

Application of San Diego Gas & Electric
Company (U-902-M) for Approval of
Demand Response Programs and Budgets
for the Years 2012 through 2014.

Application 11-03-____

CHAPTER IV

PREPARED DIRECT TESTIMONY OF

KEVIN C. McKINLEY

SAN DIEGO GAS & ELECTRIC COMPANY

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

MARCH 1, 2011

TABLE OF CONTENTS

1		
2	I. PURPOSE	1
3	II. METHODOLOGY	1
4	A. Tests	2
5	B. Program Incentive Payments	3
6	C. Portfolio Evaluation	3
7	III. MODEL INPUTS.....	3
8	A. A Factor	4
9	B. B Factor.....	4
10	C. C Factor.....	5
11	D. D Factor	6
12	E. E Factor.....	7
13	IV. OTHER ANALYSIS ASSUMPTIONS	7
14	A. Discount Rate.....	7
15	B. Measurement and Evaluation (M&E) Costs.....	7
16	C. Capital.....	8
17	D. Treatment of Technology Incentives	8
18	E. Permanent Load Shifting	9
19	F. Capacity Bidding Program.....	10
20	G. Budget Exclusions	10
21	H. Allocation of System Support Activities and Other Allocations.....	11
22	I. Expected Events.....	12
23	J. Energy Rates	12
24	V. RESULTS OF COST EFFECTIVENESS TESTING USING E3 TEMPLATE.....	12
25	VI. QUALIFICATIONS	15
26		

1 **CHAPTER IV**

2 **PREPARED DIRECT TESTIMONY**

3 **OF KEVIN C. MCKINLEY**

4 **I. PURPOSE**

5 My testimony presents the overall results of the cost effectiveness tests for the 2012-2014
6 proposed demand response (“DR”) programs and the overall portfolio. The load impacts utilized
7 in these cost effectiveness tests are covered in the testimony of Kathryn Smith.

8 **II. METHODOLOGY**

9 The primary intent of a demand response program is to reduce peak demand. The
10 benefits of demand response programs are in avoiding costs that would otherwise be increased to
11 meet the peak demand including avoided electric generation capacity costs, Transmission &
12 Distribution (“T&D”) costs, and energy costs including commodity costs, line losses and
13 environmental costs. SDG&E was required in Decision 10-12-024 to utilize the 2010 Demand
14 Response Cost Effectiveness Protocols (Protocols) in Appendix “A” of that decision and to use
15 the Cost Effectiveness Template provided by the California Public Utility Commission’s
16 consultant E3 (“E3”) to calculate the various cost effectiveness tests described below. The E3
17 template already contained the most critical assumptions and values required to calculate DR
18 cost effectiveness when received by SDG&E. As directed, SDG&E used these protocols and the
19 template provided to calculate the estimates of cost effectiveness for the Demand Response
20 program in this filing. It should also be noted that the avoided cost assumptions and the models
21 used in this analysis are different from the models and avoided costs being used in other
22 proceedings in the state including any Energy Efficiency cost effectiveness, and the Permanent
23 Load Shifting proceedings.

1 **A. Tests**

2 The primary purpose of the cost-effectiveness tests are to measure and evaluate the cost
3 effectiveness of Demand Response (DR) programs in order to properly include these programs
4 as a resource option in the utility’s resource planning process. Historically, the Commission has
5 used a broad societal perspective to identify benefits and costs and to determine cost-effective
6 energy efficiency (“EE”) programs. This generally involves using the Total Resource Cost
7 (“TRC”) test from the Standard Practice Manual (“SPM”).

8 The TRC test is a broad test taking into account all the benefits to DR customers and
9 non-participating customers in terms of avoided generation costs (including line losses), avoided
10 transmission and distribution (“T&D”) costs, avoided energy costs, and environmental benefits.
11 On the cost side, this perspective includes all the costs associated with the DR program to both
12 participating and non-participating customers. The test ignores all equipment incentive
13 payments and subsidies that are transfers from non-participants to the DR program participants.

14 The TRC test is one of the tests reported as part of the determination of the cost-
15 effectiveness of energy efficiency programs. DR programs should use this same test for
16 measuring cost-effectiveness for purposes of resource planning to put the programs on an equal
17 footing with energy efficiency.

18 In the evaluation of demand response programs, SDG&E has also included the cost-
19 effectiveness from SDG&E’s perspective in the Program Administrator Cost (“PAC”) test.
20 Because the TRC test includes the customer cost as a part of the social costs, and because the
21 PAC test includes the incentive payment as a part of the program administrator cost, when the
22 customer costs equal the incentive payment, the two tests (the TRC and the PAC) have exactly
23 the same result. (In the current analysis, the required template assumes that the customer costs

1 are 75% of the incentive. This then yields a different result for the TRC and the PAC). Another
2 test included is the Ratepayer Impact Measure (“RIM”) which is reflective of the benefits and
3 costs to non-participating customers.

4 The last major test in the SPM is the Participant test. This test is most appropriate for use
5 in designing programs and setting customer incentives. The economic analysis from the
6 participating customer’s perspective is typically a business analysis of an investment decision.
7 The customer will look at the present value of expected future net benefits and decide whether or
8 not to participate in the DR program.

9 **B. Program Incentive Payments**

10 For purposes of cost effectiveness and as described in Section 3.H of the Demand
11 Response Protocols, the cost of the program incentive payments used in this analysis are based
12 upon the *expected* number of program calls and the expected duration of those calls. These
13 values are necessarily different from what is being requested in the budgets for these programs
14 which is based on the *maximum* expected number of calls and *maximum* duration of those calls.

15 **C. Portfolio Evaluation**

16 The cost effectiveness analysis is done on a program-by-program basis for those
17 programs requiring cost effectiveness tests for 2012 - 2014. These programs, plus the
18 administrative costs associated with the PTR program and the ET program, the costs associated
19 with measurement and evaluation of the Summer Saver program and the TI costs and benefits
20 associated with CPP-D are then added and cost effectiveness is calculated at the portfolio level.

21 **III. MODEL INPUTS**

22 While SDG&E was required to follow the protocols as described in Appendix A of
23 Decision 1-12-024 and the Commission adopted DR reporting template developed by E3 to

1 develop the cost effectiveness calculations for the tests described above, there are certain
2 elements of the model that can be adjusted by SDG&E for its specific programs. These
3 adjustments to the Template are described below.

4 **A. A Factor**

5 The A Factor is intended to represent the portion of capacity value that can be captured
6 by the DR program based on the frequency and duration of calls permitted. For DR programs
7 with constraints on their availability and how often they can be used, SDG&E uses a top 100
8 hours approach, a load-based approach based on publicly available data consistent with the 2010
9 Demand Response Cost Effectiveness Protocols. SDG&E has used the top 100 hours analysis in
10 prior General Rate Case Phase 2 proceedings as a proxy for the Loss of Load Expectation
11 approach. The A Factor varies by DR program based on the hours of availability and was
12 calculated based on monthly or annual callable hours, depending on the limits of the particular
13 program. The A Factor is higher for programs available more hours of the year, with a higher
14 number of calls per month or year and a higher maximum number of hours per call. In the
15 analysis, SDG&E based its A Factor on 2006-2008 historical data from the Avoided Cost
16 Calculator. The development of the A Factor used in the Cost Effectiveness evaluation for this
17 filing will be included in a detailed Work Paper.

18 **B. B Factor**

19 The B factor is the notification time factor. SDG&E has quantified only the relative
20 value of day-ahead versus day-of notification programs. In the ancillary services market, a DR
21 program with 10 minute start-up capability or less can earn revenues for being available if
22 needed. These revenues are part of the revenue from the CAISO market and are not considered

1 in the notification parameter. No adjustment is proposed for different day-of notification
2 periods.

3 SDG&E has provided for a discount to day-ahead programs based on potential CAISO
4 forecast errors and potential unexpected events. In a day-ahead DR program, the customer must
5 be notified the day prior to being called upon to reduce load. In most cases, forecasts will be
6 sufficiently close to actual outcomes, and the day-ahead program will provide as much value as a
7 day-of program. However, in cases where unexpected events occur or weather forecasts badly
8 miss the mark, a DR program's load reduction could be needed, but would not be available
9 because it was not called the day before. Similarly, market prices are based on market
10 participants' expectations of the next day prices, which in turn are based on expected demand
11 and supply for electricity. To the extent the forecast of market participants in the day-ahead
12 market significantly underestimates the next day's conditions, a DR program based on a price
13 trigger may not be called when day-of prices would have justified a program call.

14 Based on the data reviewed, forecast errors that were significant underestimates occurred
15 roughly 14 percent of the time. This error level would suggest a B Factor of .86. This factor has
16 only been applied to the CBP Day-Ahead program. All other programs have a B Factor of 1.0.
17 Work Papers will be provided on the details of these calculations.

18 **C. C Factor**

19 The C Factor is the program trigger factor. There are two ways a trigger affects the cost
20 effectiveness analysis. One way is through energy benefits. The more flexible a trigger, the
21 more times it is expected to be called and the more energy benefits will be derived from the DR
22 program. This translates the flexibility of the trigger to different strike prices; a less flexible
23 trigger is essentially a higher implicit strike price.

1 The second way the trigger flexibility affects the value is through the C Factor. This
2 factor measures the reduction in value compared to a CT because of lack of availability, not
3 through limitations on calls or availability, but because the trigger does not allow for calling the
4 DR program when it may be needed.

5 Given the flexibility of SDG&E's triggers to call both CAISO and local events, 100%
6 was assigned to the triggers for each of SDG&E's DR programs.

7 **D. D Factor**

8 Factor D represents the percentage of T&D capacity value that can be claimed by the
9 program being tested. The default value as prescribed in the Protocols is zero. In cases where
10 customers on the program have enabling technology that allows reliable long-term load
11 reduction, a value for Factor D was established. Of the programs tested, two provided enabling
12 technology: the Small Customer Technology Deployment ("SCTD") program, and the
13 Technology Incentives ("TI") program. For SCTD, 100% of the customers have enabling
14 technology and thus a value of 100% was used for Factor D.

15 Customers on the TI program receive incentives to install equipment that will support
16 Auto DR. These customers opt into SDG&E's Capacity Bidding Program ("CBP"), Critical
17 Peak Pricing ("CPP") rate, or DemandSMARTTM. For CBP Day-Of and DemandSMARTTM, it
18 was determined that approximately 12% of the forecasted MWs for the 2012 - 2014 program
19 cycle will come from customers with TI technology. Thus, a value of 12% was used for Factor
20 D when testing these programs. Similarly, a value of 8% was used for the CBP Day-Ahead
21 program. While the CPP program was not tested separately, the costs and benefits for the TI
22 customers opting into this program are included in SDG&E's portfolio cost effectiveness result,
23 and a D Factor of 100% was used for this case.

1 **E. E Factor**

2 The E Factor is the Energy adjustment factor and is composed of two parts. The first part
3 represents the increase electric prices due to the limitations on the days a DR program is likely to
4 be called. Instead of the Avoided Cost Calculator average price over all on-peak days in June
5 through September, the E factor adjusts for the DR program’s likelihood of being only called on
6 the higher priced days. The second part of the E factor is designed to account for the stochastic
7 nature of energy prices. As a result of an analysis on these two factors SDG&E has developed
8 an E Factor of 140% which has been applied to the energy benefits of all of the Demand
9 Response resource programs. As allowed in the protocols, justification for this value will be
10 provided in Work Papers. It should be noted that this value has a very small impact on cost
11 effectiveness.

12 **IV. OTHER ANALYSIS ASSUMPTIONS**

13 **A. Discount Rate**

14 The discount rate used in the model is the after-tax weighted average cost of capital. For
15 SDG&E, this is 7.3%. This percentage is taken from the avoided cost calculator and is not
16 considered a utility input for the purposes of this model. The discount rate is used in the model
17 to discount future costs and benefits to the current year.

18 **B. Measurement and Evaluation (M&E) Costs**

19 SDG&E has included M&E costs in the program budgets for the cost effectiveness tests.
20 The total M&E budget is \$5,115,099 for the three year program cycle. Of this amount,
21 \$3,515,099 is used in the actual cost effectiveness tests. The remaining amount (\$1,600,000) is
22 not used in the cost effectiveness tests and consists of the following: 1) \$875,000 is designated as
23 M&E for the Critical Peak Pricing rates; 2) \$650,000 is designated as M&E for the Peak Time

1 Rebate program; and 3) \$75,000 is designated as M&E for permanent load shifting. These rates
2 and programs are not tested for cost effectiveness in this filing.

3 Of the \$3,515,099 M&E budget used in the cost effectiveness tests, \$890,000 was
4 included in the cost for specific programs tested in this application (specifically, BIP, CBP and
5 SCTD). Additionally, \$1,150,099 for non program-specific M&E was allocated across each of
6 the resource programs tested, and the method used for allocation was the total program budget.
7 Of the remaining M&E budget used in the cost effectiveness tests, \$1,380,000 is designated for
8 EM&V for the Summer Saver program as a portfolio cost, and \$95,000 is designated for EM&V
9 of the TA/TI programs. The \$95,000 for TA/TI EM&V was allocated across the programs in
10 which TI customers enroll: CBP, CPP and DemandSMART™.

11 **C. Capital**

12 For programs with capital investments that are assumed to provide benefits beyond the
13 three-year program cycle, the investment was amortized over a ten year period and the resulting
14 allocation for the first three years was used in the cost benefit calculation as directed in the
15 Protocols. The programs that this applies to are the Small Customer Technology program and
16 the Technologies Incentives program.

17 For programs with minimal capital expenditure assuming to provide benefits limited to
18 the three-year program cycle, the investment was entered as an expense for each of the three
19 years. The programs that this applies to are the Base Interruptible Program and Capacity
20 Bidding Program.

21 **D. Treatment of Technology Incentives**

22 The Technology Incentives (“TI”) program does not provide direct benefits, but instead
23 provides enabling support for other programs. It was treated in the cost benefit calculations as

1 follows. The TI budget was allocated across three programs. The three programs into which
2 customers who participate in the TI program enroll are CBP, CPP and DemandSMART™. For
3 CPP, the costs and benefits of the customers forecasted to be on CPP as a result of participating
4 in the TI program are included as portfolio costs and benefits, since this rate is not explicitly
5 tested in this application. The forecasted MWs associated with TI customers enrolling in CBP
6 and DemandSMART™ and the corresponding costs from the TI budget were included in the
7 cost effectiveness tests for these programs.

8 The TI incentives used in the cost effectiveness tests were calculated as follows. For the
9 base incentive, the new MWs forecasted for the programs were multiplied by the incentive of
10 \$300 per kW. Only new MWs for each year were used as the incentive is paid only once upon
11 technology installation. A 15% inflation factor was added because historical EM&V results
12 have shown that actual impacts are less than indicated by the load shed tests upon which the
13 incentive payments are based. Please refer to the testimony of Kathryn Smith for details. These
14 incentive costs were treated as long-term capital costs in the cost effectiveness tests. An
15 additional incentive was calculated for TI customers on the CPP program. The additional
16 incentive consists of a \$30 per kW annual payment to the aggregator for continuing customers
17 staying on the program. This additional payment was treated as incentive payments in the cost
18 effectiveness tests.

19 **E. Permanent Load Shifting**

20 The Cost Effectiveness for Permanent Load Shifting (“PLS”) is not being addressed in
21 this application.

1 **F. Capacity Bidding Program**

2 SDG&E’s Capacity Bidding Program (“CBP”) consists of a Day-Ahead and a Day-Of
3 option. The budget for the CBP program was allocated across the Day-Ahead and Day-Of
4 options using the load impacts forecast for each option. Each of the CBP options has three event
5 products in which customers can enroll: one to four hours, two to six hours, and four to eight
6 hours. For the Day-Ahead option, only the one to four hour product has enrolled customers. For
7 the Day-Of option, it is expected that roughly 60% of CBP Day-Of customers will choose the
8 one to four hour product and the remaining 40% will choose the two to six hour product. Each
9 product has a different capacity payment price according to the applicable tariff, so when
10 calculating the incentives for the Day-Of option to be used in the cost benefit tests, a weighted
11 average of the two product prices was used. No costs were assigned to CBP Day-Ahead 2 to 6
12 hours or 4 to 8 hours as no customers enroll in these products. Similarly, no costs were assigned
13 to the CBP Day-Of 4 to 8 hour product.

14 The 60 / 40 weighted average of CBP Day-Of customers was also used in calculating
15 Factor A for the CBP Day-Of program. In particular, the factor was calculated for both the four-
16 hour option and the six-hour option and then a weighted average of the two results was used.

17 **G. Budget Exclusions**

18 As specified in the Protocols, the pilots were not included in the cost effectiveness tests
19 for this application. The pilots include Locational Dispatch, Residential New Construction and
20 Nonresidential New Construction.

21 Expenses related to IDSM bridge funding were also excluded from the cost effectiveness
22 tests. This includes expenses related to the Flex program, Residential Microgrid, the Technical

1 Assistance program, and the IDSM component of Educational and Outreach costs. Residential
2 Microgrid is also a pilot.

3 For the CBP, TI and DemandSMART™ programs, the incentive dollars used in the cost
4 effectiveness calculations are based on expected load impacts while the budgeted incentive
5 dollars are based on maximum events. The additional amount budgeted was not included in the
6 cost effectiveness tests.

7 In addition, as mentioned earlier in the subsection on EM&V costs, the budgeted EM&V
8 costs for the Critical Peak Pricing rates, the Peak Time Rebate program, and Permanent Load
9 Shifting were not included in the cost effectiveness tests. Finally, the allocation for system
10 support activities applicable to the Summer Saver program was not included as this program was
11 not tested for cost effectiveness for this application.

12 **H. Allocation of System Support Activities and Other Allocations**

13 A total of \$7,641,097 for system support activities was allocated across all the programs
14 in the demand response portfolio. The method of allocation was done as a percentage of total
15 program budget to the total DR portfolio budget.

16 In addition, the administration costs for Education and Outreach were allocated over the
17 resource programs tested. The same was done for EM&V costs that relate to general EM&V
18 rather than for specific programs as explained in the EM&V section above. The method of
19 allocation was also total program budget.

20 Administration costs for PTR and Emerging Tech were included as portfolio costs in the
21 cost effectiveness tests.

1 **I. Expected Events**

2 The expected event assumptions used in the cost benefit calculations were as follows: for
3 the BIP program, two events were assumed. For all other programs, nine events per year were
4 assumed.

5 **J. Energy Rates**

6 For the purpose of calculating customer energy savings, an average forecasted rate was
7 used. For residential customers, the average rate used was \$0.184 per kWh for 2011 and
8 escalated by 3% for each subsequent year. For small commercial customers, the average 2011
9 rate used was \$0.176, and for medium and large commercial and industrial customers the
10 average 2011 rate was \$0.139. The medium and large C&I average rate includes all energy
11 and demand charges that the customer would pay.

12 **V. RESULTS OF COST EFFECTIVENESS TESTING USING E3 TEMPLATE**

13 Table 1 is a summary of the results of the evaluation using the models and avoided costs
14 mandated in Decision 10-12-024 Attachment 1. As prescribed in those protocols and in the
15 Guidance Document issued Jan 21, 2011, all activities that support the programs in general but
16 are not program specific (e.g. IT infrastructure, measurement, evaluation and verification,
17 operations, management, marketing and other costs) have been allocated across programs as
18 described earlier in this Testimony and included in the costs associated with each individual
19 program.

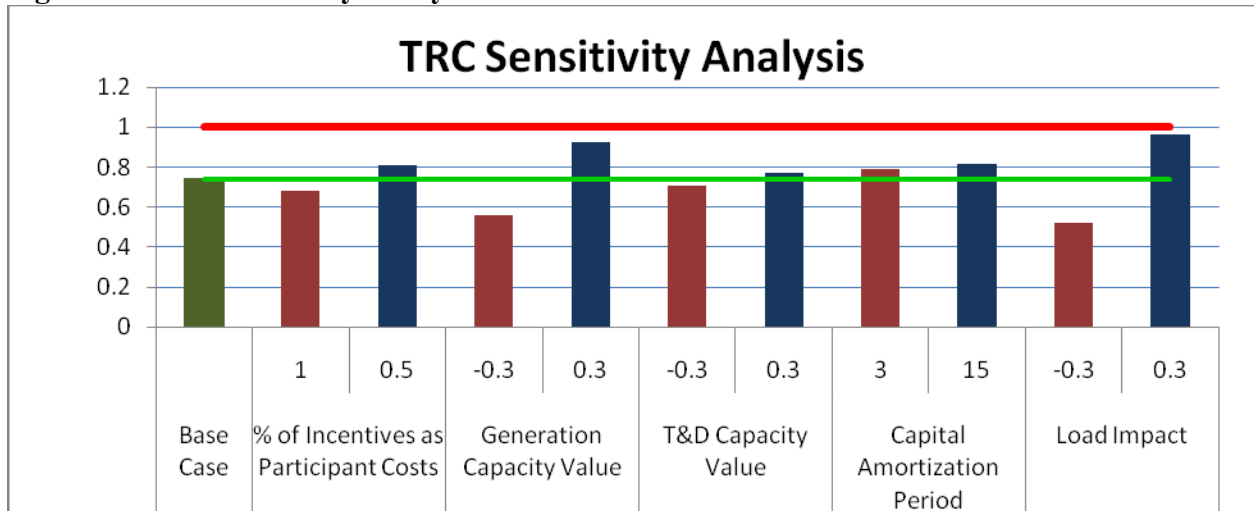
1 **Table 1: Results of Cost Effectiveness Tests**

	BIP	CBP: Day Ahead	CBP: Day of	SCTD	Demand SMART™	Portfolio
TRC	1.15	0.90	0.96	0.82	0.84	0.68
PAC	0.97	0.83	0.88	0.85	0.73	0.64
RIM	0.96	0.80	0.84	0.81	0.70	0.62
PCT	1.33	1.33	1.33	1.33	1.33	1.33
TRC Benefits¹	\$4.1	\$3.2	\$5.6	\$5.4	\$4.0	\$23.5
TRC Cost¹	\$3.6	\$3.5	\$5.8	\$6.6	\$4.8	\$34.6
TRC Net Benefits¹	\$0.6	(\$0.3)	(\$0.2)	(\$1.2)	(\$0.8)	(\$11.1)

2 ¹In millions

3 Figure 1 presents the results of the TRC sensitivity analysis in the DR Reporting
 4 Template. The figure shows how the portfolio TRC of 0.68 changes when certain assumptions
 5 are changed.

6 **Figure 1: TRC Sensitivity Analysis**



7
 8
 9 In Table 2, SDG&E has provided additional information which estimates the cost
 10 effectiveness of each individual resource program but without the burden of the unassigned
 11 overheads described above. This scenario eliminates the allocation of administrative overheads

1 which include labor costs for support personnel, ongoing maintenance costs for IT resources
 2 related to demand response programs, and new technology development for tracking and
 3 reporting of demand response programs. In addition, the costs for the DR specific Marketing
 4 and Education program for general EM&V, nonspecific to any program, were also omitted.
 5 These results give a better indication of the programs' cost effectiveness on a stand- alone basis.

6

7 **Table 2: Results of Program Tests Without Indirect Admin**

	BIP	CBP: Day Ahead	CBP: Day of	SCTD	Demand SMART™
TRC	1.38	1.10	1.16	1.16	1.15
PAC	1.12	0.99	1.04	1.21	0.96
RIM	1.11	0.94	1.00	1.14	0.91
PCT	1.33	1.33	1.33	1.33	1.33
TRC Benefits¹	\$4.1	\$3.2	\$5.6	\$5.4	\$4.0
TRC Cost¹	\$3.0	\$2.9	\$4.8	\$4.7	\$3.5
TRC Net Benefits¹	\$1.1	\$0.3	\$0.8	\$0.7	\$0.5

8 ¹In millions

9

10

1 **VI. QUALIFICATIONS**

2 My name is Kevin C. McKinley. My business address is 8335 Century Park Court, San
3 Diego CA. 92123. I am currently employed at San Diego Gas and Electric as the Supervisor of
4 Measurement and Evaluation.

5 I originally joined San Diego Gas and Electric (“SDG&E”) in 1978 and held a variety of
6 management positions in financial analysis, customer forecasting, fuel planning and marketing.
7 During the 1990s I was the Manager of Marketing Analysis for SDG&E where my
8 responsibilities included producing a series of regulatory filings for Demand Side Management
9 (“DSM”) forecasts, DSM earnings claims, and program measurement studies. I was heavily
10 involved in the development of the original Protocols used for measurement and evaluation in
11 California during the 1990s. I was a member and also Chairman of the California Demand Side
12 Management Advisor Committee (“CADMAC”) during part of this period.

13 I left SDG&E in late 1998 and consulted in the measurement and evaluation area for the
14 next several years. I rejoined SDG&E in April 2005. My current responsibilities include the
15 Measurement and Evaluation and Cost Effectiveness of DSM programs for both SDG&E and the
16 Southern California Gas Company for Energy Efficiency, Demand Response, and Low Income
17 programs. I am also a part-time instructor and have taught at several colleges and universities in
18 the San Diego area including San Diego State University, the University of San Diego,
19 University of Redlands and the University of Phoenix. I hold two masters degrees, one in
20 Economics and the other in Latin American studies, both from San Diego State University and a
21 Bachelors degree in Business Administration from Gonzaga University. I have previously
22 testified before this Commission.