BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Examine the Commission's Energy Efficiency Risk/Reward Incentive Mechanism	R.09-01-019 (Filed January 29, 2009)

COMMENTS OF THE UTILITY REFORM NETWORK ON PROPOSED SCENARIOS AND ASSUMPTIONS FOR CALCULATING ENERGY EFFICIENCY PROGRAM RESULTS

Marcel Hawiger, Energy Attorney
Cynthia Mitchell, Energy Economics, Inc.
Consultant to TURN

THE UTILITY REFORM NETWORK
115 Sansome Street, Suite 900
San Francisco, CA 94104
Phone: (415) 929-8876 ex. 311
Fax: (415) 929-1132
Email: marcel@turn.org

April 20, 2010

COMMENTS OF THE UTILITY REFORM NETWORK ON PROPOSED SCENARIOS AND ASSUMPTIONS FOR CALCULATING ENERGY EFFICIENCY PROGRAM RESULTS

Pursuant to the direction and schedule in the Assigned Commissioner's Ruling of April 8, 2010, the Utility Reform Network (TURN) files these comments on Proposed Scenarios.

Summary

TURN recommends that for purposes of identifying the "range of possible scenarios" that should be used in the Evaluation Reporting Tools (ERT) database to determine the reasonable range of possible outcomes of the incentive true-up process, the Commission should at a minimum add the following policy scenarios:

- A "cost inflation" scenario that increases the value of all incremental measure costs by 10% to account for the impacts of inflation between 2003 and 2007 and the fact that measure costs have not been verified;
- A "non-HIM measure" scenario that decreases net savings by 10% to account for the fact that the "evaluated" scenarios only adjusted data for certain "high-impact" measures; and
- A "sunk incentive" scenario that accounts for the fact that since there is no longer a claw-back provision, the first two interim incentive payments are now a sunk cost that can be included on the cost side of the equation.

The Commission should also direct Energy Division to produce a scenario that combines the results of the three policy assumptions discussed above.

TURN also suggests that the transfer of risk, as originally envisioned in D.07-09-043 from shareholders to ratepayers, warrants a recalculation of the scenario outputs in the RRIM calculator with the use of lower sharing rates. It is our understanding that the DRA may address this issue.

Discussion

The "Assigned Commissioner's Ruling on Process for True-Up of Incentive Earnings," issued on April 8, 2010 ("ACR"), sets out a framework for resolving the true-up of the Risk/Reward Incentive Mechanism for energy efficiency programs that will determine whether utilities deserve additional shareholder incentives as a 'reward' for program performance in 2006-08, or whether they have already been over-rewarded by the two prior interim payments; though any shareholder 'risk' has largely been eliminated since the utility does not have to reimburse ratepayers for unearned profits as long as their programs have resulted in some positive net benefits to ratepayers.

The RRIM incentive mechanism was structured so that in theory utilities would earn rewards if they meet certain savings targets, there would be no rewards within a deadband of performance, and utilities would be penalized if their performance fell below 65% of their targets. The Commission has repeatedly relaxed various requirements and processes originally adopted in D.07-09-043 in order to ensure timely payouts to utilities for energy efficiency activities, irrespective of the validity of the underlying numbers. However, as the last and final protection against unwarranted and unjustified payments, the Commission has repeatedly upheld that there would be a final true-up process based

on using verified *ex post* data.[1] Such a process was supposed to mitigate the fact that the utilities were freed from the risk of returning any overpayments, should the true-up results find that program benefits were lower than previously calculated, and that the first interim payment was based on utility self-reported input parameter numbers.

The Commission has now modified the final true-up process to eliminate verification and updating of measure costs, based on the concern that such an update could delay final payments past calendar year 2010.[2] Thus, the final Energy Division verification report (entitled the "2006-2008 Energy Efficiency Evaluation Report") will calculate "net benefits" of utility programs by updating only the "benefits" side of the equation, but not the "cost" side of the same equation. Those net benefits numbers will flow directly into the calculations of shareholder incentives that will be presented in Energy Division's "2006-2008 Risk Reward Incentive Mechanism Scenario Analysis" report.

The Assigned Commissioner's Ruling emphasizes that the assumptions, calculations and inputs of the RRIM mechanism as verified by the Energy Division have

---

[1] See, for example, D.08-12-059, p. 16-17 ("To further reduce the risk of overpayment, we also amend the framework as it relates to the ex post true-up for the 2006-2008 period. In D.08-01-042 the Commission determined that if the IOUs earned interim payments in a given program cycle, but the ex post true up for that cycle finds that the IOUs' performance falls within the deadband, they would continue to achieve earnings at the 9% shared savings rate applied to the fully trued-performance earnings basis. Given that we are relying on utility-submitted data as the basis for determining incentive amounts for this interim claim we think it is reasonable for the 2006-2008 period to remove this provision, and, in effect, reinstate the deadband for the ex post true up for this cycle. In the event the ex post true-up reveals that the IOUs should not have received anything, this will prevent further overpayment.");

[2] D.10-04-004 (modifying D.09-12-045 to remove the requirement for an independent verification of utility-reported incremental measure costs values.)

generated "controversy and delay" which the Commission wishes to avoid. Thus, the Commission wishes to finalize the true-up based on "simplified assumptions or metrics" that do not require "potentially unproductive and lengthy debate over the entire universe of data points across all portfolio measures associated with specific measure-level parameter values used in the ERT Input Files."[3]

For this reason, the ACR suggests that the true-up process, including a mandatory settlement conference to attempt to reach a consensus position, should be based on identified scenarios "already embedded in the ERT," as well as other potential policy scenarios. The ACR invites parties to "provide any additional recommendations on policy assumptions that should be identified for consideration in producing ERT scenario runs, together with proposed values for those parameters."[4]

The ACR provides a list of nine scenarios that are apparently already "embedded in the ERT application tools." These nine scenarios comprise three main categories. Two scenarios (Nos. 1 and 2) are based entirely on utility-reported input values without any updates or verification. Three scenarios (Nos. 3-5) include partial verification of installation rates and unit energy savings. And four scenarios (Nos. 6-9) include various permutations of net savings using Energy Division's "evaluated" numbers for key input parameters.

It appears that Scenario No. 7 most closely matches the verified true-up scenario that was originally envisioned in D.07-09-043 and D.09-12-045, prior to the elimination of cost true-up in D.10-04-004. Thus, the additional scenarios recommended by TURN

---

[3] ACR, April 8, 2010, p. 2-3.
[4] ACR, April 9, 2010, pp. 9 and 11, Ordering Paragraph 1.

should use Scenario No. 7 as the underlying basis, although our recommended assumptions could be applied to any (or all) of the enumerated scenarios.

Regrettably, the scenarios presented in the ACR stack all the cards in the utility's favor. The ACR maintains that the RRIM is broken and that we need "a process that upholds standards of integrity in measuring energy savings while providing more transparency and reducing the minutely detailed complexity" of the RRIM calculations.[5] The ACR has directed parties to negotiate a settlement without arguing about the "entire universe of data points across all portfolio measures associated with specific measure-level parameter values (i.e., NTG, UES, EULs, installation rates) used in the ERT Input Files."[6] But the ACR has then recommended the use of scenarios that bracket only one-half of the possible outcomes, on the half that favors the utility. This cannot be the basis for settlement discussions or for an outcome that "upholds standards of integrity."

The ACR includes scenarios that use Energy Division verified numbers, but without any verification of costs. The ACR then includes scenarios that use only utility-reported numbers. We have already devoted stacks of paper documenting why the use of numbers based on data from the 1990's to calculate key input parameters is totally indefensible. The Commission has in previous decisions already warned the utilities that it made little sense to use net-to-gross ratios derived from pre-2003 programs to calculate net savings results for 2006-2008.

Without repeating these arguments and assumptions, TURN emphasizes that there are a number of reasonable scenarios that will likely result in much lower – and more

---

[5] ACR, p. 2.
[6] ACR, p. 5.

accurate! - net savings and net benefit results than those calculated in any of the included scenarios. Such scenarios would thus result in lower incentives, no incentives, or potentially even penalties.

Since the Commission does not desire parties to argue about individual inputs into the ERT spreadsheet, TURN suggests that some of the key concerns regarding the validity of the true-up process might be addressed by including the following as additional scenario runs that could be easily integrated in the ERT spreadsheet:

- A "cost inflation" scenario: The Commission decided that Energy Division should not update incremental measure cost data due to the potential time delay from such a verification process. For at least the more costly measures,[7] the cost data used by the utilities has input parameters based on cost numbers 5 to 10 years old. It is reasonable to *assume as a matter of policy and fact* that such costs have escalated, at a minimum based on inflation. As a simplified metric, TURN suggests using an inflation estimate of 2% per year over a five-year period (2003-2007) to adjust costs.[8] Such a metric result in an approximate inflation increase of 10%. Thus, this adjustment is most simply applied by increasing the cost numbers by 10% on a total portfolio basis in the ERT.
- A "non-HIM measure" scenario: Another change to the true-up process made to provide timely payments was the elimination of verification of the benefits

[7] See TURN Comments on the PD Modifying the Requirement for Verification of Incremental Measure Costs, R.09-01-019, March 29, 2010.
[8] We would not oppose calculating a total escalation based on actual CPI escalators for the relevant time period. The data is easily obtainable, and the utilities routinely use such data to escalate forecasts or historical costs to provide data in real dollars.

from all measures, so that Energy Division verified only the "high impact" measures (HIM).[9] While TURN understands that this was a reasonable shortcut to save time, it is *reasonable to assume* that such a shortcut results in an overestimate of net benefits. In order to account for this shortcoming, a scenario should be conducted that decreases net savings by 10% to account for additional savings adjustments to non-high impact measures.[10]

- A "sunk incentive" scenario: The Commission agreed that shareholder incentives represent a true economic cost for purposes of calculating program cost effectiveness, but decided that those incentives amounts should not be included *on a forecast basis* in the PEB calculation.[11] However, in making that determination the Commission relied on the assumption that actual incentive costs would be unknown until after the fact, since there was a claw-back provision in the final true-up. For this reason, the Commission concluded that "until the final earnings claim is authorized for a particular program cycle, we will also need to estimate the total cost of shareholder incentives in evaluating portfolio cost-effectiveness for that cycle." However, because the claw-back provision has been eliminated, the first two interim payments[12] to

---

[9] ED Draft 2006-2008 Energy Efficiency Evaluation Report April 15, 2010, ES 2.4 Evaluation Findings, p. viii, "[Per the HIM approach,] approximately 85% of the reported kwh, kW and therms were included in the direct evaluation of gross savings."

[10] The basis for the 10% calculation is as follows:

(1) ED ex post total IOUs' net savings (4,089 GWh) divided by IOUs' total gross claimed savings (12,242 GWh) = 0.66 (ED EE Evaluation Report, Table 23, p.96).

(2) Non-HIM savings of 15% multiplied by 0.66 = 10%.

[11] D.07-09-043, Sec. 10.1.

[12] The first two interim payments totaled approximately $144 million.

the utilities are now a known sunk economic cost. The already authorized interim payments should thus be included in the cost component to calculate a reduced net benefits amount.

Since the changes adopted in order to simplify the true-up process have reduced shareholder risk and increased ratepayer risk, TURN suggests that the RRIM results be calculated by using a lower sharing rate in the RRIM calculator. TURN believes that the DRA might recommend a specific reduction to the sharing rate. Such a result does not really require a new scenario but takes the output of the ERT scenarios and changes the sharing rate in the RRIM calculator.

April 20, 2010

Respectfully submitted,

By: *__/S/ Marcel Hawiger__*
Marcel Hawiger, Energy Attorney

THE UTILITY REFORM NETWORK
115 Sansome Street, Suite 900
San Francisco, CA 94104
Phone: (415) 929-8876, ex. 311
Fax: (415) 929-1132
Email: marcel@turn.org