BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc. for Approval, Pursuant to Revised Code Section 4929.11, of a Tariff to Recover Conservation Expenses and Decoupling Revenues Pursuant to Automatic Adjustment Mechanisms and for Such Accounting Authority as May Be Required to Defer Such Expenses and Revenues for Future Recovery Through Such Adjustment Mechanisms.	)	Case No. 05-1444-GA-UNC

SUPPLEMENTAL OPINION AND ORDER

The Commission, considering the above-entitled applications, hereby issues its opinion and order in this matter.

APPEARANCES:

McNees, Wallace & Nurick, LLC, by Samuel C. Randazzo, Gretchen J. Hummel, Lisa Gatchell-McAlister and Daniel J. Neilsen, 21 East State Street, 17th Floor, Columbus, Ohio 43215-4228, on behalf of Vectren Energy Delivery of Ohio, Inc.

Marc Dann, Attorney General of the state of Ohio, by Duane W. Luckey, Chief, Public Utilities Section, by Anne L. Hammerstein and John H. Jones, Assistant Attorneys General, 180 East Broad Street, Columbus, Ohio 43215, on behalf of the staff of the Public Utilities Commission of Ohio.

Janine L. Migden-Ostrander, Ohio Consumers' Counsel, by Maureen R. Grady and Jacqueline L. Roberts, Assistant Consumers' Counsel, 10 West Broad Street, Columbus, Ohio 43215, on behalf of residential utility consumers of Vectren Energy Delivery of Ohio, Inc.

David C. Rinebolt, 231 West Lima Street, P.O. Box 1793, Findlay, Ohio 45839-1793, on behalf of Ohio Partners for Affordable Energy.

Joseph P. Meissner, Legal Aid Society of Cleveland, 1223 West 6th Street, Cleveland, Ohio 44113, on behalf of Consumers for Fair Utility Rates and the Neighborhood Environmental Coalition.

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OPINION:

I. History of this Proceeding:

The applicant, Vectren Energy Delivery of Ohio, Inc. (VEDO, applicant, or company), is a natural gas company as defined by Section 4905.03(A)(6), Revised Code, and a public utility as defined by Section 4905.02, Revised Code. On November 28, 2005, VEDO filed its application (Conservation Application) seeking authority to: (1) recover certain expenses associated with proposed conservation programs; (2) establish a mechanism to reconcile, in part, base rate revenue actually collected by VEDO with the base rate revenue authorized by the Commission in the company's last rate proceeding, Case No. 04-571-GA-AIR; (3) employ such accounting as may be required to defer certain conservation program expenses for amortization in a subsequent rate proceeding; and (4) employ such accounting as may be necessary to implement the conservation program expense recovery mechanism and the base rate revenue reconciliation mechanism. VEDO cited Section 4929.11, Revised Code, as empowering the Commission to approve the Conservation Application and asked the Commission to expedite its response.

By entry dated January 30, 2006, motions to intervene by Ohio Consumers' Counsel (OCC) and Ohio Partners for Affordable Energy (OPAE) were granted and a motion to practice *pro hac vice* for David Rinebolt was granted. By entry dated March 16, 2006, Consumers for Fair Utility Rates and the Neighborhood Environmental Coalition (Coalition) were also granted intervention. On December 21, 2005, VEDO conducted a noticed technical conference to explain and answer questions about its Conservation Application. VEDO also conducted a public presentation at the Commission meeting on February 1, 2006.

In the entry issued January 30, 2006, the attorney examiner found that expedited consideration of the Conservation Application was not appropriate and by entry dated February 7, 2006 directed that the Conservation Application be considered a request for an alternate rate plan as described in Section 4929.01(A), Revised Code, and thus controlled by Section 4929.05, Revised Code. By Entry dated February 27, 2006, and as modified by entries dated March 23, 2006 and March 29, 2006, a procedural schedule was established, including a local public hearing on March 27, 2006 and a public evidentiary hearing on April 3, 2006.[1] Notice of the local public hearing was made by VEDO (Co. Ex. 5). The testimony at the public hearing was generally directed at the high cost of natural gas, customers' reaction to the cost, including installing insulation and energy efficient devices, and customers' unwillingness to subsidize other customers. Letters were received by the Commission that supported conservation programs or protested any effort that would increase current rates.

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1 All references to the transcript for the public hearing on April 3, 2006, will be designated as Tr. I.

Further, on February 27, 2006, VEDO filed a Motion to Incorporate Standard Filing Requirements requesting that certain of the standard filing requirements (SFRs) from Case No. 04-571-GA-AIR be incorporated in the record of this proceeding. No party opposed the request. The motion was granted by attorney examiner entry dated March 16, 2006. Administrative notice of the SFRs was taken by the attorney examiner at the hearing on April 24, 2006 (Tr. II at 13). On March 10, 2006, VEDO filed a Motion for Waiver of Rules 4901:1-19-05 and 4901:1-19-03(B), O.A.C. No party objected to the request. The motion was granted by attorney examiner entry dated April 5, 2006.

On April 10, 2006, a stipulation was filed on behalf of VEDO, OCC and OPAE (April 2006 Stipulation)(Jt. Ex. 1). Testimony was filed prior to the hearing by VEDO, OCC, OPAE, and the Commission staff (Staff). An evidentiary hearing was held on April 24, 2006.[2] At that hearing, the parties stated that all parties had agreed to waive cross-examination of prefiled testimony, to submit all prefiled testimony as evidence of record and to submit the matter on that record. Post-hearing briefs were filed by Staff and OCC, and jointly filed by VEDO and OPAE. OCC, VEDO and OPAE recommended the adoption of the April 2006 Stipulation. The Staff opposed adoption of the Stipulation. The Coalition did not oppose the April 2006 Stipulation.

On September 13, 2006, the Commission issued its Opinion and Order in this case and approved the April 2006 Stipulation, as modified by the Opinion and Order. The modifications ordered by the Commission included eliminating the ratepayer funding of the conservation program, increasing VEDO's contribution to funding of the conservation program from $970,000 to $2 million, and targeting the conservation program to low-income customers. OCC filed an application for rehearing of the Opinion and Order on October 13, 2006. On November 8, 2006, the Commission denied the application for rehearing filed by OCC. On December 8, 2006, OCC filed a Notice of Termination and Withdrawal from the April 2006 Stipulation, pursuant to the following provision of the April 2006 Stipulation:

> Upon the Commission's issuance of an entry on rehearing that does not adopt the Stipulation in its entirety without material modification, any Party may terminate and withdraw from the Stipulation by filing notice with the Commission . . . . Upon notice of termination or withdrawal by any Party . . . the Stipulation shall immediately become null and void.

April Stipulation at 9-10.

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[2] All references to the transcript for the evidentiary hearing on April 24, 2006 will be designated as Tr. II.

Subsequently, on December 21, 2006, a second Stipulation and Recommendation (December 2006 Stipulation) was filed by VEDO, OPAE and Staff (signatory parties). The signatory parties requested that the Commission affirm the September 13, 2006, Opinion and Order that adopted and modified the April 2006 Stipulation, based on the existing record, without further hearing. The signatory parties further requested that the Sales Reconciliation Rider (SRR) and deferral mechanism adopted in the September 13, 2006, Opinion and Order, continue to be effective, as of the date of the order.

By entry dated December 29, 2006, the attorney examiner noted that OCC had withdrawn from the April 2006 Stipulation and determined that a hearing regarding the December 2006 Stipulation should be held. Therefore, the attorney examiner scheduled a prehearing conference for January 22, 2007. Further, the attorney examiner directed that the signatory parties file an amended stipulation which enumerates all terms agreed to by the parties, rather than incorporating the terms by reference from other documents.

On January 2, 2007, VEDO and OPAE filed a joint interlocutory appeal and motion for certification regarding the attorney examiner's December 29, 2006, entry. OCC filed a memorandum contra the joint motion on January 5, 2007 and a supplement to its memorandum contra on January 8, 2007. On January 10, 2007, the attorney examiner certified the interlocutory appeal of VEDO and OPAE to the Commission for the limited question of whether VEDO should be permitted to continue the accounting treatment authorized by the Commission in the September 13, 2006, Opinion and Order. By entry dated January 10, 2007, the Commission granted VEDO authority to continue the accounting treatment previously authorized by the Commission in the Opinion and Order. OCC filed an application for rehearing on February 9, 2007. The Commission denied the application for rehearing on February 28, 2007.

Moreover, on January 3, 2007, OCC filed an application for review and interlocutory appeal regarding the attorney examiner's December 29, 2006, entry. On January 5, 2007, VEDO and OPAE each submitted memoranda contra OCC's application for review and interlocutory appeal. On January 10, 2007, the attorney examiner denied OCC's application for review and interlocutory appeal.

On January 12, 2007, pursuant to the December 29 Entry, the signatory parties filed an amended Stipulation and Recommendation (January 2007 Stipulation). The signatory parties state that the January 2007 Stipulation is substantively identical to the December 2006 Stipulation but that the January 2007 Stipulation enumerates all terms agreed to by the parties, rather than incorporating the terms by reference from other documents. The prehearing conference was held on January 22, 2007. Afterwards, by entry dated January 23, 2007, the attorney examiner established a procedural schedule for consideration of the January 2007 Stipulation, setting the matter for hearing on February 28, 2007.

On January 29, 2007, VEDO and OPAE filed a joint motion for certification of an interlocutory appeal of the attorney examiner's January 23 Entry (Second Joint Motion). OCC filed a memorandum contra the joint motion on February 5, 2007. The Second Joint Motion was denied by the attorney examiner by entry dated February 12, 2007.

Moreover, on January 29, 2007, OCC filed an application for review and interlocutory appeal of the attorney examiner's January 23 Entry (Second Application). VEDO, OPAE and the Staff each filed memoranda contra OCC's application on February 5, 2007. The Second Application was denied by the attorney examiner by entry dated February 12, 2007.

On February 15, 2007, VEDO filed a motion for protective order and a motion *in limine*. On February 27, 2007, OCC filed a memorandum contra the motion for protective order and motion *in limine*. On February 16, 2007, OCC filed a motion for a continuance and request for expedited ruling. The attorney examiner granted the motion for a continuance and rescheduled the evidentiary hearing for March 28, 2007. Further, on February 22, 2007, OCC filed a motion to compel discovery regarding its first set of discovery. VEDO filed a memorandum contra the motion to compel on February 27, 2007. In addition, OCC filed a motion to compel discovery regarding its second set of discovery on February 27, 2007.

On February 28, 2007, a discovery conference was held to consider the outstanding discovery issues.[3] At the discovery conference, the attorney examiners granted in part and denied in part VEDO's motion for a protective order, granted in part and denied in part VEDO's motion *in limine*, and granted in part and denied in part OCC's motion to compel. On March 5, 2007, OCC filed an application for review and interlocutory appeal (Third Application) of the attorney examiners' rulings at the February 28, 2007, discovery conference. VEDO filed a memorandum contra the Third Application on March 6, 2007. The attorney examiner denied the Third Application by entry dated March 7, 2007.

An evidentiary hearing was held regarding the January 2007 Stipulation on March 28, 2007.[4] VEDO and Staff each presented one witness in support of the January 2007 Stipulation. OCC presented two witnesses in opposition to the Stipulation. Post hearing briefs were filed by all parties on April 23, 2007, and reply briefs were filed by all parties on May 3, 2007.

II. Summary of the Stipulation.

The January 2007 Stipulation was intended by the signatory parties to resolve all outstanding issues in this proceeding. The January 2007 Stipulation includes, *inter alia*, the following provisions:

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[3] All references to the transcript for the discovery conference on February 28, 2007 will be designated as Tr. III.

[4] All references to the transcript for the evidentiary hearing on March 28, 2007 will be designated as Tr. IV.

(1) The signatory parties agree that VEDO will implement a two-year conservation program for low-income customers. VEDO commits to fund such two-year program at no cost to ratepayers by supplying $2,000,000 provided the stipulation is adopted fully and without modification. Within the two-year term, VEDO shall file an application with the Commission that includes a proposal to continue the program and a rate design proposal as an alternative to or refinement of existing mechanisms (such as the Sales Reconciliation Rider). The application, which may be an application to increase rates, shall be filed sufficiently in advance of the end of the two-year term to obtain Commission approval prior to the end of such two-year term.

(2) Individual conservation programs that are part of the program will be evaluated on an ongoing basis using pertinent measures that focus on program costs and benefits achieved. Appropriate measures will be determined by the Conservation Collaborative (Collaborative), described in paragraph three below and will include evaluations of participation levels, energy savings and gas supply cost savings. Program results, including data related to program participation and cost, and the results of any testing, will be provided to the Collaborative on at least an annual basis. The Collaborative will also consider savings related to reduced customer arrearages and uncollectibles, favorable Percentage of Income Payment Plan (PIPP) impacts and other cost savings related to mitigating the total amount of customer bills. To the extent practicable, the Collaborative shall attempt to use available program funding to maximize the conservation benefits provided to customers.

(3) VEDO shall serve as the conservation program administrator, subject to input from the Collaborative. VEDO may use external vendors to assist in implementing certain individual programs and shall use its best efforts to make its intended use of such external vendors known to the Collaborative prior to such use becoming effective. The Collaborative shall consist of VEDO, the Commission's Staff, OCC and OPAE. The Department of Development, Office of Energy Efficiency, will be a non-voting member of the Collaborative. Within 30 days of approval of the January 2007 Stipulation, the Collaborative will meet and establish a schedule for overseeing the conservation program contemplated prior to OCC's withdrawal. Each member of the Collaborative shall participate in good faith and strive to resolve issues or pursue opportunities by a consensus governance process. The

Collaborative will review program data and evaluations, and the Collaborative shall file periodic reports (at least annually) with the Commission in Case No. 05-1444-GA-UNC, and the Commission shall retain ongoing jurisdiction during the term of the conservation program. Members of the Collaborative shall make a good faith effort to resolve any disputes through the Collaborative. If a dispute remains after good faith efforts to resolve the dispute, any member of the Collaborative may bring the dispute to the Commission's attention and seek such informal or formal action as the member deems necessary to resolve the dispute. The judgment of a majority of the Collaborative shall control unless and until such judgment is abrogated or modified by the Commission.

(4) The signatory parties represent that the Collaborative (including OCC) has met regularly since the issuance of the Commission's Opinion and Order on September 13, 2006, and had reached consensus in the implementation of program offerings to assist customers consistent with that Opinion and Order beginning in January 2007. The signatory parties request that the Commission approve the January 2007 Stipulation on an expedited basis in order to facilitate the delivery of the conservation programs to customers as directed by the Commission in its Opinion and Order, to minimize the delay in the current schedule.

(5) VEDO shall establish and implement the Sales Reconciliation Rider (SRR) to provide VEDO with a fair, just and reasonable opportunity to collect the base rate revenue requirement established by the Commission for the residential and general service customer classes in VEDO's recent base rate case, *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc., for Authority to Amend its Filed Tariffs to Increase the Rates and Charges for Gas Service and Related Maters*, Case No. 04-571-GA-AIR, Opinion and Order (April 13, 2005). The signatory parties agree and recommend that the tariff sheet containing the SRR be approved as part of the Commission's response to the January 2007 Stipulation and that the approved tariff sheet should show issued and effective dates of September 28, 2006, and October 1, 2006, respectively. The signatory parties agree that the SRR will, as part of the package described in the January 2007 Stipulation, support proactive and good faith efforts by VEDO to promote the identification and implementation of programs designed (through the Collaborative) to provide customers with more tools to reduce the quantity of natural gas otherwise required to meet their energy requirements as well as

the relative level of customers' total monthly bills. For the applicable customer classes, the SRR shall recover the difference between VEDO's weather-normalized actual base revenues and the base revenues approved in VEDO's most recent rate case, as adjusted for customer additions. The differences shall be calculated and recorded monthly beginning the first month after approval by the Commission in its September 13, 2006, Opinion and Order, and shall be deferred, without carrying costs, for subsequent recovery via the SRR. Effective November 1, 2007, and each year thereafter, VEDO shall implement the SRR rates required to amortize, over the subsequent 12-month period, the accumulated deferred differences between VEDO's weather-normalized actual base revenues and the base revenues approved in VEDO's most recent rate case, as adjusted for customer additions, consistent with the proposed tariff language. Once established, the SRR rates shall remain in effect for 12 months subject to adjustment each year for a successive 12-month period. The annual SRR update shall also include a reconciliation to ensure that SRR deferrals are not over- or under-recovered as a result of variances between estimated and actual data. In the event that the SRR is superseded by a rate design or other mechanism or the SRR is terminated, VEDO shall continue the SRR for a period of not more than 12 months in order to recover or refund any remaining unamortized SRR balance. Any over- or under-recovered SRR balance at the end of the extension period will be rolled into the Uncollectible Expense Rider, Sheet No. 39, for subsequent return or recovery from customers.

(6) The signatory parties agree and request that the Commission explicitly find that the deferral mechanism for the SRR shall continue to be effective so as to permit the deferrals provided for therein to begin as of October 1, 2006 and further agree that this timing for the commencement of this deferred accounting authority, as well as the issued and effective dates for the tariff sheet containing the SRR, are necessary to support the level and timing of VEDO's funding commitment of $2,000,000.

(7) Nothing in the January 2007 Stipulation shall be construed or applied to preclude VEDO from requesting or the Commission to granting rate relief on a permanent, interim or emergency basis. Nothing in the January 2007 Stipulation shall be construed or applied to preclude VEDO from proposing rate structure or design changes during the effective period of the conservation program.

(8) One year after implementation of the SRR, the parties will have the opportunity to conduct a review to ensure that the SRR is functioning appropriately. The Commission will review the conservation program and the SRR no later than two years after the inception of the conservation program and SRR. Neither the conservation program nor the SRR may be extended without the approval of the Commission. VEDO shall maintain such records and provide such accounting information as may be reasonably required to facilitate review of the SRR by an independent auditor. The independent auditor shall ensure that the rider rates are appropriately applied to customer bills, ensure that the costs in the rider are accounted for correctly and ensure that the volume numbers in the rider tie into the company's books and records.

III. Procedural Requirements for Alternate Rate Plans.

By entry dated February 7, 2006, the attorney examiner determined that the Conservation Application should be considered a request for an alternate rate plan as described in Section 4929.01(A), Revised Code, and thus controlled by Section 4929.05, Revised Code.

OCC raises a number of arguments regarding alleged failures to comply with the procedural requirements of Section 4929.05, Revised Code. OCC contends that VEDO's request for an alternate rate plan was not filed as part of an application pursuant to Section, 4909.18, Revised Code. Further, OCC claims that the Commission failed to order an investigation of the filing and that the Staff failed to issue a staff report of investigation. OCC also alleges that the Commission failed to establish just and reasonable rates for VEDO. Finally, OCC contends that the alternate rate plan was not properly noticed under Sections 4909.19, and 4909.43(B), Revised Code.

In its reply brief, VEDO argues that OCC's challenge to the Commission's consideration of the Conservation Application is untimely and outside the scope of issues before the Commission. VEDO also argues that the Commission's consideration of the Conservation Application meets and exceeds the procedural requirements of Section 4929.05, Revised Code.

The Commission notes that OCC has not raised its procedural claims in a timely manner. OCC was presented with numerous opportunities to raise these claims in a timely manner but failed to do so. After VEDO filed its Conservation Application, OCC filed a motion to intervene and motion to establish procedural process on December 14, 2005. In these motions, OCC did not argue that VEDO should comply with, or had failed to comply with, the procedural requirements of Section 4929.05, Revised Code. When the attorney

examiner in this proceeding determined, on February 7, 2006, that the Conservation Application be considered a request for an alternate rate plan as described in Section 4929.01(A), Revised Code, the attorney examiner directed that consideration of the Conservation Application be controlled by Section 4929.05, Revised Code. OCC did not object to this ruling nor did OCC argue that VEDO had failed to comply with the procedural requirements of Section 4929.05, Revised Code.

Subsequent to the attorney examiner's ruling, VEDO requested that certain of the SFRs from Case No. 04-571-GA-AIR be incorporated in the record of this proceeding in order to comply with the requirements of Section 4929.05, Revised Code. OCC did not oppose this request, and VEDO's motion was granted by attorney examiner entry dated March 16, 2006. Further, on March 10, 2006, VEDO requested a waiver of Rules 4901:1-19-05 and 4901:1-19-03(B), O.A.C. OCC did not object to this request, and the motion was granted by attorney examiner entry dated April 5, 2006. Finally, administrative notice of the SFRs was taken by the attorney examiner at the hearing on April 24, 2006; OCC did not object to this ruling (Tr. II at 13).

Moreover, a hearing on the Conservation Application was scheduled by the attorney examiner. Although OCC prefiled testimony prior to the hearing, OCC did not raise any issues regarding compliance with the procedural requirements of Section 4929.05, Revised Code in its testimony. Prior to the hearing, but after direct testimony had been prefiled, VEDO, OCC and OPAE entered into the April 2006 Stipulation. Rather than raising objections that the Conservation Application did not meet the procedural requirements of Section 4929.05, Revised Code, OCC represented to the Commission, in its brief filed on May 8, 2006, that the April 2006 Stipulation violated no important regulatory principles or practices pursuant to the Commission's three-prong test for consideration of stipulations.

Nonetheless, the Commission finds that OCC's objections regarding the procedures followed in this proceeding are misplaced. Section 4929.05, Revised Code, states, in relevant part, that, "[a]s part of an application filed pursuant to section 4909.18 of the Revised Code, a natural gas company may request approval of an alternative rate plan." OCC argues that VEDO has failed to follow the procedural requirements of Section 4909.18, Revised Code, pertaining to applications for an increase in rates. However, Section 4909.18, Revised Code, provides for two, distinct types of filings: applications not for an increase in rates and applications for an increase in rates. The procedural requirements for these two applications are different. In this proceeding, the tariff proposed by VEDO is set to zero ($0.00). Accordingly, the Commission finds that VEDO's application is an application *not* for an increase in rates.

An application not for an increase in rates is an application filed pursuant to Section 4909.18, Revised Code, as required by Section 4929.05, Revised Code. Therefore, the Commission finds that VEDO's application, which the attorney examiner determined

should be considered as an application for an alternative rate plan complies with the requirement of Section 4929.05, Revised Code, that a request for approval of an alternative rate plan be made as part of an application filed pursuant to Section 4909.18, Revised Code.

Moreover, the Commission finds that VEDO's application meets the procedural requirements of Section 4909.18, Revised Code, for an application not for an increase in rates. The Commission exercised its discretion to hold evidentiary hearings regarding the April 2006 Stipulation and the January 2007 Stipulation, and the Commission held a local public hearing on VEDO's Conservation Application on April 3, 2006, in Dayton, Ohio.

Further, Section 4929.05, Revised Code, contains procedural requirements in addition to the requirements of Section 4909.18, Revised Code. Section 4929.05, Revised Code, authorizes the Commission to approve an alternative rate plan after notice, investigation and hearing, and after determining just and reasonable rates and charges for the natural gas company pursuant to Section 4909.15, Revised Code. In accordance with this statutory authority, the Commission promulgated Chapter 4901:1-19, Ohio Administrative Code (O.A.C.). The Commission finds that VEDO has complied with the relevant statutory requirements and with the relevant Commission rules.

The Commission finds that VEDO's application has met the requirements for notice, investigation and hearing. On March 10, 2006, VEDO filed a motion for a waiver of the requirements of Rule 4901:1-19-05, O.A.C., which relate to filing requirements for alternative rate plans. No party objected to this motion, and the waiver was granted on April 5, 2006. VEDO published notice of the application and a local public hearing on the application (Co. Ex. 5). Publication of the notice of the local public hearing was made and the local public hearing was held on April 3, 2006, in accordance with Rule 4901:1-1-19-08(B)(2), O.A.C. The Staff investigated the application and filed testimony regarding the application (Staff Ex. 1) as well as the April 2006 Stipulation (Staff Ex. 2) and the January 2007 Stipulation (Staff Ex. 3). Evidentiary hearings were held on April 24, 2006, and March 28, 2007, in accordance with Rule 4901:1-10-08(B)(1), O.A.C.

Further, the Commission has determined just and reasonable rates for VEDO pursuant to Section 4909.15, Revised Code. The Commission recently determined just and reasonable rates for VEDO in a fully litigated rate case. *Vectren*, Case No. 04-571-GA-AIR, Opinion and Order (April 13, 2005), Entry on Rehearing (June 8, 2005). VEDO's application was filed on November 28, 2005, less than six months after the Commission's final order in Case No. 04-571-GA-AIR. On February 27, 2006, VEDO moved to incorporate the SFRs from that proceeding into the record in this case in order to contribute to the evaluation of the Conservation Application. No party to the proceeding objected to the motion, and the motion was granted by the attorney examiner on March 16, 2006. In addition, administrative notice of the SFRs was taken at the April 24, 2006, hearing (Tr. II at 13).

With respect to OCC's argument that the Commission failed to establish just and reasonable rates for VEDO, the Commission finds that, for purposes of Section 4929.05, Revised Code, we may rely upon a rate case, completed less than six months prior to the filing of an application for an alternative rate plan, for the determination that rates are just and reasonable. The statute expressly authorizes that Commission to approve an alternative rate plan "after" the Commission has determined that rates are just and reasonable. Further, the General Assembly defined alternative rate plans as plans which reduce regulatory costs and provide flexibility. The definition of "alternative rate plans" states in relevant part:

> Alternative rate plans may include, but are not limited to, methods that provide adequate and reliable natural gas services and goods in this state; *minimize the costs and time expended in the regulatory process;* tend to assess the costs of any natural gas service or goods to the entity, service, or goods that cause such costs to be incurred; afford rate stability; promote and reward efficiency, quality of service, or cost containment by a natural gas company; or *provide sufficient flexibility and incentives* to the natural gas industry to achieve high quality, technologically advanced, and readily available natural gas services and goods at just and reasonable rates and charges.

Section 4929.01(A), Revised Code (emphasis added).

The Commission believes that it would be consistent with this policy to interpret Section 4929.05, Revised Code, as NOT requiring a full rate case determination of just and reasonable charges less than six months after the completion of a rate case. However, our decision is limited to the specific facts and circumstances of this case, specifically the fact that VEDO had just completed a fully litigated rate case prior to filing the alternative rate application and that the alternative rate plan approved in this case is designed, in part, to promote administrative efficiency and to reduce regulatory costs and the need for future rate cases.

OCC also argues that Staff failed to file a staff report in this proceeding and that the Commission cannot approve the application because of that failure. We disagree. In its motion to incorporate the Staff Report from the previous rate case, Staff argued that the Staff Report filed in Case No. 05-571-GA-AIR, as updated by the stipulated schedule approved by the Commission in that proceeding, fully addressed the reasonableness of VEDO's current rates and that the reasonableness of the current rates is not contested in this proceeding. The Commission notes that Rule 4901:1-19-07, O.A.C., states that "[t]he commission staff will file a written report which addresses, at a minimum, the reasonableness of the current rates pursuant to section 4909.15 of the Revised Code for

applications filed pursuant to section 4929.05 of the Revised Code." The Commission finds that Staff's incorporation by reference of the Staff Report from Case No. 05-571-GA-AIR meets the minimum requirement of Rule 4901:1-19-07, O.A.C., that Staff address the reasonableness of the current rates of the applicant.

Therefore, the Commission finds that VEDO has complied with the procedural requirements of Section 4929.05, Revised Code, and the provisions of Chapter 4901:1-19, O.A.C. Thus, the Commission will now turn to consideration of the January 2007 Stipulation.

IV. Evaluation of the Stipulation.

Rule 4901-1-30, Ohio Administrative Code, authorizes parties to Commission proceedings to enter into stipulations. Although not binding on the Commission, the terms of such agreements are accorded substantial weight. *See Consumers' Counsel v. Pub. Util. Comm.*, 64 Ohio St. 3d 123, 125 (1992), *citing Akron v. Pub. Util. Comm.*, 55 Ohio St. 2d 155 (1978).

The standard of review for considering the reasonableness of a stipulation has been discussed in a number of prior Commission proceedings. *See, e.g., Dominion Retail v. Dayton Power and Light Co.*, Case Nos., 03-2405-EL-CSS et al., Opinion and Order (February 9, 2005); *Cincinnati Gas & Electric Co.*, Case No. 91-410-EL-AIR, Order on Remand (April 14, 1994); *Ohio Edison Co.*, Case Nos. 91-698-EL-FOR et al., Opinion and Order (December 30,1993); *Cleveland Electric Illum. Co.*, Case No. 88-179-EL-AIR, Opinion and Order (January 31, 1989). The ultimate issue for our consideration is whether the agreement, which embodies considerable time and effort by the signatory parties, is reasonable and should be adopted. In considering the reasonableness of a stipulation, the Commission has used the following criteria:

(1) Is the settlement a product of serious bargaining among capable, knowledgeable parties?

(2) Does the settlement, as a package, benefit ratepayers and the public interest?

(3) Does the settlement package violate any important regulatory principle or practice?

The Ohio Supreme Court has endorsed the Commission's analysis using these criteria to resolve issues in a manner economical to ratepayers and public utilities. *Indus. Energy Consumers of Ohio Power Co. v. Pub. Util. Comm.*, 68 Ohio St. 3d 547 (1997)(*quoting Consumers' Counsel, supra,* at 126). The Court stated in that case that the Commission may

place substantial weight on the terms of a stipulation, even though the stipulation does not bind the Commission.

(1) Is the settlement a product of serious bargaining among capable, knowledgeable parties?

VEDO notes that its witness Ulrey and Staff's witness Puican both agree that the January 2007 Stipulation was the product of serious bargaining among capable, knowledgeable parties (Co. Ex. 2c at 4-5; Staff Ex. 3 at 2-3). VEDO notes that Mr. Ulrey testified that discussion began shortly after the Commission issued its Opinion and Order on September 13, 2006, and continued for a period of months (Tr. IV at 25). Further, Mr. Ulrey testified that OCC was invited to participate in the January 2007 Stipulation but declined (Co. Ex. 2c at 4).

OPAE claims that there has been no evidence submitted in the record to indicate that the January 2007 Stipulation was not the product of serious bargaining among capable, knowledgeable parties. OPAE contends that the January 2007 Stipulation represents the collective judgment of the signatory parties that a stipulation embodying a ruling already made by the Commission is an appropriate resolution of this case.

OCC argues that the January 2007 Stipulation was not a product of serious bargaining. OCC reasons that there was no bargaining because the Stipulation merely reflects the signatory parties' acceptance of the modifications to the April 2006 Stipulation made by the Commission in its Opinion and Order in this proceeding. Further, OCC argues that there is no diversity of interests represented by the signatory parties because only OCC and the Coalition represent customers. Finally, OCC alleges that it and the Coalition were excluded from the negotiations which led to the January 2007 Stipulation.

The Coalition argues that there is virtually no basis in the record of this case or in the background of the three signatory parties, VEDO, OPAE and Staff to conclude that the January 2007 Stipulation was a product of serious bargaining among capable, knowledgeable parties and, therefore, the Commission should reject the January 2007 Stipulation.

Responding to OCC's contention that OPAE does not represent residential customers, OPAE notes that advocacy on behalf of low- and moderate-income residential customers is OPAE's corporate purpose. Further, OPAE argues that the Commission has repeatedly found that OPAE brings a unique perspective to its proceedings.

VEDO responds to OCC by noting that there is no requirement that a representative of any specific customer class support a stipulation in order to meet the first prong of the three-prong test. VEDO contends that establishing such a requirement would empower any

individual intervenor who is the sole representative of a customer class to hold an otherwise reasonable stipulation hostage to its demands. VEDO suggests that this cannot be the result intended by the Commission when it established the three-prong test since the three-prong test is designed specifically for partial stipulations which are not supported by all parties to a proceeding. *See Ohio Consumers' Counsel v. Pub. Util. Comm.*, 64 Ohio St. 3d at 126.

The Commission finds that the first prong of the test is met by the January 2007 Stipulation. The Commission has previously held that we will not require any individual party's approval of stipulations in order to meet the first criterion of our three-prong standard of review. *Dominion Retail v. Dayton Power and Light, supra*, at 18. In considering whether there was serious bargaining among capable and knowledgeable parties, the Commission evaluates the level of negotiations that appear to have occurred and takes notice of the experience and sophistication of the negotiating parties. The signatory parties all routinely participate in complex cases before the Commission and are all represented by counsel who practice before the Commission on a regular basis. Although OCC claims that it was excluded from the negotiations leading up to the January 2007 Stipulation, OCC does not cite to any evidence in the record to support that claim; and OCC's witnesses did not present any evidence at the evidentiary hearing regarding the first prong of the Commission's three-prong test (Tr. IV at 128; Tr. IV at 160).

Moreover, contrary to OCC's claims, the signatory parties do represent a diversity of interests, including the utility, the Staff and OPAE, an advocate for low and moderate income customers. In its motion to intervene, OPAE represented its interest in this proceeding as an advocate "for affordable energy for low and moderate income Ohioans." OCC failed to oppose intervention or otherwise dispute OPAE's statement of its interest in the proceeding in a timely manner, and intervention was granted to OPAE on the basis of its stated interest. Further, the Commission notes that OPAE has been granted intervention in numerous other Commission proceedings based upon the same or similar statement of its interest in the proceedings.

With respect to OCC's contention that there was no serious bargaining because parties simply accepted the Commission's modifications to the April 2006 Stipulation, the Commission notes that no party was obligated to accept those modifications. In fact, OCC objected to those modifications and withdrew from the April 2006 Stipulation; thus, the January 2007 Stipulation has different signatory parties than the April 2006 Stipulation. Following OCC's withdrawal from, and termination of, the April 2006 Stipulation, the parties were free to file a stipulation which was identical to the April 2006 Stipulation, to file a stipulation which included new terms, or to file no stipulation at all. Further, VEDO was free to proceed with its application as originally filed or to withdraw its application altogether. Because the parties were free to take any of these alternate courses of action, the

Commission cannot agree with OCC's contention that there was no serious bargaining with respect to the January 2007 Stipulation.

(2) Does the settlement, as a package, benefit ratepayers and the public interest?

VEDO cites the Commission's Opinion and Order in this proceeding as the best evidence that the January 2007 Stipulation, which mirrors the terms of the April 2006 Stipulation as modified by the Commission, benefits ratepayers and the public interest. VEDO contends that the only economic difference between the April 2006 Stipulation, as proposed, and the January 2007 Stipulation is a $4.7 million swing in favor of customers as a result of the elimination of customer funding of the DSM programs and the increase in funding required from VEDO. Finally, VEDO cites to the testimony of its witness Ulrey, who testified that the Collaborative of stakeholders has designed programs for which 60 percent of VEDO's residential customers are eligible and that associated marketing and education efforts will reach all customers, as will the nexus on-line tool, which assists customers in their conservation efforts (Co. Ex. 2c at 3; Tr. IV at 37-38).

OPAE contends that the Commission has already determined that the two-year pilot program in the January 2007 Stipulation is in the public interest. OPAE notes that the revenue recovery mechanism is unchanged from the prior phase in this proceeding and that the only difference is in the energy efficiency program and how it is financed. OPAE concludes that the evidence presented by OCC fails to refute the conclusion that the January 2007 Stipulation is in the public interest. Instead, the evidence presented by OCC indicates OCC's preference for a larger DSM program, paid for primarily with ratepayer funding.

OCC argues that the January 2007 Stipulation, as a package, does not benefit ratepayers and the public interest. OCC claims that the majority of the benefits accrue to VEDO while the majority of costs are thrust upon VEDO's customers. OCC alleges that the most substantial cost to VEDO is the $2 million contribution to the conservation program and that $2 million is just $1.3 million net of tax to VEDO. On the other hand, OCC claims that the January 2007 Stipulation practically guarantees recovery of residential and general service revenues authorized in VEDO's last rate case. OCC notes that, presently, the risk of recovering those revenues is shouldered by VEDO, but, with the SRR, VEDO no longer will be subject to that risk.

OCC further states that VEDO's customers receive very little in exchange. OCC cites to the testimony of its witness Kushler, who stated that:

> [T]he stipulation provides only a very small energy efficiency program that will not provide sufficient benefits on the whole to customers. Additionally, the stipulation affords VEDO the tremendous benefits of a decoupling mechanism, paid for by

> residential and commercial customers. Given the significant investment by Vectren customers, in the form of the decoupling mechanism, there should be reasonable and commensurate benefits to customers. This is absent from the [January 2007 Stipulation].

OCC Ex. F at 2-3.

The Coalition concedes that the January 2007 Stipulation would help low-income customers and that conservation programs, by reducing collection costs, reducing disconnection and reconnection costs, and helping reduce arrearages and the costs of riders to recover such arrearages, can benefit all customers. However, the Coalition argues that the costs of the SRR exceed the benefits to ratepayers and that adoption of the January 2007 Stipulation would create a precedent authorizing the use of decoupling mechanisms for VEDO and other utility companies. Therefore, the Coalition concludes that the stipulation does not benefit ratepayers and the public interest.

Staff believes that the January 2007 Stipulation is in the public interest. Staff argues that 60 percent of VEDO's residential customers are eligible to participate in the proposed $2 million conservation program, which is justified because it follows the Commission's practice of assisting low income customers, it has system-wide benefits, and it is entirely funded by the company. Staff cites to the testimony of VEDO witness Ulrey that the January 2007 Stipulation would allow a $2 million conservation program, which is designed through the collaborative efforts of the parties, including OCC. Further, qualification for the low-income program was established at 300 percent of the poverty level, which would mean that 60 percent of VEDO's customers would be eligible for the program (Tr. IV at 37-39). In addition, Staff cites to the testimony by its witness Puican, who testified that there are system-wide benefits in that, by reducing low-income customers' bills, there are potential reductions in uncollectible expenses as well as reductions in the amounts necessary for recovery of PIPP funds (Tr. IV at 169). Moreover, Staff witness Puican testified that low-income programs are beneficial regardless of whether system-wide benefits can be demonstrated (Tr. IV at 170).

Moreover, Staff argues that adoption of an SRR is in the public interest because it allows a utility to recover its actual costs and decreases the need for multiple rate cases due to the substantial drop in consumption per customer. Staff notes that the SRR is a mechanism to allow recovery of fixed costs through a non-traditional means and that, in alternate rate proceedings, the Commission can approve non-traditional mechanisms like the SRR. Further, Staff witness Puican testified that there is value in regulatory efficiency over time that will decrease the need for multiple rate cases (Tr. IV at 192).

Replying to the signatory parties, OCC argues that the costs to ratepayers in the April 2006 Stipulation, as proposed, were mitigated by the system-wide benefits derived from the DSM programs; however, under the January 2007 Stipulation, there is no similar opportunity to mitigate costs on a system-wide basis. Moreover, OCC contends that VEDO is not making a substantial contribution under the January 2007 Stipulation; rather, it is customers who are being forced to contribute substantially, while deriving little in return.

In addition, OCC responds to OPAE's arguments by citing its witnesses' testimony that, generally, low-income programs are less cost-effective than other programs (Tr. IV at 108; Tr. IV at 144). Thus, OCC argues that, if the objective is to generate economic benefits, the conservation or DSM funds would be better spent on non-low income programs.

OPAE replies to OCC by stating that the signatory parties view the January 2007 Stipulation and the revenue recovery provisions as reasonable given the two-year pilot period under the January 2007 Stipulation. OPAE contends that, between the company financing of the conservation program and the return of the GCR refund to GCR customers, the pilot may result in virtually no increase in rates at all. OPAE argues that the modifications to the April 2006 Stipulation ordered by the Commission reduced the projected impact upon customers while supporting an attempt by VEDO to reorient its mission to provide energy services through a combination of commodity sales and conservation. OPAE believes that the pilot period provides an opportunity to evaluate the benefits of this approach.

In its reply brief, Staff notes that the January 2007 Stipulation contains a substantial commitment by VEDO to fund conservation that will benefit VEDO's low and moderate income customers. Staff notes that, although OCC argues that the $2 million in conservation funding in the January 2006 Stipulation is inadequate, the $4.67 million program supported by OCC was funded with $3.7 million in ratepayer funds. Staff further argues that the benefits posited by OCC witness Kushler in his testimony are speculative, relying upon the assumption that utilities throughout the Midwest are also conducting robust DSM programs (OCC Ex. F at 4-5; Exhibit MGK-2).

The Commission finds that the settlement, as a package, benefits ratepayers and the public interest. The Commission continues to believe that it is in the public interest, in order to promote energy efficiency, to decouple the link between gas consumption and the company's ability to meet its revenue requirements. As we stated in the Opinion and Order in this proceeding, the Commission believes that the linking of gas consumption with the public utility's ability to meet its revenue requirements is counterproductive to energy efficiency. Further, as we stated in the Opinion and Order, we continue to believe that recovering fixed costs, such as those related to the distribution system, through the SRR would eliminate the counterproductive impact of VEDO promoting conservation (Opinion and Order at 16). Therefore, the Commission finds that the SRR, which would decouple the

link between gas consumption by consumers and the company's ability to meet revenue requirements, is in the public interest.

Moreover, the SRR is limited to two years under the January 2007 Stipulation, will be subject to further review by the parties and the Commission during the two-year period, and may not be extended without our approval. This two-year period and opportunity for review is consistent with our Opinion and Order in this proceeding, where we stated that:

> [W]e believe that because of its untested mechanism, the SRR needs a more thorough review than called for in the [April 2006 Stipulation, as proposed]. We find that the stipulation should be modified to require a review of both the conservation program and the SRR by the Commission. This review shall occur no later than two years after the inception of the conservation program and rider, and neither the DSM program nor the SRR may be extended without the approval of the Commission.

Opinion and Order at 16.

In addition, the Commission notes that implementation of the SRR only will allow VEDO the opportunity to collect the revenue requirement ordered by the Commission in VEDO's last rate case. The Commission has already determined that these revenues are required for VEDO to earn a fair and reasonable rate of return. *Vectren*, Case No. 04-571-GA-AIR, Opinion and Order (April 13, 2005) at 16.

Further, the January 2007 Stipulation embodies a *quid pro quo* by the signatory parties: implementation of the SRR in exchange for implementation, and company funding, of the conservation programs. In exchange for the opportunity to collect the revenues which the Commission has already determined are necessary to earn a fair and reasonable rate of return, VEDO will fund a conservation program with $2 million in company funds. No ratepayer funds and no refunds due GCR customers will be used to fund the conservation program.

The Commission notes that, as originally proposed and agreed to by OCC, the April 2006 Stipulation provided that the DSM programs would be funded by ratepayer funds in the amount of $3.7 million, including a $1.98 million GCR refund, which the Commission had previously ordered should be returned to GCR customers. *In the Matter of the Regulation of the Purchased Gas Adjustment Clause Contained Within the Rate Schedules of Vectren Energy Delivery of Ohio, Inc., and Related Matters*, Case No. 02-220-GA-GCR, Opinion and Order (June 14, 2005) and Entry on Rehearing (August 10, 2005). The ratepayer funding for the proposed DSM program also included $27,000 in interest allowances on the GCR refund, $1,600,000 in gas supply portfolio management proceeds and $93,000 to be deferred for

subsequent recovery. VEDO, on the other hand, was obligated to contribute only $970,000 for the DSM programs under the April 2006 Stipulation as originally proposed. In the Opinion and Order issued on September 13, 2006, in this proceeding, we determined that:

> We find, however, that the stipulation's two-year budget for the conservation program should not be funded by ratepayers in this case, and therefore, it is inappropriate for GCR customers to provide the money for the DSM program. We believe the funding sources identified in the stipulation as resulting from GCR refunds, interest allowance on that refund and proceeds from a gas supply portfolio management arrangement should be realized by ratepayers as ordered by this Commission in VEDO's gas cost recovery proceedings.

Opinion and Order at 13.

The Commission notes that the Supreme Court recently upheld our decision to order VEDO to refund the $1.98 million to GCR customers. *Vectren Energy Delivery of Ohio, Inc. v. Pub. Util. Comm.* (2007), 113 Ohio St. 3d 180. The Commission notes that the direct costs to ratepayers of the DSM programs in the April 2006 Stipulation, as agreed to by OCC, amounted to approximately $3.7 million (Tr. IV at 236). However, the direct cost to ratepayers for the conservation program in the January 2007 Stipulation is zero.

Further, the Commission is not persuaded by the testimony by OCC witness Kushler that $2 million is insufficient for an effective DSM program and that the minimum amount necessary for an effective DSM program is $4.65 million, as originally proposed in the April 2006 Stipulation. The Commission finds that $2 million is sufficient for the program approved in this Supplemental Opinion and Order given that the planned conservation program is limited to two years and that, during the two-year period, the parties will have an opportunity to assess the efficacy of the conservation programs.

Nonetheless, we believe that greater efforts in developing DSM programs can be made. The Conservation Collaborative shall address additional opportunities to achieve energy efficiency improvements and consider opportunities which may extend beyond programs for low and moderate income residential consumers. Staff shall promptly schedule a technical conference to address DSM program design issues and the development of DSM programs beyond those approved in this Supplemental Opinion and Order. The parties, either collectively to the extent the Collaborative reaches an agreement on a broader set of program designs, or individually to the extent complete agreement is not reached, shall submit their findings and recommendations to the Commission within ninety days or such further time as may be allowed. Further, nothing in this Order shall restrict

the Company's ability to implement additional cost-effective DSM programs or to seek recovery of additional DSM expenditures in an appropriate proceeding.

In addition, the Commission notes that we approved $1.1 million per year for conservation programs that target income-eligible customers in VEDO's last rate case. *Vectren*, Case No. 04-571-GA-AIR, Opinion and Order (April 13, 2005) at 13. Thus, over the two-year period covered by the January 2007 Stipulation, there will be a total of $4.2 million in funding for conservation programs targeted for low income customers. Accordingly, the Commission directs that the parties include a review of the conservation programs funded through the last rate case in their review of the DSM programs funded pursuant to the January 2007 Stipulation.

Finally, OCC argues that the conservation funds would be better spent on non-low income programs. The Commission disagrees with OCC's conclusion. The Commission notes that the Collaborative has defined "low income" to include both low and moderate income customers by setting the threshold qualification for the conservation program at 300 percent of the poverty level. The Commission endorses this decision by the Collaborative. By extending the conservation program to low and moderate income customers, the Collaborative's decision is consistent with our decision in the Opinion and Order to direct the conservation program to the customers most in need of assistance, including customers who do not qualify for other assistance programs such as PIPP. Although we are mindful of the need to consider cost-benefit analyses with respect to conservation and DSM programs, the Commission must also consider the fact that volatile natural gas prices have a significant impact on low and moderate income households in assessing whether the conservation and DSM programs are in the public interest. Thus, given the limited resources available to fund conservation and DSM programs, we continue to believe, consistent with our Opinion and Order in this proceeding, that it is in the public interest to target conservation programs to low and moderate income customers.

In summary, the January 2007 Stipulation provides for the implementation of the SRR, which will provide VEDO with the opportunity to collect no more than the revenues which the Commission has already determined are necessary to provide VEDO with a fair and reasonable rate of return. In exchange, VEDO will provide $2 million in company funds for a conservation program targeted to the customers who most need assistance in dealing with volatile natural gas prices; and ratepayers are not being required to fund the conservation programs. The Commission finds that this settlement, as a package, benefits ratepayers and the public interest. Therefore, the Commission finds that the January 2007 Stipulation meets the second prong of the three-prong test.

(3) <u>Does the settlement package violate any important regulatory principle or practice?</u>

OPAE notes that no OCC witness testified at the evidentiary hearing on whether or not the January 2007 Stipulation violates any important regulatory principle. On the other hand, VEDO and OPAE cite to the testimony of VEDO's witness Ulrey, who testified that the Commission has already found that the April 2006 Stipulation, as modified by the Commission, violated no regulatory principle and that the terms of the January 2007 Stipulation demonstrate that the signatory parties are willing to implement the April 2006 Stipulation, as modified by the Commission (Co. Ex. 2c at 5). VEDO and OPAE also note that Staff's witness Puican testified that the January 2007 Stipulation does not violate any important regulatory principles or practices (Staff Ex. 3 at 3).

OCC argues on brief that the January 2007 Stipulation violates important regulatory principles and practices under Section 4909.15, Revised Code, and Section 4929.02, Revised Code. Specifically, OCC argues that the SRR mechanism violates traditional rate-making concepts, such as the test period. Further, OCC contends that VEDO is not complying with the policies enumerated in Section 4929.02, Revised Code, including providing adequate, reliable and reasonably priced natural gas service, encouraging demand side natural gas services and facilitating the states' competitiveness in the global economy. Further, OCC claims that the January 2007 Stipulation unreasonably allows VEDO considerable regulatory freedom that is not commensurate with VEDO's commitments to Section 4929.02, Revised Code.

OCC also claims in its brief that VEDO has failed to sustain its burden of proving that it has complied with Section 4929.02, Revised Code. OCC concedes that VEDO has filed testimony in this proceeding that addressed these statutory requirements, but OCC claims that VEDO cannot rely on that testimony in support of the January 2007 Stipulation because the testimony was originally filed in support of the Conservation Application or the April 2006 Stipulation.

The Coalition argues that the January Stipulation would allow VEDO to collect revenue for sales it never made. Further, the Coalition contends that the Stipulation would permit VEDO to impose costs upon all its customers without an adequate showing of a benefit for all its customers. The Coalition concludes that the Stipulation places important regulatory principles at risk.

OPAE responds to OCC's arguments by noting that VEDO was operating under rates set in a fully litigated case approved barely a year prior to the filing. OPAE contends that VEDO has never requested to recover revenue in excess of that approved in the last rate case. Thus, OPAE concludes that the January 2007 Stipulation is based upon a record that meets the requirements of Section 4929.02, Revised Code.

The Commission finds that the differences between the proposed April 2006 Stipulation, which OCC supported, and the January 2007 Stipulation, which OCC opposes,

relate solely to the differences between the demand side management program and the conservation program proposed by each Stipulation. OCC did not present any evidence at the March 28, 2007, evidentiary hearing regarding differences in the SRR as proposed by the April 2006 Stipulation and the SRR as proposed by the January 2007 Stipulation. OCC's witnesses at the evidentiary hearing did not present any testimony addressing whether the January 2007 Stipulation violates any important regulatory principles or practices (Tr. IV at 129; Tr. IV at 160). Thus, the Commission finds that the SRR in the January 2007 Stipulation is identical to the SRR in the April 2006 Stipulation, which OCC represented to the Commission, in its brief filed on May 8, 2006, did not violate any important regulatory principles and practices. In fact, every party to this proceeding has, at one point or another in this proceeding, supported the implementation of the proposed SRR *and* represented to the Commission that the proposed SRR violates no important regulatory principles or practices.

With respect to the specific issues raised by OCC, the Commission finds that OCC's reliance on traditional rate-making concepts is misplaced. In this proceeding, we have determined that VEDO's application should be considered as an alternative rate plan. Section 4929.01(A) defines an alternative rate plan as "a method, alternate to the method of Section 4909.15 of the Revised Code, for establishing rates and charges..." Therefore, we find that the General Assembly intended to authorize alternative rate plans which do not rely on traditional rate-making concepts.

With respect to OCC's arguments regarding VEDO's compliance with Section 4929.02, Revised Code, Section 4929.05, Revised Code, states that, after the Commission has determined just and reasonable rates and charges for a natural gas company, it shall authorize an applicant to implement an alternate rate plan if a natural gas company has made a showing and the Commission finds that:

(1) The natural gas company is in compliance with section 4905.35 of the Revised Code and is in substantial compliance with the policy of this state specified in section 4929.02 of the Revised Code.

(2) The natural gas company is expected to continue to be in substantial compliance with the policy of this state specified in section 4929.02 of the Revised Code after implementation of the alternative rate plan.

The Commission finds that OCC has not offered any support for its claim that the Commission cannot rely upon the testimony filed in the record of this proceeding. This testimony was properly prefiled before the evidentiary hearing, was admitted into the record of this proceeding without objection, and was subject to cross-examination, which was waived by all of the parties (Tr. II at 7). The Commission finds that this testimony is relevant to whether VEDO currently is in compliance with Section 4905.35, Revised Code,

and is in substantial compliance the policy of this state specified in Section 4929.02, Revised Code, irrespective of whether the testimony was originally offered in support of the Conservation Application, the April 2006 Stipulation or the January 2007 Stipulation. Further, OCC does not cite to any other evidence in the record which disputes the evidence submitted by VEDO. Therefore, the Commission finds, based upon the full record of this proceeding, that VEDO is currently in compliance with the undue advantage requirements found in Section 4905.35, Revised Code and that it is currently in substantial compliance with the state policy specified in Section 4929.02, Revised Code.

Further, the Commission finds that the January 2007 Stipulation is consistent with the state policy objectives set forth in Section 4929.02, Revised Code. The January 2007 Stipulation will promote adequate, reliable and reasonably priced natural gas service by allowing VEDO the opportunity to collect, through the SRR, the revenue requirements for a fair and reasonable rate of return, as established by the Commission in VEDO's last rate case but no more than those revenue requirements. The January 2007 Stipulation will encourage energy efficiency by providing for a $2 million company-funded conservation program, targeted to consumers most at risk to volatile natural gas prices, without relying on refunds due GCR customers. Finally, the Commission finds that the January 2007 Stipulation facilitates the state's competitiveness in the global economy by encouraging energy efficiency through decoupling the link between consumption by consumers and the company's ability to meet revenue requirements and through encouraging conservation through the funding of the conservation program. Therefore, we find that VEDO is expected to remain in substantial compliance with the policy of this state specified in Section 4929.02, Revised Code, after implementation of the January 2007 Stipulation and that VEDO the has met its burden of proof under Section 4929.05, Revised Code, for an application for an alternative rate plan.

Moreover, our finding in this Supplemental Opinion and Order is consistent with our holding in our Opinion and Order in this proceeding, where we held that:

> The Commission finds that VEDO has presented in the record of this proceeding that it is currently in compliance with the undue advantage requirements found in Section 4905.35, Revised Code, that it is currently in substantial compliance with the state policy specified in Section 4929.02, Revised Code, and will maintain substantial compliance with Section 4929.02, Revised Code . . . .

Opinion and Order at 10.

Therefore, the Commission concludes that the January 2007 Stipulation does not violate any important regulatory principles or practices and that the January 2007 Stipulation meets the third prong of the three-prong test for the consideration of stipulation.

Finally, OCC argues that the Commission's previous findings that the April 2006 Stipulation, as modified by the Commission, are not dispositive of the reasonableness of the January 2007 Stipulation. This argument is moot. The Commission has considered the January 2007 Stipulation based upon the full record of this proceeding, including the evidence presented at the March 28, 2007, evidentiary hearing and the briefs submitted by the parties regarding the January 2007 Stipulation. Based upon our consideration of the full record of this proceeding, we have determined that the January 2007 Stipulation should be adopted by the Commission.

Accordingly, having determined that the January 2007 Stipulation meets each prong of the three-prong test, the Commission finds that the January 2007 Stipulation should be adopted by the Commission.

VI. OTHER ISSUES

OCC argues that the Commission cannot use accounting authority to circumvent the ratemaking provisions of Sections 4909.15 and 4909.18, Revised Code. OCC notes that the Commission has permitted VEDO to continue certain accounting, previously approved by the Commission when it adopted the April 2006 Stipulation, while this case is pending. OCC claims that, in authorizing this accounting, the Commission has facilitated an unauthorized rate increase.

VEDO responds that, pursuant to Section 4905.13, Revised Code, the Commission may authorize accounting treatment for the deferral of costs associated with the SRR. Staff notes that the Commission may use the systems of accounts for public utilities under Section 4905.13, Revised Code, to modify VEDO's accounting procedures, so it can track the revenue differential between actual revenues received and weather normalized revenues authorized in VEDO's last rate case. Staff argues that OCC cannot cite to any authority that prevents the Commission from using its authority under Section 4905.13, Revised Code, to modify a utility's accounting procedures.

The Commission fully addressed this issue in our Entry on Rehearing dated February 28, 2007, in this proceeding, where we held that:

> As we noted in our January 10 Entry, OCC stated, in its memorandum contra VEDO's application for an interlocutory appeal, that the accounting implemented by VEDO "is in reality a mere tracking mechanism" and that the true deferral accounting that will occur is not set to go forward until implementation of the sales reconciliation rider in the fourth quarter of 2007. OCC concluded that there is "no financial consequence to the current

> tracking." The Commission having authorized VEDO to continue the accounting treatment, OCC now claims our January 10 Entry was more than a mere accounting approval, arguing that the effect of approving the accounting is that rates will be increased significantly on the basis of the deferrals being permitted.
>
> The Commission has recognized a distinction between accounting practices under Section 4905.13, Revised Code, and the rate-making provisions of Chapter 4909, Revised Code. See, *In the Matter of the Application of Columbia Gas of Ohio, Inc., for Authority to Modify its Current Accounting Procedures for its Costs in Implementing the Commission's Moratorium on the Disconnection of Utility Service*, Case No. 01-3278-GA-AAM, Entry (January 3, 2002) at 2. See also *Consumers' Counsel v. Pub. Util. Comm.* (1983), 6 Ohio St. 3d 377, 388. In this case the Commission merely granted VEDO authority to continue the accounting treatment during the pendency of this proceeding.

Entry on Rehearing (February 28, 2007) at 8.

OCC has raised no new arguments and presented no new evidence regarding this issue. However, the Commission notes that, by adopting the January 2007 Stipulation, we are expressly permitting VEDO to continue the accounting necessary to implement the SRR.

OCC also contends that the decoupling mechanism should not be adopted on a stand-alone basis because it is not in the public interest and contravenes Sections 4909.15 and 4909.18, Revised Code. OCC notes the testimony of its witness Kushler, who testified that the decoupling mechanism should not be implemented without significant DSM investments (OCC Ex. F at 12). OCC notes, on the other hand, that Staff's witness Puican testified that Staff is now not opposed to a decoupling mechanism on a stand-along basis, with no linkage to DSM funding (Tr. IV at 189). OCC contends that approval of the decoupling mechanism on a stand-alone basis is not in the public interest.

VEDO replies that the Commission has the authority to approve the SRR as a stand-alone rate design mechanism even though a stand-alone SRR is not a feature of the January 2007 Stipulation. Staff replies that the January 2007 Stipulation contains both a decoupling mechanism and a conservation program, so the Commission is not being asked to adopt the decoupling mechanism on a stand-alone basis, as OCC suggests.

The Commission finds that the January 2007 Stipulation, which we adopt in this Supplemental Opinion and Order, does not provide for a decoupling mechanism on a

stand-alone basis because the January 2007 Stipulation contains both the SRR and the conservation program. Therefore, the Commission finds that OCC's argument on this issue is moot.

OCC also argues that the Commission has no jurisdiction to allow VEDO to implement an alternative rate plan under Section 4929.01(A), Revised Code, while it remains subject to rate of return regulation. We disagree. OCC cites to no language in Section 4929.01(A), Revised Code, in support of its argument; nonetheless, we note that Section 4929.01(A), Revised Code, broadly defines alternative rate plans:

> (A) "Alternative rate plan" means a method, alternate to the method of section 4909.15 of the Revised Code, for establishing rates and charges, under which rates and charges may be established for a commodity sales service or ancillary service that is not exempt pursuant to section 4929.04 of the Revised Code or for a distribution service. Alternative rate plans may include, but are not limited to, methods that provide adequate and reliable natural gas services and goods in this state; minimize the costs and time expended in the regulatory process; tend to assess the costs of any natural gas service or goods to the entity, service, or goods that cause such costs to be incurred; afford rate stability; promote and reward efficiency, quality of service, or cost containment by a natural gas company; or provide sufficient flexibility and incentives to the natural gas industry to achieve high quality, technologically advanced, and readily available natural gas services and goods at just and reasonable rates and charges. Alternative rate plans also may include, but are not limited to, automatic adjustments based on a specified index or changes in a specified cost or costs.

The Commission finds that this definition vests the Commission with broad discretion in authorizing alternative rate plans, including a mechanism such as the SRR proposed in this case.

VI. TARIFFS

As part of its investigation in this proceeding, the staff reviewed the proposed tariff provisions for the SRR. The Commission has reviewed the proposed tariffs and finds that the proposed tariffs are reasonable; therefore, they will be approved by the Commission.

Although the Commission will not set the effective date for this tariff as October 1, 2006, as recommended by the January 2007 Stipulation, the Commission will note that VEDO has authority, pursuant to the alternative rate plan approved in this Supplemental

Opinion and Order, to recover all deferrals made pursuant to the accounting treatment approved by the Commission by Entry dated January 10, 2007. However, VEDO shall file the initial rate for the rider as part of an application to increase rates under Section 4909.18, Revised Code. Thereafter, the Commission will allow VEDO to automatically adjust the rider subject to our review and approval.

FINDINGS OF FACT AND CONCLUSIONS OF LAW:

(1) On November 28, 2005, VEDO filed its application seeking authority to: recover certain expenses associated with proposed conservation programs; establish a mechanism to reconcile, in part, base rate revenue actually collected by VEDO with the base rate revenue authorized by the Commission in the company's last rate proceeding, Case No. 04-571-GA-AIR; employ such accounting as may be required to defer certain conservation program expenses for amortization in a subsequent rate proceeding; and employ such accounting as may be necessary to implement the conservation program expense recovery mechanism and the base rate revenue reconciliation mechanism.

(2) By attorney examiner entry dated February 7, 2006, it was directed that the Conservation Application be considered a request for an alternate rate plan as described in Section 4929.01(A), Revised Code, and thus controlled by Section 4929.05, Revised Code.

(3) The Commission granted intervention to OCC, OPAE and Citizen's Coalition.

(4) The Commission granted motion to admit David C. Rinebolt to practice *pro hac vice* on behalf of OPAE.

(5) A local public hearing was held on April 3, 2006.

(6) Notice of the local public hearing was made by VEDO.

(7) On April 10, 2006, the April 2006 Stipulation was filed on behalf of VEDO, OCC and OPAE.

(8) An evidentiary hearing was held on April 24, 2006.

(9) On September 13, 2006, the Commission issued its Opinion and Order in this proceeding, adopting the April 2006 Stipulation as modified by the Commission. OCC filed an application for rehearing of the

Opinion and Order on October 13, 2006. On November 8, 2006, the Commission denied the application for rehearing filed by OCC.

(10) On December 8, 2006, OCC filed a Notice of Termination and Withdrawal from the April 2006 Stipulation.

(11) On December 21, 2006, a second Stipulation and Recommendation (December 2006 Stipulation) was filed by VEDO, OPAE and Staff. On January 12, 2007, the signatory parties filed an amended Stipulation and Recommendation (January 2007 Stipulation).

(12) An evidentiary hearing was held regarding the January 2007 Stipulation on March 28, 2007.

(13) Post hearing briefs were filed by all parties on February 23, 2007, and reply briefs were filed by all parties on May 3, 2007.

(14) The record of this proceeding shows that VEDO is currently in compliance with the undue advantage requirements found in Section 4905.35, Revised Code, that it is currently in substantial compliance with the state policy specified in Section 4929.02, Revised Code, and will maintain substantial compliance with Section 4929.02, Revised Code, in the event the Commission approves the stipulation submitted in this proceeding.

(15) VEDO has met its burden of proof under Section 4929.05, Revised Code, for an application for an alternative rate plan.

(16) The January 2007 Stipulation was the product of bargaining among knowledgeable parties.

(17) The January 2007 Stipulation, as a package, benefits ratepayers and the public interest.

(18) The January 2007 Stipulation does not violate any important regulatory principle or practice.

(19) The January 2007 Stipulation is reasonable and should be adopted.

ORDER:

It is, therefore,

ORDERED, That the stipulation filed January 12, 2007, be approved. It is, further,

ORDERED, That Applicant is authorized to file in final form four complete, printed copies of tariffs consistent with this Supplemental Opinion and Order, and to cancel and withdraw its superseded tariffs. One copy shall be filed with this case docket, one copy shall be filed with the Applicant's TRF docket (or may make such filing electronically as directed in Case No. 06-900-AU-WVR) and the remaining two copies shall be designated for distribution to the Rates and Tariff Division of the Commission's Utilities Department. The Applicant shall also update its tariffs previously filed electronically with the Commission's docketing division. It is, further,

ORDERED, That the effective date of the new tariffs shall be a date not earlier than the date of this decision, and the date upon which four complete, printed copies of final tariffs are filed with the Commission. The new tariffs shall be effective for services rendered on or after such effective date. It is, further,

ORDERED, That nothing in this Supplemental Opinion and Order shall be binding upon this Commission in any future proceeding or investigation involving the justness or reasonableness of any rate, charge, rule or regulation. It is, further,

ORDERED, That a copy of this Supplemental Opinion and Order be served on all parties of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO

Alan R. Schriber, Chairman

Paul A. Centolella

Ronda Hartman Fergus

Valerie A. Lemmie

Donald L. Mason

GAP:ct

Entered in the Journal
JUN 27 2007

Reneé J. Jenkins
Secretary

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc. for Approval, Pursuant to Revised Code Section 4929.11, of a Tariff to Recover Conservation Expenses and Decoupling Revenues Pursuant to Automatic Adjustment Mechanisms and for Such Accounting Authority as May Be Required to Defer Such Expenses and Revenues for Future Recovery Through Such Adjustment Mechanisms.	)	Case No. 05-1444-GA-UNC

CONCURRING OPINION OF COMMISSIONER PAUL A. CENTOLELLA AND VALERIE A. LEMMIE

This concurring opinion addresses my views on the requirement in the Supplemental Opinion and Order that the Conservation Collaborative address additional opportunities to achieve energy efficiency improvements and consider programs which are not limited to low and moderate income residential consumers.

The current record in this proceeding differs significantly from what was available to the Commission at the time of its September 13, 2006 Opinion and Order. Assessments introduced in OCC's testimony indicate that existing markets have not produced an efficient level of consumer investment in gas energy efficiency improvements and that the failure to implement these improvements has significant costs.

In its September Opinion and Order, the Commission recognized that conservation and efficiency should be an integral part of natural gas policy, found the efforts to develop demand-side management (DSM) "laudable" and was unable to adopt the demand-side management programs delineated in the proposal before it at that time. The Commission's concerns regarding these specific demand-side program designs, however, do not represent a conclusion that only demand-side programs targeting low income consumers can be justified.

Parties to the Conservation Collaborative should develop demand-side program designs that are cost-effective, produce demonstrable benefits, and produce a reasonable balance between reducing total costs and minimizing impacts on non-participants, consistent with Ohio's economic and energy policy objectives. Future programs may

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address DSM opportunities without being limited to low and moderate income residential consumers.

A. Potential for Energy Efficiency Improvements

Citing the detailed technical and economic analysis of efficiency opportunities contained in the Vectren DSM Action Plan: Final Report,[1] OCC witness Kushler testified that, "because VEDO does not have a history of operating significant energy efficiency programs, there should be a great amount of technical potential for improving the energy efficiency of homes and businesses in the VEDO service territory." (Direct Testimony of Martin G. Kushler at 8.)[2]

A careful review of the Vectren report supports Dr. Kushler's conclusion that the unrealized potential to improve the efficiency of gas usage is large.

- Vectren's analysis includes a detailed market assessment calculating the current average gas consumption per consumer in different market segments by end use (space heating, water heating, cooking, etc.). This assessment of end use gas consumption provides a baseline reflecting current practices.

- Second, the study analyzes conservation potential, the amount by which consumption could be reduced through available efficiency measures. The *conservation potential analysis combines modeling the net impacts of a set of* available efficiency improvements and an analysis of the levelized cost of individual efficiency measures.[3] The modeling shows that if all consumers implemented available efficiency improvements, gas use could fall by up to 47%. And, the assessment of individual measures indicates that most of these savings can be achieved at a levelized cost that is well below the delivered price of gas.

- Finally, Vectren's Action Plan describes a DSM program planning process and specific DSM programs proposed for Vectren's Indiana distribution company. The programs proposed to ramp up Vectren's Indiana DSM initiative are

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1 The Action Plan was prepared for Vectren by Forefront Economics, Inc., and H. Gil Peach and Associates in consultation with an Advisory Board consisting of utility, residential and industrial consumer representatives; Dr. Peach of H. Gil Peach and Associates testified in this proceeding on behalf of OPAE.

2 Although the Action Plan was prepared for VEDO's Indiana affiliate, VEDO witness Karl testified that given the close geographic proximity and demographic similarities of the two service territories, "the results from the Vectren Indiana assessment are applicable to VEDO's service territory." (Direct Testimony of Douglas A. Karl on Behalf of Vectren Energy Delivery of Ohio, Inc. sponsoring Applicant's Exhibit No. DAK-1 at 6).

3 The modeling approach used captures the interactions between measures.

expected to reduce gas consumption by 1.4% by the fifth year of program implementation. The assessment concludes:

> "At less than half the cost per therm of delivered gas supply, the demand side resource is shown to be highly cost effective. Net energy costs in the Vectren North service area are expected to be $37 million lower if the DSM programs are implemented. Most of these benefits accrue to residential and small commercial customers."

Apparently assuming no impact on gas commodity prices, the rate impact from the cost of the proposed programs ranges from less than one mill per therm (4 programs) to 2 mills per therm for the Small Buildings program, which provides over 80% of the total resource cost savings.

Vectren's analysis finds that there is a large unrealized potential for gas efficiency improvements in a market that closely resembles VEDO's service territory.

This observed unrealized potential to make additional efficiency improvements is inconsistent with the application of a rigid assumption of consumer rationality to the energy efficiency implications of consumer purchasing decisions.[4] Gas prices are a primary driver of recent consumer investment in gas energy efficiency.[5,6] However, that

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4 Although it is useful to assume in various types of economic modeling and analyses that consumers are well informed and act as if making precise economic calculations of costs and expected returns, this is an assumption. Such consumer rationality originally was assumed to facilitate the application of mathematics to economic problems, and not on the basis of studies of actual consumer behavior. Over the last several decades, economists and social scientists have increasingly studied actual consumer decisions to better understand the limitations of neoclassical theory and develop alternative models that provide better match to reality. Recognition of this work was punctuated by the award of the 2002 Nobel Prize in Economics to Daniel Kahnemen and Vernon Smith for their work in Behavioral and Experimental Economics. For a review of contemporary research in behavioral economics, see: Camerer, C.F., Lowenstein, G., and Rabin, M., eds. 2004. *Advances in Behavioral Economics.* Princeton, N.J.: Princeton University Press. For a history of the assumption of consumer rationality and a less technical summary of contemporary economic perspectives, see: Beinhocker, E. 2006. *The Origin of Wealth: Evolution, Complexity, and the Radical Remaking of Economics.* Boston, MA: Harvard Business School Press.

5 Building and appliance efficiency standards also play a significant role. Additionally, federal tax incentives are currently available for some efficiency improvements. Significant utility or state efficiency programs are in place in some jurisdictions. See: Exhibit MGK-4, attached to the testimony of OCC witness Kushler.

6 The record in this case does not include any analysis of the long-run price elasticity of natural gas consumption as it relates to the adoption of efficiency measures at a household or business level. Price elasticity of demand is an economic measure of how consumption responds to changes in price. It may be inappropriate to assume a high degree of elasticity given that at least some studies suggest residential gas consumption may be relatively inelastic. See: Bohi, D. R., & Zimmerman, M. B. (1984). An Update on Econometric Studies of Energy Demand Behavior. *Annual Review of Energy. 9,* 105-154. Bernstein, M., & Griffin, J. (2005). *Regional Differences in the Price-Elasticity of Demand for Energy.* RAND Infrastructure, Safety, and Environment. (Technical) Report No. TR-292-NREL.

does not mean that consumers are adopting most available and cost-effective energy efficiency measures.

Consumer decisions which impact energy efficiency often occur in a context where energy efficiency is not the central consideration. Consumers are seeking the ability to live in a warm house, cook their food, dry their clothes, or take a hot shower. They use natural gas only as a means to obtain these services. Many of the consumer decisions which impact on gas energy efficiency are made in the course of buying a home, selecting an apartment, buying an appliance, or quickly replacing a failed furnace or water heater when energy efficiency may not be the primary consideration.

Based on the then available record, the Commission's September Opinion and Order found that the net economic benefit of demand-side programs may best be ensured by directing programs to low income consumers. The additional data presented in this case suggest that there is a large potential for cost-effective energy efficiency improvements that is not limited to low and moderate income residential consumers.

There are market failures that can affect a broad range of consumer purchasing decisions and that may help explain the large unrealized potential for efficiency improvements, including:

- *Information Asymmetries*: Energy use is one attribute of a large number of products and services. Information on energy is often not readily available or evident to consumers when making purchasing decisions that implicitly involve the choice to make or not to make an energy-efficiency investment.[7] As a result, consumers in some circumstances may be poorly informed regarding cost, technology, and their energy-efficiency choices. The asymmetric distribution of information also may create barriers to communicating the benefits of energy-efficiency investments within firms.[8] These asymmetries make it more difficult to change historical purchasing practices.

- *Bound Rationality*: Evaluating energy-efficiency investments can require solving complicated optimization questions. Consumers may lack the expertise necessary to reasonably gather, process, and apply some of the

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7 A. Sanstad and R. Hawarth, "'Normal' Markets, Market Imperfections and Energy Efficiency," *Energy Policy*, Vol. 22, No. 10 (1994) pp. 812-818; W. Kempton and L. Layne, "Consumer's Energy Analysis Environment," *Energy Policy*, Vol. 22, No. 1 (1994) p. 857; P. Komor, et al, *Energy Use, Information, and Behavior in Small Commercial Buildings*, PU/CEES-240 (Princeton, NY: Princeton University, July 1989).

8 S. DeCanio, "Barriers within Firms to Energy-Efficient Investment," *Energy Policy*, Vol. 21, No. 9 (1993) p. 906.

information needed to make energy-efficient choices.[9] Thus, although consumers may intend to be rational, limited attention, resources, and ability to process information may effectively limit their choices.[10] When faced with unfamiliar options, empirical studies indicate that consumers tend to repeat prior purchasing patterns and avoid cost minimizing choices that have a higher first cost.[11] Such behavior can impede the adoption of energy-efficient technologies.

Additional barriers to the adoption of efficiency measures may include the split incentives that can occur when a developer or landlord makes investment decisions which impact the utility bills of the ultimate homeowner or tenant. [12]

B. The Distribution of Costs and Benefits

The parties have discussed the distribution of benefits and costs between program participants and non-participant ratepayers. However, a lack of adequate discussion of program design alternatives and the parties' focus on spending levels has made it difficult for the Commission to identify a balanced approach to pursuing cost-effective efficiency improvements, without unduly impacting non-participant ratepayers.

There are three considerations which help frame when it is appropriate to go forward with programs that may increase costs to non-participants. First, to the extent a DSM program facilitates an efficiency investment that would not otherwise have occurred and that investment reduces the total costs of achieving the same or an improved level of energy services, the net cost reduction is a benefit, even if the benefit flows only to the program participant. Program designers and ultimately the Commission may have to consider whether a given program is inequitable, but we should not confuse equity considerations with whether there is a net economic efficiency benefit. Second, a "no

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9 A. Sanstad and R. Hawarth, "'Normal' Markets, Market Imperfections and Energy Efficiency," *Energy Policy*, Vol. 22, No. 10 (1994); W. Kempton and L. Montgomery, "Folk Quantification of Energy," *Energy*, Vol. 7, No. 10 (1982) p. 817.

10 H. Simon, *Models of Man* (New York, NY: Wiley and Sons, 1957); A. Tversky and D. Kahneman, "The Framing of Decisions and the Psychology of Choice," *Science*, Vol. 211 (1981) p. 452; A. Tversky and D. Kahneman, "Rational Choice and the Framing of Decisions," *Journal of Business*, Vol. 59, No. 4-2 (1986) p. S251.

11 H. Huntington, "Been Top Down So Long, It Looks Like Bottoms Up to Me," *Energy Policy* (October 1994) p 833; R. Thaler, *The Winner's Curse: Paradoxes and Anomalies of Economic Life* (New York, NY: The Free Press, 1992); R. Thaler, "Toward a Positive Theory of Consumer Choice," *Journal of Economic Behavior in Organization* (March 1990) p. 39.

12 W. Golove and J. Eto, *Market Barriers to Energy Efficiency: A Critical Reappraisal of the Rationale for Public Policies to Promote Energy Efficiency*, Lawrence Berkeley Laboratory Report No. LBL-38059 (Berkeley, CA: Lawrence Berkeley Laboratory, March 1996).

losers" test which ensures that no consumer faces additional costs as a result of a DSM program is inappropriate. While such Pareto optimality might be desirable goal in some contexts, it cannot define the limits of reasonable energy efficiency program design. Businesses and policy makers are continuously faced with choices that may impose additional costs on some individuals in order to achieve larger economic benefits for the enterprise or community as a whole. A standard which prohibits DSM programs, if some rate payers would incur additional costs, ensures that many consumers will be made worse off. Third, non-participant impacts should receive reasonable consideration. An appropriate approach is to, first, minimize unnecessary ratepayer impacts and then find a reasonable balance between efficiency benefits as reflected in reductions in net total resource or societal costs and equity considerations as reflected in any negative ratepayer impacts. Avoiding undue impacts on non-participants and striking an appropriate balance between efficiency and equity considerations is part of the art of DSM program design.

In this case, the OCC and OPAE witnesses have presented testimony indicating that efficiency programs provide at least three benefits, in addition to directly avoided gas, capacity, and distribution costs, which will benefit society generally or non-participating consumers.

First, OCC and OPAE witnesses have recognized that improving end use efficiency will tend to reduce fossil fuel consumption and thereby reduce the emission of greenhouse gases. This is significant because energy efficiency can cost-effectively avoid greenhouse gas emissions without imposing additional emission reduction costs. Moreover, the homes built and some of the equipment purchased today could remain in service for decades. There can be significant lost opportunity costs, if efficiency is not fully considered at the time of construction or initial purchase. Given the potential for significant limitations on greenhouse gas emissions, avoiding long-term lost opportunities deserves careful consideration in energy efficiency program design.

Second, greater reliance on energy efficiency investments could result in the addition of Ohio jobs. OCC witness Kushler testified that because Ohio is dependent on imported natural for 87% of its gas supplies, there is a dollar drain on the state's economy. Based on a study of the impacts of regional energy efficiency programs,[13] Dr. Kushler estimates that a moderately aggressive five-year regional program would produce a net gain of approximately 5,300 jobs and $100 million in additional net annual employee compensation in Ohio by 2010. (Direct Testimony of Martin G. Kushler at 5-7 and Exhibit MGK-2.) These estimates of job and payroll increases are based on an input/output model

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[13] Kushler, M., D. York, and P. Witte. 2005. *Examining the Potential for Energy Efficiency to Help Address the Natural Gas Crisis in the Midwest.* Washington, D.C.: American Council for an Energy Efficient Economy. Exhibit MGK-2 attached to the Direct Testimony of Martin G. Kushler.

and thus reflect both direct employment impacts related to the installation of efficiency measures and price induced changes in employment. It is not possible to distinguish between direct and price induced employment impacts based on the filing in this case. However, given that marginal gas supplies tend to be from other states and countries, it is reasonable to conclude that significant gas efficiency programs are likely to produce a net gain in Ohio jobs and payrolls, independently of whether such programs are adopted in other states or produce a net reduction in energy prices.

Third, OCC witnesses Kushler and Chernick testified that significant efficiency programs will result in a reduction in natural gas prices that will be enjoyed by all consumers. Mr. Chernick makes the fundamental point: spikes in gas prices when the weather is cold reflect the fact that the supply curve for natural gas can be relatively steep. A material change in the gas usage could result in a significant change in the market price of gas. And, if the change in demand is small, the change in price may not be striking, but it should occur. (Direct Testimony of Paul L. Chernick at 17.) This observation is directionally correct.[14] The record includes results from two studies suggesting the potential magnitude of such price impacts. First, the 2005 Midwest study, attached to Dr. Kushler's Direct Testimony as Exhibit MGK-2, found that a moderately aggressive five-year regional energy efficiency initiative[15] would result in total utility bill savings to Ohio customers of nearly $800 million per year by 2010, with cumulative savings over five years of nearly $3 billion. (Direct Testimony of Martin G. Kushler at 5-7 and Exhibit MGK-2.) The price impact of a more modest program of gas efficiency improvements was analyzed in a recent New York State Energy Research and Development Authority Administration (NYSERDA) study. The NYSERDA study found that a gas DSM program capturing just 5% of economic conservation potential and reducing gas consumption by 1.5% by 2016 could reduce total retail gas prices by 0.3%, saving New York consumers over $500 million. (Direct testimony of Paul L. Chernick at 18.) These studies support the conclusion that improvements in gas efficiency will tend to reduce the price of gas supplies, at least partially offsetting the impact of program costs on non-participants.

It has been argued that the Commission should not consider the Midwest regional study because it is uncertain whether other states will initiate the efficiency programs assumed in that study. If every state takes this approach, it will become a self-fulfilling prophecy that efficiency programs will not be undertaken. Fortunately, companies such as Vectren are initiating efficiency programs in other states, there are already significant gas

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14 To the extent there is an impact on wholesale gas prices, there could be additional impacts on the price of electricity during those periods when gas fired units are on the margin and setting the market price for electricity.

15 The study is based on programs reducing gas and electric loads by approximately 6% over 8 Midwestern states.

efficiency programs in at least 2 of the 8 states covered by the study,[16] and the Midwest Energy Efficiency Alliance, which includes approximately 60 utilities, government agencies, corporations, and non-profit organizations has been working to foster efficiency programs across the region based, in part, on the results of the study presented in this case. To the extent that genuine regional economic benefits can be achieved, Ohio utilities should not be among the last to come to the table.

C. Program Design Considerations

The balance between cost savings and any negative ratepayer impacts, to a large degree, is struck through the design of specific DSM programs. Unfortunately, the parties in this case elected to focus on spending levels and presented little testimony on program design alternatives. The objective of efficiency programs is to achieve cost effective savings, not to increase DSM spending. Without a more detailed discussion program design alternatives, their costs, and likely impacts, the Commission is left with limited information on which to base a decision about the appropriate level of DSM expenditures.

The lack of information on program design alternatives means that obvious questions regarding previously proposed programs remain unanswered. For example, there is, at least, a significant minority of consumers who have purchased efficient gas furnaces. There are ways to structure a furnace program to avoid simply paying incentives to consumers who would have purchased high efficiency furnaces without an incentive, i.e. "free riders." These alternatives might include a shared savings program in which the additional capital cost of a high efficiency furnace is initially paid by the utility and repaid by the participant through sharing the resulting bill savings. Alternatively, a targeted approach focusing on specific market segments where barriers such as split incentives prevent the widespread adoption of efficient furnaces might achieve net savings and minimize incentive payments to free riders. However, approaches to limiting free ridership were not adequately addressed. Similarly, a program that features installation of programmable thermostats will need to address the choice between thermostats that may be programmable to reduce winter gas consumption and programmable controllable thermostats which may represent a cost-effective measure for reducing both gas use and peak period electric air conditioner demand. Further, there was not an adequate discussion as to how the impacts of informational programs would be measured and evaluated.

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16 The evidence in this case indicates that there are significant gas efficiency programs in Minnesota and Wisconsin and some gas efficiency programs in Illinois and Iowa. (Direct Testimony of Martin G. Kushler at Exhibit MGK-4, p. 6-7.)

Parties proposing energy efficiency programs should address program design alternatives, why specific proposed designs were selected, and how the proposed program addresses specific design considerations. The design of energy efficiency programs should consider:

- How to best achieve net total resource cost and societal benefits;
- How to minimize unnecessary and undue ratepayer impacts;
- How process and impact evaluations will be conducted to ensure the programs are implemented efficiently and achieve demonstrable benefits;
- How to capture what might otherwise become lost opportunities to achieve efficiency improvements in new buildings and from the purchase of equipment that is likely to remain in service for an extended period of time;
- How to minimize "free ridership" and the perceived inequity resulting from the payment of incentives to those who might adopt efficiency measures without such incentives; and
- How to integrate, where appropriate, gas DSM programs with other initiatives including federal tax incentives and improvements in electric energy efficiency.

The Company, and other parties proposing efficiency expenditures, should take these factors into consideration in developing a reasonable and balanced portfolio of energy efficiency programs.

Paul A. Centolella
Commissioner

Valerie A. Lemmie
Commissioner

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JUN 27 2007

Reneé J. Jenkins
Secretary