

BEFORE THE CORPORATION COMMISSION OF OKLAHOMA

COURT CLERK'S OFFICE - OKC
CORPORATION COMMISSION
OF OKLAHOMA

IN THE MATTER OF THE APPLICATION OF)
BRANDY L. WREATH, DIRECTOR OF THE)
PUBLIC UTILITY DIVISION, FOR)
DETERMINATION OF THE CALCULATION) CAUSE NO. PUD 201500153
OF LOST NET REVENUES AND SHARED)
SAVINGS PURSUANT TO THE DEMAND)
PROGRAM RIDER OF OKLAHOMA GAS)
AND ELECTRIC COMPANY)

**OKLAHOMA GAS AND ELECTRIC COMPANY'S EXCEPTIONS
TO THE REPORT AND RECOMMENDATIONS
OF THE ADMINISTRATIVE LAW JUDGE**

COMES NOW Oklahoma Gas and Electric Company ("OG&E") pursuant to OAC 165:5-13- 5(a)(2) and files these Exceptions to the Report of the Administrative Law Judge ("ALJ Report" or "Report") issued in this Cause on March 28, 2016. OG&E takes exception to the portions of the ALJ Report as described below.

STANDARD OF REVIEW

The recommendations from an administrative law judge are advisory and that the Oklahoma Corporation Commission ("OCC" or "Commission") must reach its own independent decision on matters before it based upon the evidence. *Smith Cogeneration Mgmt., Inc. v. Corp. Comm'n*, 1993 OK 147; *Cameron v. Corp. Comm'n*, 1966 OK 75, ¶29; *State ex rel. Cartwright v. Okla. Natural Gas*, 1982 OK 11,

The Oklahoma Supreme Court affords no special weight to a report, but rather reviews matters solely based upon the order of the Commission. *Cameron v. Corp. Comm'n*, 1966 OK 75. The Commission acts as the final arbiter and, therefore, is free to "accept or reject any or all of the recommendations of the examining officer, or add to them." *State ex rel. Cartwright v. Okla. Natural Gas*, 1982 OK 11. In addition, when carrying out its duties, the Commission must abide by legal and equitable principles that result in determinations that are fair and reasonable to both the public and the utility. *Cnty. Natural Gas v. Corp. Comm'n*, 1938 OK 51.

I. INTRODUCTION

The primary issue raised by OG&E's Exceptions to the ALJ Report is the appropriate

method of compensating the Company for lost revenues caused by the implementation of the SmartHours program in calendar years 2013 to 2015. No one questions the fact that when the utility implements a new demand program, the revenue it would otherwise receive under previously approved tariffs is impacted. The Commission's decision in this Cause as to how the Company is appropriately compensated for a revenue loss related to demand programs implemented between general rate reviews is central to the success of residential and small business demand response programs, past, present and future.

The SmartHours program has its genesis in a decision by this Commission in February, 2008 that it was in the best interest of OG&E's customers for the Company to promote and implement effective energy efficiency programs. Subsequently, the Commission's decision to support OG&E's early deployment of Smart Grid technology opened the door for the expansion of that concept for demand response programs, including in particular the SmartHours program.

The success of the SmartHours program is uncontroverted. The sign-up rate for OG&E customers and the peak demand reductions resulting from the program have made OG&E and Oklahoma a national leader in demand response programs. In fact, OG&E's approach has become a national role model for how to reduce customer costs by encouraging highly effective customer actions. An unprecedented percent of OG&E's eligible customers (more than 110,000 customers) have voluntarily opted to participate in the Smart Hours program, benefiting both participating and non-participating customers and producing high customer satisfaction ratings. The 150 MW of peak load reduction resulting from the program has saved all OG&E customers the cost of building or buying that amount of expensive capacity. In addition, participants are experiencing and can continue to experience more than \$16 million annually in lower costs. And OG&E continues to experience high residential customer satisfaction results from JD Powers surveys.

Unfortunately, the recommendations of the ALJ in this cause threaten to unravel the regulatory agreement which included a commitment to fairly compensate the Company for its efforts to promote, implement and sustain demand programs, a commitment which is consistent with the goals established by the Commission in 2008 and confirmed when the Commission promulgated Demand Program rules in 2009.

If sustained, the ALJ recommendations would deprive OG&E of a significant portion of the appropriate compensation earned as a result of the phenomenally successful SmartHours

program. As importantly, the general compensation policy recommended by the Commission Staff witness and implicitly endorsed by the ALJ recommendations is contrary to best practices and, if adopted by this commission, would discourage, and potentially eliminate, the creation of additional innovative customer choice programs.

BACKGROUND

This Cause involves OG&E's 2013-2015 Demand Program Portfolio approved by the Commission in Cause No. PUD 201200134, Order No. 605737 (2013 DPR Case). OG&E's 2013-2015 Portfolio is the successor of the 2008 Quick start Demand Program and the 2010-2012 Portfolio. In the 2013 DPR Case, the Commission approved a Settlement Agreement which modified the energy efficiency portfolio that had been OG&E's focus since 2008 and, for the first time, the Company added demand response programs, including the SmartHours program (Rowlett Resp., 4:9-15). The appropriate compensation for the SmartHours program is the primary concern addressed by these Exceptions.

The purpose of energy efficiency programs in general is to reduce customer electricity consumption and the purpose of demand response programs is to reduce customer demand for electricity for specified periods of time¹. Both types of programs are intended to save participating and non-participating customers money by moderating the cost of generation and the need for future generation capacity. Witnesses for PUD, the Attorney General and the Company all appear to agree that the programs, and in particular the OG&E's SmartHours program, have been successful in achieving those goals.

The 2013 Commission Order also approved the Demand Program Rider (DPR tariff) as the cost recovery mechanism for OG&E. The DPR involves three distinct categories of cost recovery: (1) costs expended by OG&E to promote and administer the specific programs, (2) "shared savings", which serve as incentives for OG&E to aggressively promote the programs and (3) "lost net revenues," which compensate the Company for the loss of revenue authorized by the Commission when rates were set in the most recent OG&E rate case.

During 2013, the Company collected revenues for the estimated SmartHours program costs² based on the expected enroll of new customers in the SmartHours program in 2013. The

¹ OAC 165:35-41-3 Definitions

² ID

DPR tariff also provides for an annual review of the previous year activities and a determination the DPR cost recovery rates to be applied prospectively. The prospective DPR rates, applied in 2014, are to reflect (i) the recovery of actual DPR program costs which includes incentives provided to customers, (ii) the actual prior period lost net revenues and earned shared savings based on the effectiveness of the program, and (iii) a true-up of any over or under revenue collections .

On February 27, 2014, OG&E submitted to PUD the Company's calculation of the costs from the Demand Programs utilized by customers in 2013 and a request that the DPR tariff factor for 2014 be adjusted so OG&E could receive lost net revenue, shared savings and the under-recovered balance for program costs from 2013.

Following the Company's submission in February of 2014, PUD raised concerns with some of the cost recovery components of the DPR Tariff. PUD did not challenge the program costs submitted by the Company, but did express disagreement with the Company's lost net revenue calculation for SmartHours during the 2013 period, as well as shared savings and lost net revenue calculations for energy efficiency programs.

The Company and PUD engaged in discussions regarding Staff's concerns for nearly a year and in January, 2015, the Company voluntarily modified its proposed DPR cost recovery for the 2014 period. The modification was an attempt to address one area of PUD's concern by limiting lost net revenues for the SmartHours program in 2013 and 2014 to customer activity in the period from June to October for each year. The Company originally calculated the SmartHours lost net revenues in 2013 to be \$11.2 million; the modification reduced that amount by \$1.1 million.

The Company and PUD continued discussions but were unable to come to agreement and on April 14, 2015, PUD filed its Application requesting that the Commission issue an order determining the proper calculation methodology for lost net revenues pursuant to the DPR. PUD proposed the Company recover \$4.9 million in lost net revenue for the SmartHours program in 2013.

To the extent the recommendations of the ALJ support PUD's interpretation of the methodology for calculating lost net revenues for the SmartHours program they are contrary to the Commission Rules, the Settlement Agreement approved by the Commission in Order No. 605737, the appropriate reading of the DPR tariff and industry best practices. Consequently, the

Commission should find that as related to the SmartHours program, OG&E will be allowed to recover \$11.2 million in lost net revenues for calendar year 2013 and the lost net revenues derived from applying the same methodology for subsequent calendar years.

The ALJ's recommendations rejecting OG&E's calculation of the lost net revenues experienced as a result of the SmartHours program is contrary to Commission Demand Programs rules.

The definition of lost net revenues reflected in the Commission rules has not changed since the inception of the Demand Program rules in 2009. OCC 165:35-41-3 provides that

“**lost net revenue**” means income from the retail sale of electricity foregone by the utility directly resulting from the success of its demand portfolio, less expenses the utility was not required to pay foregoing the sales.”

However, the ALJ Report incorrectly states “... lost net revenue is determined by identifying the total energy and demand savings and multiplying those savings by the embedded fixed cost factor. OG&E's claim of all revenue difference as lost net revenues overstates the lost net revenue.”³ This statement is inconsistent with the clear definition of lost net revenue in the Commission rules. And ignores the fact that in order for the SmartHours program to be successful customers must migrate from standard rates to the time-of-use SmartHours rates.

The success of an energy efficiency program is easily measured by determining the number of kwh saved as a consequence of the efficiency program and multiplying that number by the appropriate retail rate. However, demand response programs measure their success not by how many kwh they save, but by how much they reduce the demand for electricity in a targeted period of time. This distinction became critical when the Commission authorized OG&E to add the SmartHours program to its Demand Portfolio in 2013.

The SmartHours program targets on-peak consumption by customers who currently pay a flat rate (or standard tariff), no matter when they use electricity. These customers are enrolled and put on a two part time of use rate. This new rate consists of lower than standard tariff off peak rates which are applicable to electricity used from 7 pm to 2 pm. The second part of the rate charges varying prices for the use of electricity during on-peak period from 2 pm to 7 pm. In addition,

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customers are provided consumer education and free programmable thermostats as aids to maximizing their savings under the program.

The SmartHours program is a success to the extent the participants reduce their on peak usage, but a very important consequence of that success is that they generally move their on peak consumption to the lower cost off peak periods, and may even increase their consumption of off peak energy by an amount greater than the on peak reduction.

Consequently, the revenue forgone by the Company directly resulting from the success of the SmartHours program has two components (i) the number of kwh saved as a consequence of lower on peak consumption multiplied by the standard tariff rate, off-set by the excess revenue received from the kwh sold at the on peak rate and (ii) the difference between the standard rate and the lower off peak rate for all kwh sold off peak.

By contrast, the approach proposed by PUD ignores the second component of the calculation, apparently because staff assumes that the more than 110,000 OG&E customers would have migrated to the SmartHours program without the Company's Demand Program efforts. PUD's calculation only accounts for the change in energy from SmartHours customers' on peak consumption and omits the revenue impact of the change to a lower, SmartHours rate. This approach ignores the fact that lower off peak rates incent customers to delay activities during the on-peak period to off peak hours. The lost revenues associated with the lower off peak rates account for more than half of OG&E's "income" that is "forgone" as a result of the SmartHours success.

The definition of "lost net revenues" advocated by the PUD and apparently supported by the ALJ's recommendations is contrary to the clear reading of the Commission rules and the practical understanding customer motivation which drive the success of the SmartHours program. In contrast, the Company's method for calculating "lost net revenues" for the SmartHours program is consistent with the Commission rules and should be adopted.

The ALJ's recommendations rejecting OG&E's calculation of the lost net revenues experienced as a result of the SmartHours program is contrary to the Settlement Agreement approved by the Commission in Order No. 605737

Section III, Paragraph 3 of the Settlement Agreement which the Commission adopted in the 2013 DPR case provides that "OG&E shall recover 100% of the lost net revenues resulting

from the success of the programs in OG&E's Demand Portfolio," a portfolio which includes the SmartHours program.

The only facts in the record for the 2013 DPR Case addressing the methodology for calculating lost net revenue for the SmartHours program were presented by OG&E witness Philip Bartholomew. Mr. Bartholomew attached the Company's proposed DPR tariff to his testimony and included a detailed calculation of the lost net revenue recovery OG&E estimated to occur based on the expected enrollment of residential customers in 2013, 2014 and 2015.

As it relates to the calculation of lost net revenues, **the DPR tariff attached to Settlement Agreement and which was ultimately authorized by the Commission is the exact tariff proposed by OG&E and sponsored by Mr. Bartholomew.** No party proposed alternative tariff language or suggested at any time an alternative methodology for calculating lost net revenues.

Similarly, no party filed testimony or otherwise disputed Mr. Bartholomew's explanation of the revenue estimates he provided. In particular, there is no evidence in the record of the 2013 DPR case suggesting PUD proposed a calculation methodology or challenged the calculation methodology presented by OG&E. In fact, Mr. Bartholomew testifies that he met with staff witness, Nicholas Fiegel, prior to the execution of the Settlement Agreement and explained the Company's methodology and revenue estimates in great detail. That testimony is unchallenged.

In addition, when the estimates provided by Mr. Bartholomew in the 2013 DPR case are modified to reflect the actual customer enrollment, actual customer behavior, and actual weather in 2013, the results are consistent with the \$11.2 million in lost net revenue requested by the Company⁴.

Finally, it should be noted that prior to the meeting with Mr. Bartholomew, Mr. Fiegel filed Responsive Testimony recommending total disallowance of lost net revenue. However, the basis for that recommendation was Mr. Fiegel's contention that any SmartHours program cost recovery was more appropriately addressed in a future "Phase III" filing by modifying OG&E's 2010 Smart Grid filing. PUD subsequently testified in support of the Settlement Agreement which included the Company's proposed tariff language regarding calculation of the lost net revenues component⁵.

⁴ Bartholomew Responsive Testimony pages 7 - 9

⁵ Seanz Testimony supporting Settlement Agreement
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Additionally, in his testimony supporting the Stipulation Agreement, PUD Witness Luis Saenz addressed the major provisions of the stipulation. He stated that OG&E is allowed to recover 100% of the lost net revenues and cited OAC 165:35-41-4. Rule 41-4 requires the Company to meet many requirements including a requirement for a detailed explanation of the utility's request for recoupment of lost net revenue. The required detail explanation of the SmartHours lost net revenues calculation was covered in the Company's application and supported by the testimony of Witness Bartholomew.

While conceding all these facts, the ALJ dismissed the information provided by the company **prior to the execution of the Settlement Agreement** and overlooked PUD's failure to express any disagreement with the lost net revenue calculation methodology provided by the company. Instead, the ALJ incorrectly found "OG&E's claim that PUD acquiesced or agreed to OG&E's calculation by not voicing objection is refuted by paragraph 4's requirement that approval or acquiescence in an any methodology be specifically provided in this Joint Stipulation"⁶

The ALJ's statement ignores the fact that the tariff ultimately approved by Commission was fully vetted with the parties to the Settlement Agreement. Taken to its logical conclusion, the ALJ Report supports a process in which one party, by being silent, may knowingly allow other parties to agree to a tariff interpretation which that party intends to challenge. Such an approach is detrimental to the process and inconsistent with the expectations of this Commission.

The ALJ's recommendations rejecting OG&E's calculation of the lost net revenues experienced as a result of the SmartHours program is contrary to the best reading of the DPR tariff

The ALJ characterizes the methodology advocated by PUD staff as a "literal" reading of the DPR tariff language and characterizes the calculation methodology utilized by OG&E as a "liberal" reading of the same language. The characterizations are based on an erroneous assumption.

The ALJ Report states, "PUD's interpretation gives literal and proper effect to the tariff language and applies the EFC factor as developed using the embedded costs for the customer classes from the most recent embedded cost of service study."⁷ This statement is incorrect. PUD

⁶ ALJ Report page 21

⁷ ALJ Report, Page 8 First Paragraph
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relies on existing tariffs as a proxy for embedded fix costs. The ALJ further characterizes OG&E's interpretation as, "OG&E has applied a liberal interpretation of the EFC that uses rates instead of the embedded fixed costs."⁸ What the ALJ apparently fails to understand is that PUD follows a similar process for developing their proxy for embedded costs. The difference between the two approaches is that OG&E calculates an EFC for each time-of-use period and rate. PUD omits the impact of time-of-use periods when determining their EFC calculation

More importantly, the recommendations of the ALJ appear to hinge on the incorrect assumption regarding treatment of embedded costs and an assumption that when a choice is to be made between two possible interpretations, the so-called literal interpretation should prevail. In fact, as already demonstrated, the interpretation followed by the company is consistent with the Commission's rules and consistent with the tariff application the parties adopted in the Settle Agreement approved by this Commission. As such, it is the Company's interpretation which should prevail.

The ALJ's recommendations rejecting OG&E's calculation of the lost net revenues experienced as a result of the SmartHours program is contrary to best practices in the industry

The ALJ appears to give little credence to industry best practices. Specifically, the ALJ appears to give no weight to the fact that the Company's calculation methodology is also consistent with industry best practices, specifically the California Public Utilities Commission Demand Response Protocols and the Synapse-RAP Report, *A Framework for Evaluating the Cost-Effectiveness of Demand Response*, which were relied upon by both Dr. Faruqui and the Company. Dr. Faruqui testified that OG&E's methodology is consistent with the accepted industry practice on how to calculate lost net revenue for a demand response program such as SmartHours⁹. Dr. Faruqui noted that there are no other documents that lay out how lost net revenues should be computed other than these cost effectiveness documents¹⁰ and stated that the

⁸ ALJ Report, Page 8 Second Paragraph

⁹ Faruqui Resp., 7:1-5

¹⁰ Tr. 6/30/2015 III 19:20-24

methodology used by the Company matches the approach endorse by the Synapse-RAP Report¹¹ regarding how to compute lost net revenue¹².

Dr. Faruqui, a well-known expert in the field of demand side management programs, testified that “calculations of the LNR for the SmartHours program should account for both the change in load shape and change in rates as customers switch from the standard tariff to the SmartHours program.¹³” According to Dr. Faruqui, the lost net revenue calculation for the SmartHours program has two elements. He explains the formula as Part A and Part B. Part A consists of net revenue losses that arise when customers switch from the standard rate to the SmartHours rate prior to making any changes in their load shapes. Part B consists of net revenue losses that arise when customers change their load shape in response to the incentives provided by the SmartHours rate by either curtailing their usage during their peak periods or by shifting it to the off-peak period. (Faruqui Resp., 6:21-29). Dr. Faruqui also states that it is important that the calculation be done for the year as a whole and not just for the summer months (Faruqui Resp., 9:10-11).

In the ALJ Report, the ALJ ignored the best practices recommendations as reflected in California Public Utilities Commission Demand Response Protocols, the Synapse-RAP Report and recommendations by Dr. Faruqui. Instead the ALJ adopted an approach which is contrary to those best practices recommendations.

Respectfully Submitted,

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¹¹ Hearing Exhibit 4, e-mail Dr. Tim Woolf, May 20, 2015 10:05 am

¹² Tr. 6/30/15, and 28:25-29:1-2

¹³ Tr. 6/30/2015 III 16:16-19

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CERTIFICATE OF MAILING

This is to certify that on the 11th day of April 2016 a true and correct copy of the above and foregoing was electronically transmitted to the following:


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