BEFORE THE STATE OF MINNESOTA

OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of the Application of CenterPoint Energy Resource Corp., d/b/a CenterPoint Energy Minnesota Gas for Authority to Increase Natural Gas Rates in Minnesota	)	**OAH No. 12-2500-20147-2** **MPUC Dkt. No. G-008/GR-08-1075**

Rebuttal Testimony of
J. Richard Hornby
Synapse Energy Economics

On Behalf of
Izaak Walton League of America – Midwest Office
Minnesota Center for Environmental Advocacy

July 20, 2009

I. Introduction/Summary

Q. PLEASE STATE YOUR NAME, EMPLOYER, AND PRESENT POSITION.

A. My name is J. Richard Hornby. I am a Senior Consultant at Synapse Energy Economics, Inc., 22 Pearl Street, Cambridge, MA 02139.

Q. ARE YOU THE SAME J. RICHARD HORNBY WHO SUBMITTED PRE-FILED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. My rebuttal testimony responds to certain of the points that witnesses for other parties have made in their direct testimony regarding the Conservation Enabling Rider ("CE Rider") that CenterPoint Energy (CenterPoint or the Company) has proposed on a three year pilot basis. Mr. Chavez, on behalf of the Minnesota Office of Energy Security, and Mr. Lindell, on behalf of the Minnesota Office of the Attorney General, each filed direct testimony opposing a CE Rider pilot. My rebuttal responds to several points in their respective direct testimonies that relate to the design of the CE Rider pilot agreed to under the Stipulation between CenterPoint, the Izaak Walton League of America (IWLA), the Minnesota Center for Environmental Advocacy (MCEA), and the Energy CENTS Coalition. To distinguish this from the CE Rider that CenterPoint proposed in its original filing I will refer to it as the Stipulation CE Rider. I address those points under three broad headings – (1) link to efficiency-related reductions in annual gas use, (2) application to small volume firm service customers, and (3) anticipated rate impacts. The

fact that I do not respond explicitly to other specific points in their respective direct testimonies does not necessarily mean I agree with those other points.

II. Link To Efficiency-Related Reductions In Annual Gas Use

Q. PLEASE SUMMARIZE THE TWO POINTS MR. CHAVEZ HAS PRESENTED REGARDING THE RELATIONSHIP BETWEEN THE CE RIDER AND EFFICIENCY-RELATED REDUCTIONS IN ANNUAL GAS USE.

A. Mr. Chavez expresses two related points regarding links between efficiency-related reductions in annual gas use and design of the CE Rider. Both points stem from the fact that the CE Rider is not designed to adjust CenterPoint's annual revenues solely for reductions in annual gas use from its conservation programs. He expresses the first point starting on page 27 as a concern about the absence of explicit links between the operation of the CE Rider and reductions in annual gas use beyond, or incremental to "business as usual" levels. He expresses the second point starting on page 36 as a concern that the CE Rider will adjust the Company's revenues for changes in annual use relative to test year levels regardless of the reason, e.g., "….deviations in the efficient use of natural gas, but also deviations in weather, the commodity price of natural gas, the price elasticity of residential customers, and the changes in economic activity."

Q. COULD THE TWO POINTS RAISED BY MR. CHAVEZ POTENTIALLY APPLY TO THE STIPULATION CE RIDER?

A. Yes, the two points Mr. Chavez has presented regarding the relationship between the CE Rider and efficiency-related reductions in annual gas use are potentially applicable to the

Stipulation CE Rider, except for the fact that the latter will not include adjustments for changes in usage attributable to weather.

Q. DID YOU ANTICIPATE THESE POINTS IN YOUR DIRECT TESTIMONY?

A. Yes. In my direct testimony, I noted that some parties might propose a narrower rate adjustment mechanism, such as one that would limit rate adjustments to reductions in annual usage attributable to the Company's energy efficiency programs incremental to the levels of reductions it has been achieving in the absence of a CE Rider or similar mechanism.

Q. PLEASE RESPOND TO THESE TWO POINTS AS THEY RELATE TO THE STIPULATION CE RIDER.

A. In response to the concern raised by Mr. Chavez, and as noted in my direct testimony, the Stipulation CE Rider is a reasonable approach. For starters, the CE Rider will be tested on a pilot basis that will last no longer than three years, during which it will operate subject to a rate cap.

Of more importance, the Stipulation CE Rider is preferable to a more limited mechanism from an energy and environmental policy perspective. This broader approach makes the Company financially indifferent to all efficiency-related reductions in usage regardless of the sources or causes of those reductions, e.g., CenterPoint conservation programs, price elasticity, new building codes, new appliance standards. In fact, the Next Generation Energy Act of 2007 which Mr. Chavez cites anticipates that Minnesota will achieve annual energy savings through a combination of initiatives, some implemented directly by utilities and others implemented by other parties and supported by utilities:

> **216B.2401**. ENERGY CONSERVATION POLICY GOAL. It is the energy policy of the state of Minnesota to achieve annual energy savings equal to 1.5 percent of annual retail energy sales of electricity and natural gas directly through energy conservation improvement programs and rate design, and **indirectly through energy codes and appliance standards, programs designed to transform the market or change consumer behavior, energy savings resulting from efficiency improvements to the utility infrastructure and system, and other efforts to promote energy efficiency and energy conservation**." (Emphasis added.)

Third, the Stipulation CE Rider imposes less administrative burden than a more limited rider because it does not require detailed analyses to distinguish reductions attributable to Company conservation programs from reductions attributable to other factors. In addition, this approach does not require analyses to distinguish the portion of reductions in annual gas use from conservation programs that are beyond, or incremental to a "business as usual" level.

Q. DOES YOUR LAST POINT MEAN THAT THERE WILL BE NO EVALUATION OF THE EFFICIENCY-RELATED REDUCTIONS IN GAS USE ACHIEVED UNDER THE STIPULATION CE RIDER PILOT?

A. Not at all. On the contrary, as I noted in my direct testimony, the performance of the Stipulation CE Rider will be subject to a comprehensive evaluation each year as well as at the end of the three-year pilot. My point regarding a lower administrative burden with this broader approach is based upon my understanding of the experience of other jurisdictions with partial decoupling and narrower riders, sometimes referred to as lost revenue adjustment mechanisms. Under a partial decoupling approach, considerable effort has to be placed on distinguishing the reductions solely attributable to Company conservation programs from reductions attributable to any other factors. If the partial

decoupling was to be further limited to only reductions in annual gas use from conservation programs incremental to a "business as usual" level, even more analysis would be required.

Q. PLEASE RESPOND TO THE SPECIFIC POINT EXPRESSED BY MR. CHAVEZ REGARDING THE ABSENCE OF AN EXPLICIT LINK BETWEEN OPERATION OF THE STIPULATION CE RIDER AND EFFICIENCY-RELATED REDUCTIONS IN GAS USE.

A. In response to the specific concern raised by Mr. Chavez regarding the absence of an explicit link between operation of the Stipulation CE Rider and efficiency-related reductions in gas use, I expect that link to be examined as part of the evaluation of the Stipulation CE Rider pilot. In other words, I expect the Commission to assess the efficiency-related reductions in gas use that were achieved during the period the Stipulation CE Rider was in effect.

One point of reference for that assessment will likely be the 2010-2012 Triennial CIP Plan in which CenterPoint proposes to ultimately achieve double the annual savings it is currently achieving. At the end of the Stipulation CE Rider pilot the Commission will have to determine whether to continue it on a regular basis or to terminate it. When making that decision I am sure that the Commission will consider the actual efficiency-related reductions that CenterPoint has achieved relative to those proposed in its 2010 - 2012 Triennial CIP Plan.

The annual savings that CenterPoint is proposing to achieve in the 2010 -2012 Triennial CIP Plan reflect the new energy and environmental policy environment under

which it will be operating. The proposed Stipulation CE Rider provides CenterPoint with a rate mechanism consistent with that new operating environment.

Q. IS THERE EVIDENCE INDICATING THAT A RATE ADJUSTMENT MECHANISM SUCH AS THE STIPULATION CE RIDER SHOULD HAVE A POSITIVE INFLUENCE ON THE ATTITUDES OF UTILITY MANAGEMENT TOWARDS HELPING CUSTOMERS IMPROVE EFFICIENCY.

A. Yes. The following examples indicate that a rate adjustment mechanism such as the Stipulation CE Rider should have a positive influence on the attitudes of utility management towards helping customers improve efficiency.

The first example is the evaluation of a Distribution Margin Normalization mechanism (DNM) prepared by Christensen Associates Energy Consulting in 2005[1]. Northwest Natural Gas Company (NW Natural) implemented the DNM on a pilot basis in 2002. The Oregon Public Utility Commission (PUC) required the evaluation as an input to its decision to continue or terminate the mechanism. The evaluation found that the DNM had a number of positive results. In particular it was found to be an effective means of reducing NW Natural's disincentive to promote energy efficiency and to contribute to a shift in marketing from sales to conservation. The Oregon PUC approved continuation of the mechanism.

[1] A Review of Distribution Margin Normalization as Approved by the Oregon Public Utility Commission for Northwest Natural, Christensen Associates Energy Consulting, LLC, March 2005 (available at http://www.aga.org/NR/rdonlyres/9F74E959-3319-4DD3-9164-3F3B0F91D02E/0/0706CHRISEVALPRO.PDF).

The second example is Avista Utilities, an electric and natural gas utility operating in Washington and Idaho. In February 2007 Avista received approval from the Washington State Utilities and Transportation Commission to implement a natural gas decoupling mechanism on a pilot basis from January 2007 through June 2009 (Order 04, Docket UG-060518). Avista commissioned an evaluation of the pilot dated March 30, 2009.[2] Tables 2 and 3 of the evaluation indicate that Avista's average annual reductions from DSM in Washington during the pilot in 2007 and 2008 were 61% higher than its 2004-2005 annual averages, and 37% higher than its IRP DSM annual savings goals for those years.

The third example is CenterPoint Energy Arkansas Gas, the sister company of CenterPoint operating in Arkansas. In October 2007 CenterPoint Energy Arkansas Gas received approval from the Arkansas Public Service Commission to implement a decoupling mechanism. Subsequent to receiving that approval, CenterPoint Energy Arkansas Gas increased its annual spending on energy efficiency programs from less than $700,000 in calendar 2008 to a proposed $4 million for calendar 2010. (Responses to Information Requests No. 12 and No. 16 of IWLA and MCEA).

[2] Evaluation of Avista Natural Gas Decoupling Mechanism Pilot -- Final Report to Avista and the Stakeholder Advisory Group, March 30, 2009 (available at http://www.utc.wa.gov/rms2.nsf/177d98baa5918c7388256a550064a61e/7a41ed2be10bba3d8825758a0070d946!OpenDocument).

Q. HAVE OTHER STATES APPROVED RATE ADJUSTMENT MECHANISMS FOR GAS UTILITIES WITH EFFICIENCY PROGRAMS?

A. Yes. According to a report released by the American Gas Association in May 2009, nineteen states allow gas distribution utilities to recover all or part of the revenue impact of customer conservation of natural gas through a decoupling mechanism, a flat monthly rate design or a lost margin tracker.[3]

Q. PLEASE ADDRESS THE RELATED POINT THAT MR. LINDELL HAS RAISED.

A. Mr. Lindell presents a related, but somewhat different perspective. He notes, starting on page 28, that the annual gas usage per CenterPoint customer has not been declining materially in recent years and therefore there is no need for a CE Rider. However, the exact magnitude of decline in annual gas usage per customer in the past is not the factor driving support for the Stipulation CE Rider from an energy and environmental policy perspective. The factor driving support for the Stipulation CE Rider is the goal of making the Company financially indifferent to all efficiency-related reductions in usage regardless of the sources or causes of those reductions.

[3] Natural Gas Rate Round-Up, American Gas Association, May 2009 (available at http://www.aga.org/NR/rdonlyres/E1041155-29E6-4D15-8607-6CF4B6D96DB8/0/0905RegulatoryApproachesPromotingEE.pdf).

III. Application To Small Volume Firm Service Customers

Q. PLEASE SUMMARIZE THE POINT REGARDING APPLICABILITY TO SMALL VOLUME FIRM CUSTOMERS RAISED BY MR. CHAVEZ AND MR. LINDELL.

A. Both Mr. Chavez and Mr. Lindell note that the CE Rider would be limited to small volume firm service customers. Mr. Chavez discusses this point starting page 39 while Mr. Lindell addresses it starting page 34. The Stipulation CE Rider is similarly limited to small volume firm service customers.

Q. IS IT REASONABLE TO LIMIT THE APPLICATION OF THE STIPULATION CE RIDER TO SMALL VOLUME FIRM CUSTOMERS?

A. Yes. Limiting application of a decoupling mechanism such as the Stipulation CE Rider to small volume firm service customers is not unusual for a gas utility and it does not disadvantage those customers.

Limiting application of a decoupling mechanism to small volume firm service customers is not unusual for a gas utility such as CenterPoint. For example, the gas decoupling pilot approved for Avista Utilities only applied to its residential and small commercial customers. This approach is not unusual for gas utilities because, unlike electric utilities, gas utilities serve a large number of dual-fuel customers who are not "captive". Instead, customers in dual fuel rate classes, which Mr. Chavez identifies in Table 1 of his direct testimony as SVDF and LVDF, have the ability to switch to their alternative fuel source if their burner-tip price of gas, i.e., the CenterPoint distribution service charge plus their commodity cost of gas supply, exceeds the burner-tip price of

their alternate fuel. On the other hand, gas utilities typically do not experience the same magnitude of lost margin per therm if those customers use less gas because they typically allocate a lower amount of fixed costs to rate classes that are not receiving firm service.

Limiting application of a decoupling mechanism such as the Stipulation CE Rider to small volume firm service customers does not disadvantage those customers. The Stipulation CE Rider is designed to give CenterPoint the opportunity to recover only the portion of its test year revenue requirements that was approved for recovery from small volume firm service customers. CenterPoint cannot use the Stipulation CE Rider to, in effect, shift recovery of margin from dual-fuel customers to small volume firm service customers.

IV. Anticipated Rate Impacts

Q. PLEASE SUMMARIZE THE POINTS REGARDING ANTICIPATED RATE IMPACTS RAISED BY MR. CHAVEZ.

A. Mr. Chavez discusses three points relating to anticipated rate impacts, on pages 46 to 53. His basic concern appears to be that the CE Rider may elicit objections by a significant number of ratepayers and may result in rates that are not reasonable.

Q. DID MR. CHAVEZ PROVIDE A QUANTITATIVE ESTIMATE OF THE POTENTIAL IMPACT OF THE CE RIDER ON RETAIL RATES THAT MIGHT ELICIT OBJECTIONS BY RATEPAYERS?

A. No. I certainly agree that any proposed change in rates needs to be scrutinized. However, as part of that scrutiny it is important to place the magnitude of the proposed change into perspective. For example, had the Stipulation CE Rider been in effect since

the Company's last general rate case, it would have been set at $0.04281 per dekatherm (DT) for residential customers from July 2008 through May 2009. That is approximately 0.45% of the average total volumetric rate of $ 9.5273/dt those customers were paying during that period and would have collected $4.04 in total from an average customer over that ten month period. This minimal level of impact is illustrated in Responses to OES Information Requests 1046 and 1047.

Q. DID MR. CHAVEZ DISCUSS THE POTENTIAL OFFSETTING LONG-TERM BENEFICIAL IMPACTS ON AVERAGE BILLS FROM INCREASING EFFICIENCY-RELATED REDUCTIONS?

A. No. The discussion of any potential adverse rate impacts of the CE Rider or the Stipulation CE Rider should also include a discussion of the potential offsetting long-term beneficial impacts on average bills from increasing efficiency-related reductions. Since gas supply costs are the dominant component of average bills of residential and small commercial customers, the potential reductions in that component in the long-term due to efficiency-related reductions in gas use should far exceed any modest increases in the distribution component due to the CE Rider.

Q. DOES THIS COMPLETE YOUR REBUTTAL TESTIMONY?

A. Yes.