NRDC
THE EARTH'S BEST DEFENSE

NATURAL RESOURCES DEFENSE COUNCIL

July 14, 2010

Via Electronic Mail - records@utc.wa.gov

Mr. David Danner, Executive Director and Secretary
Washington Utilities and Transportation Commission
P.O. Box 47250
1300 S. Evergreen Park Drive SW
Olympia, WA 98504-7250

RE: Conservation Incentive Inquiry, Docket No. U-100522

Dear Mr. Danner:

Attached please find the Natural Resources Defense Council's Additional Comments in the above-referenced docket.

Sincerely,

Noah Long
Energy Program Attorney
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BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the	)	**Docket No. U-100522**
	)	
Conservation Incentive Inquiry	)	**Natural Resources**
	)	**Defense Council's**
	)	**Additional Comments**
	)	
	)	**July 14, 2010**
	)	

Introduction:

In accordance with the July 2 Notice of Opportunity to File Written Comments, the Natural Resources Defense Council ("NRDC") respectfully submits the following comments in this docket.

In its Notice, the Commission requests that interested persons indicate if they support, oppose, or are neutral to four specific policy options.

All of the options (even third party efficiency implementation) attempt to confront the problem created by the connection between utility fixed cost recovery and sales, though they do so with different impacts on customers and utilities. Only full decoupling effectively ends utility reliance on energy throughput as a means to recover (or over recover) fixed costs between rate cases. And only decoupling protects customers from paying lost margins from energy conservation, when utilities are simultaneously collecting "found margins" from sales increases beyond the level used for setting rates. Lastly, while we support a variety of third party efficiency implementers, we do not see the creation of such an organization in Washington as necessary or sufficient to eliminating the throughput incentive.

1) Full decoupling, including all declines and all increases in sales from any source.

NRDC fully supports a full decoupling mechanism and strongly recommends this as the preferred and only comprehensive approach to remove electric and gas utility "throughput" incentive. Decoupling effectively resolves concerns over fixed cost recovery from effective energy conservation programs, but its benefits do not stop there. A full decoupling mechanism severs the link between utility fixed cost recovery and electricity and gas sales. Such a severance is increasingly necessary in Washington, as customers are expected to meet more and more of their energy service needs from energy efficiency, rather than from increased energy generation. The Northwest Power and Conservation Council recommends the region acquire at least 1,200 average megawatts by 2014 from energy efficiency, and 5,900 average megawatts by 2030.[1] If

[1] Northwest Power and Conservation Council, *Sixth Northwest Conservation and Electric Power Plan*, February,

Washington is to pursue its share of this appropriately aggressive mandate, utilities, and customers must share the objective of minimizing energy sales- utilizing every tool available, including resource acquisition through conservation incentives, building codes, appliance standards, market transformation, innovation, and education.

Washington has successfully implemented full decoupling mechanisms for both electric and gas utilities and we believe that this mechanism remains the best approach to ensure that all Washington utilities neither over nor under recover their allowed revenue.[2] The Washington Utilities & Transportation Commission (WUTC) dealt with many of the same issues when it first adopted a full per-customer decoupling mechanism for Puget Power in 1991. As the Commission determined at that time:

> [T]he revenue per customer mechanism does not insulate the company from fluctuations in economic conditions, because a robust economy would create additional customers and hence, additional revenue. Furthermore, the Commission believes that a mechanism that attempts to identify and correct only for sales reductions associated with company-sponsored conservation programs may be unduly difficult to implement and monitor. The company would have an incentive to artificially inflate estimates of sales reductions while actually achieving little conservation.[3]

The Commission implemented Puget's revenue-per-customer cap by "set[ting] up a deferred account allowing a reconciliation of revenue and expenses that would be subject to hearing and review."[4] In its initial review of the mechanism it adopted two years earlier, the Commission in 1993 "accept[ed] the parties representations" that the revenue-per-customer cap had "achieved its primary goal – the removal of disincentives to conservation investment," and concluded that "Puget has developed a distinguished reputation because of its conservation programs and is now considered a national leader in this area."[5] Based on these findings, the Commission granted a three-year extension of the revenue-per-customer cap.[6] In 1995, as part of a litigation settlement

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2020, p. 10-2.

[2]As early as 1990-91, A Collaborative process recommended a fully decoupling mechanism for Puget Sound Power and Light. The Commission subsequently adopted a full decoupling mechanism and successfully implemented, with great strides made by Puget in efficiency promotion for a number of years, until it was suspended in a larger rate reform effort. NRDC has participated in UTC proceedings to advocate full decoupling several times in the last 20 years, including in UE 921262 (See the May 1993 Direct Testimony of Ralph Cavanagh); UE-030311/UE-0304023 (See the May 6, 2003 Comments of Ralph Cavanagh on the UTC Review of Least Cost Planning and Procurement Rules); UE-032065 (See the July 8, 2004 Direct Testimony of Ralph Cavanagh and the October 6, 2004 Brief of the Natural Resources Defense Council); and UE-050684 (See the November 2, 2005 Direct Testimony of Ralph Cavanagh). NRDC does not consider the Avista pilot mechanism a full decoupling mechanism, since its true-ups only partially correct for under- or over-recovery of the utility's authorized nonfuel costs.

[3] Docket No. UE-901183-T, Third Supplemental Order (April 10, 1991), p. 10. The Commission also determined that the mechanism did not constitute retroactive ratemaking, and that it was "fair, just and reasonable" even though it did not perfectly match costs and rates: "even under the current system of ratemaking, costs and rates will diverge immediately following implementation of a rate change." Id. at p. 10.

[4] Id., at p. 10.

[5] See Washington UTC, Eleventh Supplemental Order, Docket No. UE-920433, p. 10 (September 21, 1993).

[6] See id. , p. 10 (concluding that "the PRAM/decoupling experiment should continue for at least another three-year cycle").

proposal intended to create no precedent, Puget and several other parties filed a request with the Commission to terminate a complex system of rate adjustment mechanisms that included the revenue-per-customer cap (along with other rate adjustment mechanisms, e.g., a controversial approach to allocating risks of hydropower fluctuations). The Commission approved that request, but the proposal itself expressly reserved the right of all parties to bring forward in the future "other rate adjustment mechanisms, including decoupling mechanisms, lost revenue calculations, [and] similar methods for removing or reducing utility disincentives to acquire conservation resources."[7] This proceeding could be characterized as part of a very long public conversation initiated by that order.

Many of the questions raised in the June 29, 2010 workshop about various mechanisms to ensure that energy conservation efforts do not undermine fixed cost recovery focus on the problem of potential shifts in risk to or from customers. A full per-customer decoupling mechanism without weather adjustment ensures that utilities can recover their allowed fixed costs while protecting customers from utility over recovery when sales exceed expectations because of "found revenues," whether they result from extreme weather events, increased consumption due to changes in technology, economic changes or demographic shifts. Decoupling simply "trues-up" the difference between expected and actual sales and has the potential to either slightly increase or decrease rates. The most recent and comprehensive analysis of electric and gas decoupling mechanisms showed that the resulting rate adjustments have been both upward and downward, and are almost invariably very small: on the order of seven cents a day for the average household's electric bill and five cents a day for its natural gas bill.[8]

Furthermore, the frequency of rate cases does not resolve the issue of efficiency impacts on fixed cost recovery. Regardless of how often a utility comes in for a rate case, customers and utilities spend most of their time between rate cases. As a result, a utility without decoupling will always benefit from over recovery if sales are higher than anticipated in the last rate case and always be harmed by sales lower than anticipated.

NRDC supports the use of utilities customer count as a proxy for shifts in fixed costs between rate cases and accordingly we recommend a "per customer" full decoupling mechanism. While no proxy for changes in fixed costs between rate cases will be perfect, we agree with the Commission's earlier cited conclusion back in 1991 that customer count is at least as good as the status quo (which assumes that energy use tracks fixed costs). Attempt to further complicate a decoupling mechanism to account for potential new cost increases could create perverse incentives. For example, while NRDC fully supports and anticipates the roll out of an electric vehicle fleet, the Commission should not maintain the throughput incentive in whole or in part for the promotion of electric vehicles. Doing so could put utilities in the unfortunate position of benefiting from the most inefficient electric vehicles. If the Commission wants to motivate

[7] Docket No. UE-921262, Joint Report and Proposal Regarding Termination of the Periodic Rate Adjustment Mechanism (April 20, 1995).
[8] Pamela Lesh, "Rate Impacts and Key Design Elements of Gas and Electric Utility Decoupling: A comprehensive Review," The Electricity Journal, Vol. 22, Issue 8, Sept. 2009, pp.65-71.

utility engagement in vehicle electrification, it could provide financial incentives tied to the number of vehicles added to the system, or the amount of gasoline displaced by their use.

2) **Lost margin adjustment for declines in sales due only to company sponsored conservation efforts.**

A lost margin recovery mechanism is an attempt at a more limited approach to ensuring fixed cost recovery, but in fact tends to present greater risk to customers. For example:

- Customers pay utilities for energy saved through conservation, programs, but are not protected from utility over-recovery of fixed costs through "found margins" when sales increase.
- Customers can vastly over pay for energy savings. If utilities play even a modest role in meeting the Council's Sixth Regional Plan conservation targets, recovery of lost margins could be a large and escalating cost that would require repeated attention in rate cases as multi-year programmatic savings and their lost revenues accumulate rapidly over time.
- Utilities are encouraged to maximize claimed savings from their own programs and to obstruct (or certainly not to promote) savings from other highly cost effective energy saving strategies like building codes, appliance standards and market transformation.

On one occasion NRDC provisionally supported lost margin recovery mechanisms as a partial and imperfect stopgap mechanism, even as we have continue to urge full decoupling as the best long-term solution.[9] However, while such a mechanism can provide some limited help to utilities in confronting the impact of successful energy efficiency programs, it does not address the fundamental and perverse tie between energy sales and fixed cost recovery and it can get quite expensive and controversial. As discussed above, a per-customer decoupling mechanism protects customers from utility over-recovery of fixed costs, while ensuring that utilities' ability to recover their approved fixed costs is not undermined by necessarily aggressive and growing energy conservation efforts on all fronts.

Furthermore, NRDC cautions against the view that good measurement and verification alone can make a lost margin recovery mechanism preferable to a full decoupling mechanism. As discussed at the workshop, improving measurement and verification in the Northwest and elsewhere is an imperative given the growing need for energy savings from efficiency, but even a

[9] In Montana, NRDC supported a temporary lost revenue requirement mechanism as an incomplete solution with the recommendation that the Commission conduct a full review of the mechanism in two years. "NRDC believes that a decoupling mechanism provides broader support for DSM efforts, including non-utility DSM programs. In addition, NRDC thinks the incentives implicit in a lost revenue adjustment are incomplete. However, [NRDC, District XI Human Resource Council and the Renewable Northwest Project] support adopting NorthWestern's proposal in this case for a trial period to deal immediately with the utility's concerns about lost T&D revenues. Part of our proposal involves exploring alternative ways of dealing with the DSM lost revenue problem over the next two years and bringing back to the Commission the results of that analysis. In addition, our proposal involves "truing-up" the projected lost revenues associated with DSM programs with the results of an analysis of actual savings. We believe that for the next two years, the lost revenue adjustment proposal that NorthWestern has made is a reasonable initial step from which a great deal can be learned." Response Testimony of Thomas Power on behalf of District XI Human Resource Council, Natural Resources Defense Council and the Renewable Northwest Project. Department of Public Service Regulation, Before The Public Service Commission of the State Of Montana, Docket No.s D2003.6.77, D2004.6.90, p.9, Lines 15-27.

lost margin recovery mechanism combined with the best measurement and verification is still only an incomplete imperfect solution because it does not sever the link between utility fixed cost recovery (including the possibility of substantial over-recovery) and energy sales.

3) **Attrition adjustment based on the results of an attrition study.**

NRDC has no objection to the use of attrition adjustments as part of decoupling mechanisms, as a way to adjust authorized non-fuel revenue requirements between rate cases (as indicated earlier, the utility's customer count can be used for the same purpose). But an attrition mechanism without full decoupling will fail to break the link between the utility's financial health and its retail sales.

An attrition mechanism generally escalates the revenue requirement by inflation minus a productivity offset each year between a rate case. It is typically a part of the rate case decision and can also be a part of a decoupling mechanism. Even with an annual general rate case and/or forward-looking attrition adjustment, conservation savings within a given year (utility-sponsored and not) will still cause the utility financial harm when savings result in lower than expected sales. Alone, this mechanism simply does not address the issue at hand.

4) **An independent conservation provider (*i.e.* similar in concept to the Energy Trust of Oregon).**

NRDC fully supports independent conservation providers including the Energy Trust of Oregon. The Energy Trust of Oregon, Wisconsin's Focus on Energy, Efficiency Vermont, New York State Energy Research and Development Authority and the Northwest Energy Efficiency Alliance are excellent examples of effective energy efficiency organizations with a variety of relationships with utilities and customers. Each of these organizations interacts with or includes utilities and in all cases, utility commitment to energy efficiency affects the ability of the organization to achieve energy efficiency savings. It is noteworthy that Oregon, Vermont, Wisconsin and New York have all embraced decoupling for electric utilities, because all recognize the importance of utilities as engaged partners in achieving energy efficiency results.

However, while we are fully supportive of a variety of models for energy efficiency promotion and delivery, the discussion of energy efficiency delivery is separate and distinct from the pertinent discussion at hand in this proceeding. Regardless of who administers energy efficiency programs, utilities will continue to have a large and important role in achieving energy efficiency savings. The Oregon Public Utility Commission's decoupling order for Portland General Electric recognized the fundamental link between utilities and energy efficiency:

> "[W]hile the parties do not disagree that relying on volumetric charges to recover fixed costs creates a disincentive to promote energy efficiency, they contend that decoupling is unnecessary because, with the ETO running energy efficiency programs in PGE's service territory, the Company has limited influence over customers' energy efficiency decisions. We find this position unpersuasive, because PGE does have the ability to influence individual customers through direct contacts and referrals to the ETO. PGE is also able to affect usage in other ways, including how aggressively it pursues distributed generation

and on-site solar installations; whether it supports improvements to building codes; or whether it provides timely, useful information to customers on energy efficiency programs."[10]

Full per-customer decoupling provides an opportunity to end utility reliance on energy throughput as a means to ensuring recovery of fixed costs and opens the door to utility support and partnership with all avenues of energy efficiency delivery, whether from a third party program implementer, a partner organization or a government agency.

Furthermore, while third party efficiency organizations can be highly effective, so can properly motivated utilities and there is justification for delaying efficiency implementation in Washington to await the creation of a new organization. Washington can and must do more to promote energy efficiency in the coming years and a decoupling mechanism will make that transition more feasible for customers and utilities alike.

Conclusion:

NRDC appreciates the opportunity to participate in this proceeding. We recommend the Commission now move forward with proceedings to consider the appropriate decoupling mechanism for each Washington utility.

Dated: July 14, 2010

Respectfully submitted,

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[10] Order No. 09-020, Docket UE 197, Jan. 22, 2009, at 27.