 whether they are identified as lost net revenue or inducements.

1 **Q: Do you have any additional concerns regarding the future effectiveness of the Smart**
2 **Hours program?**

3 A: Yes. OG&E will be filing a rate case in the near future. At that time the OG&E's rates
4 will be designed to recover all of its costs so that the lost net revenue will be eliminated
5 from the DPR rider. If OG&E reduced its promotion of the program in future years it
6 would realize increased earnings unless differences in earnings from the Smart Hours
7 program participation rate is tracked and the lost or gained revenue recovered or credited
8 in the DPR.

9 **RECOMMENDATIONS**

10 **Q: What is your recommendation to the Commission regarding the calculation of net**
11 **lost revenue to be recovered under the DPR tariff?**

12 A: I recommend that OG&E be allowed to recover all net revenue lost from the
13 implementation of the Smart Hours program. If the Commission finds that the tariff
14 should be strictly followed I recommend that the Commission order OG&E to file an
15 amended tariff that clearly states that all net revenue lost from the implementation of the
16 Smart Hours program is to be recovered.

17 **OTHER ISSUES**

18 **Q: Does your testimony address all issues in this Cause?**

1 A: No, it does not. I will review issues raised by other parties to this Cause and reserve the
2 right to address those issues in supplemental testimony.

3 **CONCLUSION**

4 **Q: Does this conclude your testimony?**

5 A: Yes, it does.

CERTIFICATE OF SERVICE

On this 2nd day of June, 2015, a true and correct copy of the above and foregoing *Rebuttal Testimony of Edwin C. Farrar on Behalf of the Oklahoma Attorney General*, was sent via electronic mail to the following interested parties:

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