BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the	)	**Docket No. U-100522**
	)	
Conservation Incentive Inquiry	)	**NW Energy Coalition's**
	)	**Reply to Responses to**
	)	**Consolidated Issues List**
	)	
	)	

In accordance with the May 13 Notice of Opportunity to File Written Comments, the NW Energy Coalition ("Coalition") respectfully submits the following reply to responses to the Commission's consolidated list of issues in this docket.

In the interest of brevity, we focus our reply on a select few issues or comments raised by other parties where we believe a response is warranted.[1] We do not use this reply to restate our main points from our June 4 submission to the Commission, nor do we use it to reply to all issues raised by other parties where we may have some disagreement.

Using an independent third-party to implement energy efficiency does not resolve concerns regarding lost margins.

Several parties referenced or recommended use of an independent third party similar to the Energy Trust of Oregon (ETO) to develop and implement future investor-owned utility (IOU) energy efficiency programs.[2] The Coalition advocated for the creation of ETO and strongly supports its mission and activities. We would support consideration of creating a similar entity in Washington.

We note for purposes of this proceeding, however, that transferring energy efficiency program implementation responsibilities from the IOUs to an independent third party does not obviate the need for mechanisms to address utility disincentives to conservation. An IOU still has a unique role in promoting energy efficiency, it still faces declining loads and associated revenues if energy efficiency programs are successful, and it still must cover its non-production costs. Creation of a third party administrator alone does not ultimately move IOUs any closer to a business model where company financial interests are aligned with customer and societal interests in maximizing energy efficiency. As concrete examples, administration of programs by an independent third party does nothing to remove a utility's incentive to oppose upgrades to energy efficiency codes and standards or to enable independently owned, clean distributed

[1] Lack of reply to the remaining comments and issues of other parties does not imply agreement with or endorsement of those points of view. In many cases, we see eye-to-eye with other parties, and in some cases, we agree to disagree at this time.

[2] Cost Management Services (CMS) Response at p. 1-2 and questions 5, 23; The Energy Project Response at question 2b; Public Counsel Response at ¶12-14; Industrial Customers of Northwest Utilities (ICNU) Response at §2.

generation. Increased energy use would still yield automatic financial rewards for shareholders and the fundamental causes of the IOUs' throughput incentive would remain unaddressed. Ultimately, use of an independent third party does not address the utility's attitudes or throughput incentive. Under the third-party model, the utility does not face the conflict between effectively administering energy efficiency programs and its throughput incentive, so it may focus fully on increasing profits by increasing sales.[3] And the disincentive to support effective codes, standards and consumer-driven measures remains.

It is also important to understand that the utility's active and positive cooperation with and promotion of the third party's efforts is critical to success. Without removing the utility's disincentive, moving the energy efficiency programs to a third party will not be as successful. The only way to ensure enthusiastic partnership over the long term is to align the IOUs' business model with energy efficiency. If the Commission decides to examine the advantages and disadvantages of pursuing third party implementation of IOU conservation, we recommend consideration of whether such a decision would remove utility disincentives to promote conservation.[4]

The Legislature established statewide greenhouse gas (GHG) emissions reduction limits; these limits apply to electric utilities and gas utilities.

RCW 70.235.020 sets GHG emissions reduction limits for Washington State. Question 14.5 in the Commission's Consolidated Issues List focuses on the state's ability to meet those limits if the link is removed between kilowatt-hours sold and financial returns for utilities. Given the narrow framing of that question around "kilowatt-hours sold," some of the responses from members of the gas utility industry indicate this is an electric industry-only issue.[5] We urge the Commission to broaden the scope of its inquiry regarding this question to include the effects of removing the link between therms sold and financial returns for utilities. Gas utilities and their customers contribute to GHG emissions and ultimately will face limits on those emissions; more aggressive conservation will reduce those emissions and help the state reach its mandatory limits.

In addition, the relationship between electricity use, natural gas use and transportation is complicated but important to understand for reducing GHG emissions. It may be that fuel substitution that can increase gas and/or electricity use is desirable. Without decoupling utilities on both the gas and electricity side may oppose such efforts if they see their loads on the "losing" side of the substitution. On the other hand, they may receive windfall profits from increased use (e.g., electric vehicles). While most discussion regarding decoupling has focused on lost revenues to utilities when loads decline, another benefit of decoupling is to protect customers if per-customer usage increases.[6]

[3] Regulatory Assistance Project, *The role of decoupling where energy efficiency is required by law*, September 2009.
[4] We note that creating a separate entity that receives funds from rates and invests directly in energy efficiency is not incompatible with authorizing a decoupling mechanism for the participating IOU.
[5] Northwest Industrial Gas Users (NWIGU) Response and Northwest Natural's (NWN) Response at question 14.5.
[6] We recognize this is a complex issue in the case of electric vehicles in that significant expansion of electric vehicles will require substantial distribution infrastructure upgrades.

Utility support is critical to the passage of new energy codes and standards.

Improved energy codes are the cheapest, most reliable and most equitable means to achieving long-term energy savings. Since 1980, energy efficiency has met approximately half the Northwest's new electricity demand.[7] Over the past 20 years, state building codes and federal and state appliance standards have accounted for over one-third of all savings in the region.[8] The Northwest Power and Conservation Council's Sixth Plan says codes and standards in combination with market transformation efforts and new initiatives will account for 40-45 percent of the 6,000 average megawatts of cost-effective efficiency identified in the Sixth Plan.[9]

Proposed new codes and standards require broad political support, technical expertise and the best available information regarding energy consumption patterns. Electric and natural gas industries are key to these efforts. Yet those utilities have a built-in disincentive to support changes in codes and standards that will further reduce the sale of their product. Several parties suggest the Commission not include reductions in load due to changes in codes and standards as part of a disincentive-removal mechanism.[10] We believe such a policy would undermine support and advocacy for changes to codes and standards, potentially leading to increased need for conservation program funding from ratepayers.

As a point of reference, we point the Commission to the rules adopted by the Department of Commerce in implementing I-937. WAC 194-37-080 (4)(c) ensures public utilities are not harmed in meeting their biennial targets as a result of passage of new codes and standards, enabling the utilities to count savings from those efforts in the biennium in which they become effective.[11] WAC 194-37-080 (5) allows public utilities to count savings from local building and/or local equipment codes and standards that are more stringent than the state's requirements. They can count those savings in the biennium in which they become effective as well as each biennium the local standards are enforced and achieve incremental savings above minimum state or federal codes and standards.

At a minimum, the Commission could consider including similar policy guidance for electric IOUs subject to I-937 (and for gas utilities where conservation targets may be established in the IRP process as required by WAC 480-90-238 or in conjunction with a disincentive-removal mechanism). We also recommend any disincentive-removal mechanism explicitly address reduced ability to recover non-production costs due to new energy codes and standards, though we recognize that debate will ensue over how best to measure those effects.

Decoupling is separate and distinct from straight fixed variable (SFV) rate design and lost margin recovery.

Thematically, we were pleased to note that parties generally distinguish between incentives and disincentive-removal mechanisms and the purpose of each, though some conjecture that an

[7] NW Power and Conservation Council, Sixth Power Plan, p. 1-10.
[8] *Id.*, p. 4-16.
[9] *Id.*, p. AP-2.
[10] NWIGU Response at Question 6e; Public Counsel Response at ¶38; ICNU Response at §4 p. 6.
[11] Subsequently, assumed savings from codes and standards will be removed from a utility's ten-year potential assessment and therefore its next biennial target.

incentive could be designed to replace the need for a mechanism such as decoupling.[12] However, we think it is important to distinguish between decoupling and other disincentive-removal mechanisms to ensure the parties are collectively using the same basic terminology.

Decoupling is not the same as SFV rate design or lost margin recovery, nor does it serve the same purpose.[13] Each of these mechanisms can be considered a disincentive-removal mechanism, but they function in different ways and have distinct advantages and disadvantages. Decoupling assures recovery of a pre-defined or formulaic distribution revenue requirement for fixed costs as authorized by the Commission, often with caps that bound pricing adjustments, and it precludes over-recovery. In contrast, lost margin recovery is far narrower in scope, assuring recovery of lost revenues net of avoided short-run variable cost due to specific programmatic energy conservation actions by the utility. SFV rate design uses a fixed charge to recover all costs that do not vary with sales volume, and has the effect of discouraging conservation by reducing a customer's ability to lower his/her bill. While SFV rate design may reduce utility disincentives, it simultaneously creates consumer disincentives for efficiency investments. A proposal by the National Regulatory Research Institute creates other problems.[14]

Comments specific to individual parties

We noted a few comments raised by other parties that deserve a brief reply here.

- Avista references potential advantages of capitalizing rather than expensing energy efficiency investments.[15] To the best of our knowledge, neither the statute nor the rules require an IOU to expense its conservation, and presumably a utility could propose to capitalize those investments instead. We note there are potential downsides to capitalizing energy efficiency, including potentially greater lag in cost recovery; greater competition among divisions within the utility for scarce dollars; risk of over-recovery for efficiency investments; and potentially less ability to borrow money to finance energy efficiency projects which do not have collateral akin to a supply-side project. On the other hand, the obvious advantage to capitalizing energy efficiency investments is to make those investments more comparable to supply-side investments through the opportunity to earn a profit.
- Avista also references a concept raised in its recent initial I-937 biennial target filing regarding carry-over of savings achieved from one biennium to the next.[16] We did not support Avista's proposal in that proceeding. As we discussed, conservation achieved in excess of a biennial target automatically reduces the utility's subsequent 10-year potential, thus already affecting the level of the subsequent biennial target.
- CMS proposes that large industrial customers should not be included in utility-sponsored energy efficiency programs.[17] We strenuously disagree. All customers benefit from

[12] See for example ICNU at §5.
[13] See for example NWN Response at question 1.
[14] *See* Hethie Parmesano, NERA Economic Consulting, "Electricity Journal debate: A response to Boonin's straight fixed variable 'feebate' rate design," *The Electricity Journal*, November 2009.
[15] Avista Response at questions 2b, 3e, and 23.
[16] *Id.* at question 16. The Company retracted that proposal from its final filing, approved by the Commission in Docket No. UE-100176.
[17] CMS Response at question 9.

acquisition of cost-effective energy efficiency; all should have the opportunity to participate in utility programs; and all should contribute to paying for these programs. There is abundant evidence that large industrial customers do not invest in energy efficiency using a utility-investment time horizon, and that immense energy efficiency benefits will be left unachieved if they are excluded. Stimulus program funding for industrial energy efficiency has identified many opportunities with one to two year payback periods, compared with a 20 – 30 year time horizon for utility supply investments. I-937 does not exclude the electric utilities from responsibility for achieving all cost-effective industrial energy efficiency, and full inclusion of these customers within the utility programs is the best way to assure that this statutory mandate is met.

- Puget Sound Energy (PSE) suggests that low-income households in its service territory consume the same amount of energy as an average household.[18] We question that presumption. As PSE correctly notes, the only identifiable group of low-income customers are those that have received bill assistance from the utility. Yet only a small percent of low-income households apply for assistance. Hence we have no data concerning the energy consumption patterns of the vast majority of PSE's low-income customers.
- The Energy Project proposes considering not having low-income households pay in their rates for utility-sponsored energy conservation or bill assistance programs.[19] Compared with the average residential customer, low-income households on average pay a higher percentage of their income for energy. And as discussed by The Energy Project, low-income households have difficulty accessing utility programs. We recommend considering other ways to resolve these concerns, such as enhancing utility efficiency programs for low-income, removing barriers to participation, addressing split incentives associated with implementing conservation in rental units, and generally being more aggressive in utilities' commitment to the low-income sector. The Commission also could consider rate design options that may be beneficial to low-income.[20]
- ICNU argues that decoupling provides a disincentive for utilities to control costs and improve customer satisfaction because utilities are indifferent to the amount of electricity they sell.[21] We believe the opposite is true. With decoupling, the utility no longer profits by increasing sales, so the only way it can profit is to increase the efficiency of its operations – the holy grail of regulatory lag.
- ICNU suggests decoupling is unnecessary because Washington utilities have a history of aggressively investing in conservation, and because electric utilities are subject to I-937.[22] We remind the Commission of the roller coaster of energy efficiency investments in Washington and the region over the past three decades.[23] Today's level of investment in energy efficiency may not be sustainable over the long-term if utilities' associated

[18] PSE Reply at question 12.
[19] The Energy Project Response at question 12.
[20] We understand one option being explored in a decoupling proceeding involving a utility with inverted block rates in New Mexico is to apply surcharges to the utility's top blocks but apply credits to the initial blocks. It would be interesting to analyze whether such a rate design would be helpful to low-income households.
[21] ICNU Response at §8.
[22] ICNU Response at §9.
[23] As one example, compare PSE's acquisition of approximately 0.5 aMW of energy efficiency in 1997 to its current target to acquire 71.0 aMW in 2010-2011.

financial conditions are not addressed in one way or another.[24] Decoupling is not the only way to address these. For example, the penalty provisions of I-937, if assiduously implemented, will help ensure achievement of the statutory mandate for full acquisition of cost-effective energy efficiency. But merely "trusting" that past results are a guide to future performance is baseless.

Conclusion

Again, the Coalition appreciates the opportunity to participate in this proceeding, and we hope the Commission moves forward with issuing specific guidelines of general applicability related to IOU incentive and disincentive-removal mechanisms. We will attend the next workshop on June 29 and would be happy to answer any questions at that time.

[24] We offer a similar response to Public Counsel's assertion in its Response (at ¶58) that "it is difficult to find evidence that any disincentive actually exists."