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Decision 82 08 014 AUG 4 - 1982 ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY for authority, among other things, to increase its rates and charges for electric and gas service. (Electric and Gas)	Application 60153 (Filed December 23, 1980)

(See Appendix A for appearances.)

OPINION ON FURTHER HEARING ON CONSERVATION PERFORMANCE INCENTIVES

In Decision (D.) 93887 (December 3, 1981) we invited all gas and electric corporations to file comments on proposed procedures for adjusting earnings based on conservation achievements. Pacific Gas and Electric Company (PG&E), Southern California Gas Company (SoCal), Southern California Edison Company (Edison), San Diego Gas & Electric Company (SDG&E), California Energy Commission (CEC), and the Commission staff filed comments March 1, 1982. A prehearing conference was held before Administrative Law Judge Robert T. Baer on March 15. Hearings began March 25 and ended April 8. During the eight days of hearing, 10 witnesses testified, sponsoring 10 exhibits. The proceeding was submitted May 26, 1982, when briefs were filed.

The Proposal

Reproduced here in full is the proposed procedure to adjust earnings for conservation performance[1] found on pp. 148-148a of D.93887:

[1] While this is a convenient starting point, it should be recalled that CEC proposed an incentive program in earlier hearings. (D.93887, p. 147a.)

"<u>Establish conservation targets for 1982</u>.

"In this proceeding, PG&E projected that its proposed conservation programs and budget would generate lifecycle savings of 4.1 billion kWh and 957 million therms. After eliminating savings attributed by PG&E to the ZIP and RCS programs (which are the subject of a separate decision) and those attributed to programs recommended for reduction or elimination in this decision, projected savings for PG&E's adopted conservation program are 2.4 billion kWh and 335.1 million therms, on a lifecycle basis. We proposed these conservation levels as the 1982 targets.

"We note that not all conservation estimated by the company in A.60153 would generate conservation earnings under this proposal. Many programs may not produce measurable, tangible conservation under our evaluation methodology. We expect this will encourage management to focus resources on those programs that permit clear evaluation of the company's performance.

"<u>Establish a 'dead band' around the targets</u>.

"The conservation targets should be at the center of a dead band within which no earnings adjustments would be made. We propose to establish a dead band of 5% above or below the targets.

"<u>Establish a schedule of earnings adjustments</u>.

"If the company demonstrates conservation results within the dead band for gas or electric savings, no adjustment should be made for either gas or electric earnings. If the company is unable to demonstrate performance to the lower limit of the dead band, earnings should be reduced in two ways. Gas earnings should be reduced by $750,000 plus an additional 85 mills for each therm below the lower limit of the dead band. Electric earnings should be reduced by $750,000 plus an additional 12 mills for each kWh below the lower limit of the dead band. If the company is able to demonstrate conservation performance above the upper limit of a dead band, earnings should be increased in like amounts.

"The earnings adjustments of $750,000 at either end of the dead bands recognize success or failure of the programs in achieving minimum expectations. This adjustment is made at approximately one-half the amount of earnings adjustments outside the dead band. The electric earnings adjustment outside the dead band is intended to meet the so-called non-participant [test] of cost-effectiveness. Approaching deregulation of natural gas prices renders this test inapplicable to gas conservation programs. The gas earnings adjustment outside the dead band has, therefore, been kept to approximately 10% of current marginal costs. Compared to current estimates, the gas earnings adjustment is about 5% of the cost of gas to be delivered by increasingly costly Alaska Natural Gas Transportation System.

"<u>Establish a maximum level for the adjustment</u>.

"We would limit the potential exposure of ratepayers and the utility during the initial year of operation by limiting the total size of the adjustment. We propose to adjust PG&E's earnings by no more than $10 million up or down based on 1982 performance. The level and desirability of ceilings in future years should be discussed by the parties.

"<u>Provide for annual review</u>.

"We propose to adjust earnings for conservation performance in the annual Conservation Financing Adjustment (CFA) proceeding. The company's CFA application should include savings attributable to the company's programs developed in accordance with the evaluation methodology dismissed [sic - discussed] herein [and] a calculation of any earnings adjustment that is in order."

The Issues

The issues to be resolved in this proceeding are:

1. Should a procedure to provide management incentive for achieving conservation be adopted for PG&E?

2. If so, is the procedure set out above, that proposed by CEC, or some other procedure sound? (D.93887, p. 147c.)

The two issues are not mutually exclusive. One of the factors which must be considered to answer the first question will be the feasibility or soundness of the proposed programs. If, for instance, therms and kilowatt/hours saved during a given period cannot reliably or economically be attributed to PG&E's conservation programs (as opposed to other forces beyond its control) then an incentive program may be unworkable and inappropriate.

Positions of the Parties

Toward Utility Rate Normalization (TURN) believes that no incentives are needed for further conservation. TURN asserts that "it seems absolutely ridiculous...after all the havoc created because ...of the December 30 decision, to even consider adding five cents to any utility bill...." (PHC-4:185.)

The City and County of San Francisco (San Francisco) also opposes the conservation incentive programs advocated in this proceeding. In its closing argument San Francisco stated:

> "...there is an incentive in normal utility rate making for efficiency, the utility can earn more by spending less through efficiency.
>
> "But the ratepayers' rates don't go up when that happens. This brilliant plan mandates that when efficiency occurs, rates go up.
>
> "As a matter of fact, we showed on the record that really they go up two ways because of ERAM (Electric Revenue Adjustment Mechanism) they go up in the incentive plan itself and in an ERAM rate increase." (Tr. 84:10135.)

The Policy and Planning Division witness for the Commission staff (staff) recommended that the Commission not adopt an incentive mechanism at this time, neither as proposed in D.93887, nor as described by the Energy Conservation Branch (ECB) witness, nor as described by the CEC witness. The ECB sponsored an incentive plan, but the witness did not recommend it to the Commission because: "I have seen nothing that proves that they're (incentives are) needed." (Tr. 78:9788.)

In its brief the staff summarized eight reasons why an incentive plan is neither necessary or appropriate. They are:

"1) The Commission's objective in proposing a conservation incentive program is poorly defined.

"2) The record suggests that an incentive plan may not be necessary.

"3) An incentive plan may in practice produce unintended results, stimulating activity which will in no way increase energy savings, and altering utility conservation programs in unintended respects.

"4) It will be difficult to establish conservation incentive program targets which provide any real incentive to utilities to increase conservation achievement.

"5) Whether or not an incentive program will increase energy conservation is subject to serious question.

"6) Any conservation incentive plan reviewed in this proceeding will increase administrative costs to the Commission, utilities and interested interveners.

"7) An energy conservation incentive plan would have few advantages over the Commission's present practice of reviewing utility conservation programs in each general rate case and imposing a rate of return penalty for poor performance.

"8) Whether an energy conservation incentive program would be cost-effective is subject to doubt." (Staff brief, p. 2.)

PG&E does not believe that conservation incentives will assist its return to financial health. It believes that there are sufficient regulatory, market, and managerial incentives for it to make its conservation programs efficient, productive, and accountable, and thus, another incentive is not needed.

Edison's witness stated its position as follows:

"Considering present realities, rewards and penalties may be inappropriate. Rewards could be perceived by our customers as unprecedented expense; penalties could be perceived by our bond and shareholders as an unjustified risk; and the process could be perceived by the utility and its regulators as redundant regulation." (Exhibit 198.)

By "present realities" Edison refers to the adverse consumer reaction to rate increases recently experienced in California. In light of this statewide response, Edison does not believe that additional revenues given it as a reward for conservation achievement would gain the approval of the ratepayers.

SDG&E also believes that California utilities have sufficient incentives to promote cost-effective conservation programs and that an additional incentive is not necessary. It argues that supposed disincentives to the promotion of conservation by utilities do not exist because:

1. Estimates of sales in rate proceedings incorporate the effect of conservation.

2. ERAM, adopted in SDG&E's 1982 rate case, and the gas Supply Adjustment Mechanism (SAM), protect the utility's revenues from the effects of conservation and unusual weather and also protect the ratepayer if revenues exceed utility requirement.

3. The utility tradition of providing help to customers naturally leads to aggressive conservation programs as long

as they are helpful or cost-effective to the ratepayers. This is particularly true with SDG&E, which has high rates.

4. Conservation will help reduce the need for new power plants and thus minimize consumer rates.

SDG&E believes that an incentive program would be viewed by consumers as rewarding utilities for doing what they should already be doing and in fact have been ordered to do by the Commission.

SoCal supports the concept of a conservation reward but does not support the procedure proposed in D.93887. SoCal believes that current conservation programs are successful and will saturate many markets in a few years. It proposes a program to reward utilities for conservation achievements in difficult-to-penetrate markets, such as low-income and rental housing, solar applications, cogeneration, and heat recovery. SoCal's proposal would: provide rewards but not penalties; evaluate programs on the basis of specific hardware installations; and define markets, reward limits, reward increments, and other variables in each utility's general rate case.

CEC urges the Commission to adopt its incentive program. CEC believes that an incentive structure should:

1. Cover all conservation programs.
2. Have incentives large enough to focus management and stockholder interest on a utility's conservation performance.
3. Encourage efficiency in operation and management of utility conservation programs.
4. Encourage expansion of cost-effective conservation programs beyond current budget levels.

The Sierra Club, in its brief, supports the position of CEC.

Sierra Pacific Power Company (SPPC) urges the Commission to find that conservation incentive programs designed to reward or punish utilities for either meeting or failing to meet specific conservation goals (1) are unnecessary, (2) would only add an expensive, unjustified layer of regulation, and (3) would, if rewards are given to the utilities, result in an adverse public reaction to these programs.

Having summarized the positions of the parties, we will now discuss whether a conservation incentive program is necessary or appropriate.

Necessity for a Conservation Incentive Program

That we should carefully explore the issues of necessity and appropriateness is indicated by the diversity of views on conservation incentives expressed by commissioners concurring in D.93887. While one commissioner believes that "[w]e are approaching closure on incentives for conservation," another expects "a careful and thorough analysis of both the appropriateness of conservation incentives for utilities and the viability of each incentive proposal offered at hearing." Another commissioner observes that "[t]he reward-penalty mechanism proposed in this case today for utility conservation efforts is an important step toward further analysis of such an approach" but warns that "[e]xcessive or poorly designed rewards could have the perverse effect of making inherently economical approaches overly costly to consumers."

Only CEC, echoed by Sierra Club, and SoCal argue that conservation incentives are necessary. In his prepared testimony the CEC witness makes two statements on why conservation incentives are necessary:

> "An incentive program which rewards PG&E for good performance both in conservation programs within the existing budget levels and for cost-effective program expansion will serve to promote the goals of rate stabilization and improved utility finances by focusing management and stockholder attention on conservation performance." (Exhibit 199, p. 1.)

This statement assumes that the attention of management and stockholder is either not focused or is inadequately focused on conservation performance. CEC's factual basis for that assumption is not stated. The statement also shows that CEC is interested not merely in efficient use of budgeted conservation funds but also in expansion of conservation activity beyond the programs for which funds were budgeted in D.93887. However, the statement does not explain why its incentives proposal is necessary or appropriate but merely concludes that it is.

In his second statement the CEC witness explains why he believes that conservation incentives are more productive than simply ordering the utility to act and penalizing it if it does not, as follows:

> "A regulatory policy based on setting and monitoring minimum standards for utility performance is served by ordering action and penalizing the utility if the action is not taken. However, such a policy gives the utility no regulatory incentive to move beyond the minimum standard.
>
> "In addition, Decision 93887 considered and rejected detailed CPUC oversight of specific utility conservation programs and instead allows PG&E discretion to do what it believes necessary to achieve maximum energy savings within its budget and other broad limits set by the CPUC. A conservation incentive program would promote increased conservation efforts and complement the policy of reducing the day-to-day regulatory burden by providing rewards to management if results are achieved and penalties if they are not. Because of the major savings to ratepayers that result from cost-effective conservation, PG&E should be given some targets, even while being given more regulatory flexibility to attain them." (Exhibit 199, pp. 4-5.)

Again, the goal of an incentive program could be to encourage efficiency in existing programs or to impel the utility into new activities beyond those assumed in D.93887. In any event the concern of the first paragraph is with regulatory incentives; other kinds of incentives are not mentioned. In the second paragraph CEC asserts that a conservation incentive program would complement the policy of reducing the day-to-day regulatory burden. To the contrary, a new conservation incentive program will more likely diminish the flexibility we granted to management in D.93887 to administer its conservation programs; this could disrupt long-term development of conservation programs by concentrating management's attention or coping with the incentive program and trying to ensure that the Commission adopts goals it can achieve (and be rewarded for). And the additional regulatory burden of administering such a program appears to be significant both for the utility and for our staff.

The question whether conservation incentives are necessary must be answered after analyzing the evidence on incentives and disincentives for conservation that may now apply to utilities. In the words of PG&E's witness, "...there are already sufficient regulatory, market, and managerial incentives for PGandE to make its conservation programs efficient, productive and accountable." (Exhibit 196A, p. 3.) What then are those incentives?

PG&E first mentions that it is already subject to intensive regulatory oversight of its conservation program. It files detailed plans for conservation activities each December 1 and submits equally detailed reports on accomplishments each March 31. Its programs, plans, and results are then vigorously scrutinized in rate and related proceedings. PG&E, for instance, filed 17 volumes of workpapers to support its $72 million conservation program request in this proceeding. Four PG&E conservation witnesses testified and were cross-examined over a seven-day period.

If after this vigorous examination, PG&E's efforts do not meet the requirements of the Commission, then proposed expenses can be disallowed or rate of return penalties can be imposed.

PG&E also argues that since conservation and load management are integral parts of PG&E's long-term load forecasting and resource plan, decreasing the energy supply from these sources by failing to achieve forecasted conservation would necessitate substituting higher cost energy from either purchases in the short run or through capital investment in the long run. It follows, according to PG&E, that it has considerable incentive to ensure that its conservation programs produce the amounts of energy savings projected.

Edison argues, and the evidence is undisputed, that conservation is a desirable method of reducing the need for capital-intensive generation, transmission, distribution, and storage projects. Thus, the utilities have an incentive to promote conservation to avoid or postpone these capital-intensive projects.

In addition to those existing incentives for utilities to promote conservation just mentioned, the utilities argue that the recent establishment of ERAM has eliminated what has traditionally been considered to be a major disincentive to conservation, i.e. decreasing revenues from lower sales. Now that there is a formal mechanism in place to adjust the rates to account for declining sales, that traditional disincentive no longer exists.

Is An Incentive Plan Appropriate?

Several of the parties argued that an incentive program involving rewards would not be well-received by the ratepayers because it would be viewed as rewarding utilities for doing what they are already expected to be doing. Several witnesses cited the public's reaction to recent large rate increases as evidence that the citizenry and its representatives are currently sensitive to rate increases. In effect, the Commission, it is argued, should preserve its limited goodwill with the public by exercising restraint in cases, such as this one, involving elective rate increases.

Some parties testified that an incentive program involving penalties would establish another element of risk to those who invest in or lend to the utilities. Any additional risk would then be reflected in the cost of capital to the utilities and their ratepayers. The utility experts uniformly testified to the adverse reaction of the financial community to the incentive proposals involving penalties. No rebuttal evidence was proffered.

The utilities argue that an incentive program will increase administrative burdens of the Commission staff. Such a program would involve the setting of new priorities for the staff. For if it spends more time on incentives, it must spend less time on other programs, given constant levels of staffing and at a given budget. Additional sets of hearings may also be required to administer an incentive program. Annual targets for conservation will provide a fruitful area for litigation, but there is good likelihood that those targets will be no more accurate than sales forecasts have been in the recent past. In addition, targets must be based upon the prior year's savings analyzed as if no incentive system were in place. This will add another imponderable to the process of setting targets.

Even before targets are set it would be necessary for the utility and the staff (and perhaps other parties) to agree upon per unit life cycle energy savings for each kind of conservation transaction (or measure taken by a customer). This process, all parties agree, would involve determining on a program-by-program basis:

1. What constitutes a transaction.
2. How a transaction would be defined.
3. The acceptable method (whether actual counting or the appropriate estimating process) for counting the numbers of each kind of transaction.
4. The energy savings assumptions per transaction.

Though complex and technical in and of itself, that process should be further refined to reflect that the potential life cycle savings and numbers of transactions per program are dependent in part on factors beyond the utility's control, such as weather and the economy. If equity factors[2] were to be injected into the process, further complications would arise, all leading to potential differences of opinion and lengthy hearings to resolve those differences.

On the issue of administrative burden and cost the staff summarizes the evidence and arguments as follows:

> "At a minimum annual proceedings would be required (1) to determine an appropriate annual energy savings goal for each utility taking into account the different characteristics of each utility service territory and changing conservation penetration levels, and (2) to determine whether an economic reward or penalty is appropriate for each utility, and if so, the appropriate amount of such penalty or reward. The complexity of such an undertaking should be apparent. The Commission could not possibly hope to reduce administrative costs by adopting any energy conservation incentive proposal considered in this proceeding. Costs it would seem will unavoidably increase." (Staff brief, pp. 13-14.)

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2 By "equity factors" we mean the equal sharing of conservation benefits among customer classes. For instance, the energy savings credit could be increased for more socially desirable programs.

The staff raises another issue that bears on the question of appropriateness. That is the question of the goal we seek to reach in implementing an incentive program. The staff rightly observes that in D.93887 we alluded to at least three potential goals without selecting one of them as primary. Those goals are:

1. Stimulating greater efficiency and productivity in utility conservation programs. (D.93887, pp. 147 and 720.)
2. Expanding conservation efforts. (Ibid, pp. 147 and 147a.)
3. Increasing utility management's accountability for conservation expenditures. (Ibid, pp. 147 and 147a.)

Different programs may well be indicated by different goals. Certainly the programs offered by the parties differ because they seek to accomplish different objectives. CEC is primarily interested in expanding conservation programs and expenditures. The staff believes that the Commission's goal is to promote greater efficiency and productivity in existing utility conservation programs and has, accordingly, offered a program designed to foster that goal. SoCal believes that if the Commission wishes to implement an incentive program, it should abandon the complex program under which it operated in 1981 and put in place a simple program designed to promote the installation of conservation hardware in difficult-to-penetrate markets, e.g. low income.

In deciding upon an appropriate goal, we see immediately that CEC's goal conflicts with D.93887. While in that decision we reduced PG&E's proposed conservation expenses, CEC would now have us authorize additional expenditures by letting the upper level float (presumably through a balancing account), limited only by the utility's judgment of their cost-effectiveness. We are not willing to retreat so abruptly from limits we established only last year.

Moreover, if it were our goal to expand utility conservation programs, there are probably better ways to do it than the one suggested by CEC. As the staff suggests, the rewards proposed by CEC would be taxable income to the utilities. Thus, ratepayers would be required to pay \$2 in rates for every \$1 in additional earnings rewarded to utilities! A less expensive way to expand utility conservation programs would be simply to increase authorized funding for such programs. Even the CEC witness agreed that it would be a better buy for the ratepayer to pay \$1 directly for conservation program expenses than to pay \$2 to provide a \$1 after-tax reward.

The goal suggested by SoCal also has problems. Were we to limit incentives to hard-to-penetrate markets, we might inordinately focus management's efforts on those markets to the probable neglect of markets where conservation could be fostered more easily and perhaps more cost-effectively. We do not suggest that utility conservation efforts in hard-to-penetrate markets will necessarily be less cost-effective than the alternatives; indeed, the multi-family housing market offers an example of an apparently rich field of conservation which has been insufficiently addressed. We have previously made clear our concern that the utilities devote substantial efforts to reaching the hard-to-penetrate multi-family, low-income, and innovative technology markets. Such initiatives as PG&E's recent proposal of a direct weatherization component to its zero-interest (ZIP) program (A.82-07-035, filed July 16, 1982) indicate that utilities are responding to our concerns. We believe it is too early to conclude that more costly management incentives are needed to provide adequate motivation for utility action in this area. Our periodic review of utility conservation programs will indicate whether an appropriate balance is being achieved and will offer means of redressing any imbalance.

The third potential goal of an incentive program is to increase utility accountability for conservation expenditures. The staff asserts that the Commission's proposal in D.93887 seems unnecessarily complex and likely to be ineffective in reaching that goal. The staff believes:

> "Utility management is already responsible to shareholders for earnings and financial performance. Under existing Commission practice earnings are already at risk depending upon conservation program performance. If a utility's conservation programs are not found vigorous, imaginative and effective the company's rate of return

> may be reduced by the Commission. Whether substituting a conservation incentive plan for existing Commission practice will increase the accountability of utility managers for earnings and conservation program performance is questionable. Even if it will, it would seem that there must be less cumbersome ways of accomplishing the same result." (Staff brief, p. 5.)

The most appropriate of the four goals mentioned above is that of stimulating greater efficiency and productivity in PG&E's conservation. However, upon reconsideration of that goal in light of the evidence produced in these supplementary hearings, we conclude that there is little to recommend it beyond pure theory. Certainly we have not found PG&E's overall conservation program inefficient, unproductive, or inadequate; rather, in D.93887 at p. 145 we expressed satisfaction with PG&E's conservation efforts, noting that "all parties have agreed that PG&E has been the acknowledged leader in the field of conservation." And at p. 113 we concluded:

> "In D.84902, we first announced we would evaluate the 'vigor, imagination, and effectiveness' of the conservation efforts of PG&E when determining PG&E's rate of return. In this proceeding, it has been made clear that no penalty is in order."

The staff asks, rhetorically: If PG&E's present conservation efforts are satisfactory, are additional regulatory incentives to promote conservation necessary? As we have indicated earlier the overwhelming preponderance of the evidence indicates that they are not necessary. For this reason and for other reasons indicated in the preceding discussion, we conclude that none of the proposals for conservation incentive plans should be implemented at this time.

Findings of Fact

1. Utilities now have economic and regulatory incentives to promote conservation.

2. Conservation provides an opportunity to increase short-term profits by avoiding or postponing new, capital-intensive supply projects.

3. Under existing Commission practice, where the vigor, imagination, and effectiveness of utility conservation programs are reviewed in each general rate case, rate of return may be reduced if conservation efforts are found inadequate.

4. The record does not demonstrate that the proposed incentive programs would provide any greater incentives than existing economic and regulatory incentives.

5. ERAM and SAM eliminate disincentives for utilities to promote conservation.

6. The proposed incentive programs would conflict with our policy to allow management greater flexibility in administering funds budgeted for conservation programs.

7. The proposed incentive programs would be likely to cause utilities to stress conservation programs with easily measured, short-term energy savings in easy-to-penetrate markets, and to deemphasize programs with long lead times, high expense, or more difficult-to-measure savings.

8. The proposed systems of rewards and penalties could lead to the manipulation of conservation goals, rather than to productive conservation efforts.

9. Setting accurate conservation goals is extremely difficult because customer conservation response is motivated by many different factors, including: energy prices and utility rate levels, economic conditions, weather, general conservation ethics, federal and state tax credits and deductions, mandatory appliance and building standards, and financing terms and availability.

10. No witness was able to state precisely what a utility might do in response to the proposed incentive programs to increase the efficiency and productivity of their existing conservation programs.

11. The proposed incentive programs would increase administrative costs because hearings to establish annual conservation goals, to value energy savings for each utility conservation program or transaction, or to evaluate utility performance for the purpose of conferring rewards or imposing penalties would be likely.

Conclusions of Law

1. The proposed conservation incentive proposals are neither necessary nor appropriate at this time.

2. No conservation incentive plan, beyond that already in place, should be implemented for PG&E.

SUPPLEMENTAL ORDER

IT IS ORDERED that a conservation incentive program for the Pacific Gas and Electric Company is not adopted, and this phase of Application (A.) 60153 is closed. A.60153 remains open for the consideration of electric rate design issues, which are in rehearing.

This order becomes effective 30 days from today.

Dated August 4, 1982, at San Francisco, California.

JOHN E. BRYSON
President
LEONARD M. GRIMES, JR.
VICTOR CALVO
PRISCILLA C. GREW
Commissioners

I will file a concurring opinion.
/s/ LEONARD M. GRIMES, JR.
Commissioner

Commissioner Richard D. Gravelle, being necessarily absent, did not participate in the disposition of this proceeding.

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

Joseph E. Bodovitz

Joseph E. Bodovitz, Executive Director

APPENDIX A

List of Appearances

Applicant: Daniel E. Gibson, William H. Edwards, Steven F. Greenwald, and Gail A. Greely, Attorneys at Law, for Pacific Gas and Electric Company.

Interested Parties: David J. Gilmore and John S. Fick, Attorneys at Law, for Southern California Gas Company; John Bury, David Barry, III, Richard Durant, Jim Lehrer, and Clyde Hirschfeld, Attorneys at Law, for Southern California Edison Company; Thomas J. Graff, Attorney at Law, by Daniel Kirshner, for Environmental Defense Fund; Graham & James, by Boris H. Lakusta, David P. Marchant, Thomas J. MacBride, and Ann C. Pongracz, Attorneys at Law, for Sierra Pacific Power Company; Sylvia Siegel, for Toward Utility Rate Normalization; Michael Paparian, for Sierra Club; George P. Agnost, City Attorney, by Leonard Snaider, Deputy City Attorney, for City and County of San Francisco; Robert E. Burt, for California Manufacturers Association; Gregg Wheatland and Dian Grueneich, Attorneys at Law, for California Energy Commission; John R. Asmus, Jr., Attorney at Law, for San Diego Gas & Electric Company; Joseph E. La Buda, for California Tea Party; Nancy Ciane, for herself; Steven F. Hirsch, Attorney at Law, for Natural Resources Defense Council; and John W. Witt, City Attorney, by William S. Shaffran, Deputy City Attorney, for City of San Diego.

Commission Staff: Edward W. O'Neill, Attorney at Law, Bruce DeBerry, and George Amaroli.

(END OF APPENDIX A)

A.60153
D.82-08-014

COMMISSIONER LEONARD M. GRIMES, JR., Concurring:

While I concur in the decision not to adopt a conservation incentives program at this time, I have several concerns that must be expressed to avoid misinterpretation of my action today.

Last October, I issued a proposal to make rather significant changes in our approach to regulation. A conservation incentives mechanism was among the changes I suggested adopting. My concurrence that we not adopt such an approach today is not based on a retreat from my views expressed at that time. Rather, I believe we must work to replace the current regulatory practices with schemes that reflect the world of today and the future.

I have become particularly concerned about the conflicting signals to the utilities that some of our decisions seem to cause. As we have found in OII 82-04-02, our investigation of the incentives in the ECAC procedure, even well thought out programs can create unforeseen conflicts. Until we have had an opportunity to consider changes in the ECAC that would hopefully result in a single, central incentive I am concurring that it is premature to adopt a separate incentive for conservation. Fuel and conservation are to interrelated to look at them separately

Candidly, I have reached this conclusion without much help from the record. Despite our pleas in D.93887 for the development of a full record and for innovative ideas, I found the presentations of our staff and of the companies to be unimaginative.. Arguments in opposition to the concept (and all but the California Energy Commission were opposed) were more impressive in weight than in substance and basically a plea to remain with the status quo. My disappointment with the result of this supplementary proceeding confirms my often expressed feeling that Commission procedures do not provide for the kind of creativity needed to cope with the future.

Finally, our rejection of conservation incentives today leaves some unresolved problems before us. Market penetration of low income and renter markets with conservation programs has been unsatisfactory. While steps are being taken to improve penetration of the low income markets through direct weatherization programs, renters are still largely beyond the reach of current utility programs. These are the classic non-participants that my fellow commissioners are concerned with and we will have to redouble our efforts in these areas.

I also harbor a continuing sense of unsureness in measuring utility performance in the conservation area. We have previously relied on the best efforts of our overworked staff to get the most bang for ratepayer dollars in conservation. Now we are allowing substantially more discretion to utility management, a step which I have strongly advocated. Yet without some form of profit incentive to management coupled with reduced Commission involvement forced by budget constraints can we guarantee the efficiency and efficacy of utility conservation programs to our ratepayers?

LEONARD M. GRIMES, JR., Commissioner

San Francisco, California
August 4, 1982

Moreover, if it were our goal to expand utility conservation programs, there are probably better ways to do it than the one suggested by CEC. As the staff suggests, the rewards proposed by CEC would be taxable income to the utilities. Thus, ratepayers would be required to pay $2 in rates for every $1 in additional earnings rewarded to utilities. A less expensive way to expand utility conservation programs would be simply to increase authorized funding for such programs. Even the CEC witness agreed that it would be a better buy for the ratepayer to pay $1 directly for conservation program expenses than to pay $2 to provide a $1 after-tax reward.

The goal suggested by SoCal also has problems. Were we to limit incentives to hard-to-penetrate markets, we might inordinately focus management's efforts on those markets to the probable neglect of markets where conservation could be fostered more easily and perhaps more cost-effectively. We do not suggest that utility conservation efforts in hard-to-penetrate markets will necessarily be less cost-effective than the alternatives; indeed, the multi-family housing market offers an example of an apparently ~~rich~~ field of conservation which has been insufficiently addressed, ~~thus far has gone untilled due more to paucity of imagination than to lack of potential~~. KL We have previously made clear our concern that the utilities devote substantial efforts to reaching the hard-to-penetrate multi-family, low-income, and innovative technology markets. Such initiatives as PG&E's recent proposal of a direct weatherization component to its zero-interest (ZIP) program (A.82-07-035, filed July 16, 1982) indicate that utilities are responding to our concerns. We believe it is too early to conclude that more costly management incentives are needed to provide adequate motivation for utility action in this area. Our periodic review of utility conservation programs will indicate whether an appropriate balance is being achieved and will offer means of redressing any imbalance.

Findings of Fact

1. Utilities now have economic and regulatory incentives to promote conservation.

2. Conservation provides an opportunity to increase short-term profits by avoiding or postponing new, capital-intensive supply projects.

3. Under existing Commission practice, where the vigor, imagination, and effectiveness of utility conservation programs are reviewed in each general rate case, rate of return may be reduced if conservation efforts are found inadequate.

4. The record does not demonstrate that the proposed incentive programs would provide any greater incentives than existing economic and regulatory incentives.

5. ERAM and SAM eliminate disincentives for utilities to promote conservation.

6. The proposed incentive programs would conflict with our policy to allow management greater flexibility in administering funds budgeted for conservation programs.

7. The proposed incentive programs would be likely to cause utilities to stress conservation programs with easily measured, short-term energy savings in easy-to-penetrate markets, and to deemphasize programs with long lead times, high expense, or more difficult-to-measure savings.

8. The proposed systems of rewards and penalties could lead to the manipulation of conservation goals, rather than to productive conservation efforts.

9. Setting accurate conservation goals is extremely difficult because customer conservation response is motivated by many different factors, including: energy prices and utility rate levels, economic conditions, weather, general conservation ethics, federal and state tax credits and deductions, mandatory appliance and building standards, and financing terms and availability.

SUPPLEMENTAL ORDER

IT IS ORDERED that a conservation incentive program for the Pacific Gas and Electric Company is not adopted, and this phase of Application (A.) 60153 is closed. A.60153 remains open for the consideration of electric rate design issues, which is in rehearing.

This order becomes effective 30 days from today.

Dated AUG 4 1982, at San Francisco, California.

JOHN E. BRYSON
President
LEONARD M. GRIMES, JR.
VICTOR CALVO
PRISCILLA C. GREW
COMMISSIONERS

I will file a concurring opinion.
Leonard M. Grimes, Jr.
Commissioner

Commissioner Richard D. Gravelle, being necessarily absent, did not participate in the disposition of this proceeding.