BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Reform the Commission's Energy Efficiency Risk/Reward Incentive Mechanism.	R.12-01-005 (Filed January 12, 2012)

COMMENTS OF THE UTILITY REFORM NETWORK ON THE PROPOSED EFFICIENCY SAVINGS AND PERFORMANCE INCENTIVE (ESPI) MECHANISM PROPOSED FOR 2013-2014

TURN
THE UTILITY REFORM NETWORK
Lower bills. Livable planet.

Marcel Hawiger, Staff Attorney
Cynthia Mitchell, Energy Economics, Inc.

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 26, 2013

TABLE OF CONTENTS

LIST OF TABLES

COMMENTS OF THE UTILITY REFORM NETWORK ON THE PROPOSED EFFICIENCY SAVINGS AND PERFORMANCE INCENTIVE (ESPI) MECHANISM PROPOSED FOR 2013-2014

Pursuant to the direction and schedule in the "Assigned Commissioner's Ruling Soliciting Comments Regarding Efficiency Savings and Performance Incentive Design for Energy Efficiency 2013-2014 Portfolio" ("ACR"), dated April 4, 2013, the Utility Reform Network ("TURN") respectfully provides the following comments concerning the proposed Efficiency Savings and Performance Incentive ("ESPI") mechanism proposed in the ACR.

1. TURN Generally Supports the Proposed ESPI as an Alternative to the Prior Energy Efficiency Incentive Mechanism, and Recommends Two Modifications

The mechanism proposed in the ACR results in a maximum potential shareholder award of $159 million over two years based on the results of four metrics, as summarized in Table 1 below:

Table 1: Summary of ESPI Payments as Proposed in ACR

	Cap as % of Budgets	Primary Metric	Max Payment
Management Fee - Non-resource programs	3%	$250 million proposed non-resource budget	$7,491,944
Management Fee - Codes and Standards	10%	$25 million proposed C&S budget	$2,575,441
Ex Ante Compliance Performance Award	2%	Detailed Metrics re Timeliness and Quality of Presentations	$29,797,779
Ex Post Savings Performance Award (Target Scenario)	8%	Amount of savings compared to unit coefficients based on goals and budgets	$119,191,114
Total 2013-14 Payment (Target Scenario)			**$159,056,278**

TURN supports many of the principles and outcomes proposed in the ACR. While TURN originally supported using verified *ex post* results to measure utility performance for purposes of any shareholder awards,[1] TURN has over the years modified our position to prefer a simpler management fee model that does not rely *ex post* analyses. Linking *ex post* analyses with utility profits has introduced significant controversy and dispute between utilities and Energy Division over EM&V activities and results, to the detriment of program review and program design.

Nevertheless, TURN appreciates that ideally "performance incentives" would reward utilities for actual savings based on *ex post* analyses of results, showing how much energy savings can really be attributed to utility actions over the program period.

TURN is not sanguine that the proposed mechanism can work smoothly; however, the ACR takes three significant steps to promote the potential success of an *ex post* mechanism. First, the ACR adopts a linear incentive calculation that eliminates penalties or large step changes in rewards, thus minimizing (or essentially eliminating) utility risk. Second, the ACR continues an award, first introduced for the 2010 program year, that provides for a significant payment based on utility compliance with EM&V *ex ante* review processes. Third, the ACR uses actual "savings" rather than "net benefits" as the measure of performance. This third step requires an *ex post* calculation of savings and associated parameters, but at least eliminates disputes concerning the calculation of measure costs and avoided costs.

Thus, TURN supports the proposed ESPI for 2013-2014 with the following proposed modifications:

- The TRC "adder" should be eliminated, as it only reintroduces the problems eliminated by going to a "savings" model. Instead the ESPI should include an adder for reducing the percentage of program funds spent on non-incentive activities in order to maximize program participation and program benefits.
- The savings-based award cap used to calculate the earnings rate coefficients for the energy savings and demand reduction component should be reduced to 6% of spending, rather than 8%, to more appropriately provide an incentive that is sufficient to motivate performance but not unreasonable when compared to other similar mechanisms and the reduced utility risk.

---

[1] TURN has consistently opposed shareholder awards for spending on energy efficiency; however, if forced to choose among competing incentive mechanisms, TURN originally favored the *ex post* mechanism as a means to properly attribute savings to utility activities.

In Section 2 below, TURN explains our proposed modifications. In Section 3 TURN responds to the specific questions posed in the ACR, to the extent they have not been already addressed.

2. TURN's Proposed Modifications Reduce the Potential for Conflict and Maximize Consumer Benefits from Energy Efficiency Programs

2.1. The TRC Adder Should be Eliminated

The ACR proposes to multiply the resource program savings award (maximum of about $120 million) for each utility by a "multiplier" based on the difference between the *ex post* verified TRC ratio and the *ex ante* TRC ratio based on the approved portfolios.[2] The goal of the TRC adder is to "reward the utilities for achieving the energy savings in as cost-effective manner as possible."

The TRC adder reintroduces a number of problems that are eliminated by moving from a "net benefits" to a "savings" *ex post* incentive model. It is true that calculating *ex post* savings does depend on inputs from the EM&V process. However, calculating both net benefits and the TRC requires monetizing the energy and capacity savings through the avoided cost model and calculating accurate incremental measure costs to determine net measure costs. Essentially, calculating the TRC involves all of the same EM&V inputs as calculating the net benefits under the old RRIM.

Moving to the *ex post* savings model already introduces some of the potential problems associated with the EM&V process. TURN strongly recommends against reintroducing all of the elements of the "shared savings" model by introducing the TRC adder.

Even more importantly, the TRC adder rewards the utilities based on the gross average portfolio cost-effectiveness. While TURN certainly supports cost-effectiveness as a bedrock principle for ensuring ratepayer value, there is justified concern that even the sophisticated E3 cost effectiveness model fails to reflect "true avoided costs." The energy efficiency cost effectiveness model averages over all measures, and while it accounts for the *time* effect on capacity and energy value, it does not in any way account for locational value. But actual utility generation and T&D investments are increasingly driven not by "system-wide" generation needs, but by local reliability needs, renewable transmission needs and local circuit capacity needs. It is

[2] ACR, p. 21. For example, if the ex ante TRC is 1.2, and the ex post TRC is 1.5, the award would be multiplied by (1+0.3)=1.3.

unclear how far apart the theoretical "system average avoided costs" are from the on-the ground decisions to build a peaker to support potential loss of once-through cooling generation, to upgrade transmission to deal with SONGS, or to install additional substation transformers to deal with local demand growth.

The "earnings rate coefficient" approach in the ACR is substantively quite different, in that it takes a specific dollar amount (8% of authorized funds) to calculate a "incentive rate" based on adopted programs goals converted into lifecycle demand and energy savings goals. The resulting "correlation coefficient" is multipled by actually realized demand and energy savings to calculate the estimated payment.

2.2. Instead, the ESPI Should Include an Adder Based on Decreased Non-Incentive Spending

In approving the budgets for 2013-2014 the Commission reiterated the reasonableness of having a target spending on "non-incentive" costs of 20% as compared to the total budgets.[3] The Commission noted that despite this historical goal, as well as caps on administrative costs and marketing and outreach expenses, spending on non-incentive costs has been steadily increasing and is significantly above the 20% target.

The Commission found that the increase in these non-incentive costs is contributing to the decrease in cost effectiveness values. The Commission adjusted the budgets to increase cost-effectiveness results and declared that:

> We still require the utilities to minimize their non-incentive budgets as much as possible to achieve the target of no more than 20% of the budget associated with the "implementation-customer services" category of costs.[4]

Despite these directives from the Commission, the utility compliance filings failed to significantly reduce, and in the case of SCE and SCG actually increased, the percentage of budget spent on non-incentive activities, resulting in an unweighted average ratio of 36%.[5]

[3] D.12-11-015, p. 98.
[4] D.12-11-015, p. 101.
[5] TURN conservatively reduced the percentages by subtracting 6% as a proxy for non-resource program costs.

Table 2: Percentage of Program Budgets Spent on Non-Incentives

	PG&E % T	SCE % T	SDG&E % T	SCG % T
Applications Direct Implement: Customer Services (net 6% non-resource costs)	36%	30%	31%	37%
Advice Letter Compliance Filings Direct Implement: Customer Services (net 6% non-resource costs)	32%	37%	30%	44%

Source: IOUs Advice Letter Compliance Filings, A.12-07-001, January 2013, Budget Placemats (Appendix C)

A higher percentage of spending on incentives and rebates indicates success on multiple fronts. It indicates generally greater participation levels, resulting in larger savings and better cost-effectiveness.

Thus, rather than focusing on the TRC metric, which requires inputs from the EM&V process to monetize costs and benefits, TURN recommends an adder focused on the much simpler metric of non-incentive/total spending. TURN recommends that each utility receive \$500,000 for a 1/10th reduction from their compliance percentage to a 20% goal, with a maximum potential award of \$5 million if the utility achieves the 20% goal during the two-year period.

So, for example, since SCE is forecast at 37% spending on non-incentives, it would receive \$500,000 for each 1.7% reduction in the metric.[6]

TURN proposes this utility-specific metric in order to reward utilities based on actual performance. An equal metric (for example, \$500,000 for each 1% reduction) could have the unintended consequence of rewarding utilities that poorly design their programs to start with a high percentage of non-incentive spending.

2.3. The *ex post* Resource Incentives Should be Capped at 6% of Budgets

The ESPI calculates the correlation coefficients by using 8% of the authorized resource program funds (excluding administrative costs, EM&V, ME&O, C&S, and REN/CCA programs)[7] as the basis. The mechanism is designed so that the four utilities could achieve the

[6] (37-20)/10=1.7%. A reduction to 20% would thus earn the maximum \$5 million.

[7] TURN has not confirmed the allocations presented in 4a, 5a, 6a and 7a of the ACR.

"maximum cap" of almost $120 million in this category if their resource programs 1) hit the target EUL (12 years electric, 15 years gas) and target NTG (portfolio average of 0.8), and 2) achieve 110% of the adopted first year energy and demand savings. If the utility programs 1) achieve 100% of target energy and demand savings, and 2) achieve the same average EULs and NTG as in 2010, they would receive the 'business-as-usual' payment of almost $75 million in this category.

The maximum award results in an overall ESPI potential payment of almost $160 million for the two years, or a one-year shareholder award of $80 million. Under the BAU case, the average annual award would be $52 million.

One of the most subjective issues that the Commission has addressed in designing the efficiency incentive mechanism is the potential "size" of the award necessary to overcome utility "disincentives" to do energy efficiency. TURN has argued repeatedly that if one accepts the notion that the fundamental utility regulatory rate-of-return model (which calculates return based on capital spending) is incompatible with the promotion of energy efficiency, then the logical response is to contract for an independent entity or entities to run energy efficiency. However, if the utilities continue their role as program administrators, TURN has also provided factual arguments showing that incentives equal to about 5% of spending should be sufficient to "motivate" upper management to appropriately prioritize energy efficiency divisions in company-wide planning and strategy. These arguments include:

- When properly adjusted, energy efficiency incentives in other states average about 7% of program costs, but not all these states have full revenue decoupling protection;[8]
- Under the "shared savings" energy efficiency mechanisms in 1990-1997 the four utilities received a combined average annual awards of $62 million;[9]
- Other performance-based incentive mechanisms in California have provide maximum annual payouts of between $1 million and $35 million.[10]

Even more importantly, the Commission has long recognized that an incentive mechanism should appropriately balance risks and rewards. During the 2006-2009 program years

[8] TURN Post-Workshop Comments, October 1, 2012, p. 4-6; See, also, TURN Comments, R.12-01-005, July 16, 2012, p. 13-15.
[9] TURN Comments, R.12-01-005, July 16, 2012, p. 10.
[10] TURN Comments, R.12-01-005, July 16, 2012, p. 10.

the utilities were awarded average annual incentives of almost $68 million under the RRIM mechanism, which included deadbands, livebands and penalties.[11] In 2010 the utilities were awarded a payment of $42.2 million based on a mechanism awarding up to 6% of spending.[12] Under the proposed ESPI the utilities are guaranteed an award if they achieve *any positive savings from resource programs and/or spend any money on non-resource programs.* There is no risk of zero rewards. There is no risk of penalties. There is only upside potential for the utilities.

It is fundamentally unfair to reform the RRIM mechanism to create a one-sided profit potential for the utilities while at the same time increasing the potential payout. The absolute maximum annual payout under the ESPI should not be significantly higher than the average 2006-2009 RRIM payment of $68 million. TURN thus recommends that the cap on the *ex post* savings component be based on an allocation of 6% of authorized program budgets. This results in a maximum potential (two-year) award of $90 million in this category, or a total maximum ESPI payment of almost $130 million, resulting in maximum annual awards of $65 million.

Reducing the potential payout under the ex post savings mechanism may have the additional benefit of minimizing significant disputes concerning EM&V.

TURN also notes that there appears to be an inherent unfairness in creating an ESPI mechanism that applies only to the IOUs. Approximately 34% of the authorized budgets are allocated to third party programs, local government partnerships and RENs.[13] None of these other entities that manage or administer programs receive additional "profits" on top of their administrative costs.

2.4. Summary of TURN Proposal

The ACR requested parties to submit spreadsheet versions of Tables 12a and 12b. TURN's proposal results in a change to the "ex post savings performance award" rows of each spreadsheet due to our modification of the cap used to calculate the correlation coefficients from 8% to 6%. TURN's proposed modification to the adder does not impact the results in Tables 12a and 12b.

The revised Tables 12a and 12b are as follows:

---

[11] The Commission awarded $211,853,077 for 2006-08 (D.10-12-049), and $60,011,998 for 2009 (D.11-12-036).
[12] D.12-12-032, pp. 26-28, 38-39.
[13] D.12-11-015, Table 13, p. 103-104.

Table 3: TURN Version 12a (Maximum Payment Cap by Component and IOU)

Total Incentive Caps	PG&E	SCE	SDG&E	SCG	Total
Non-resource program Management Fee	$3,323,861	$3,157,556	$633,494	$377,033	$7,491,944
Ex Ante Compliance Performance Award	$13,018,331	$10,432,231	$3,427,937	$2,919,280	$29,797,779
Codes and Standards program Management Fee	$1,224,832	$1,009,646	$189,785	$151,178	$2,575,441
Ex Post Savings Performance Award	$39,054,994	$31,296,693	$10,283,810	$8,757,839	$89,393,336
All IOU 2013-14 Payment Cap	**$56,622,019**	**$45,896,126**	**$14,535,025**	**$12,205,329**	**$129,258,499**

Table 4: TURN Version 12b (Estimated "Business as Usual" Payments by Component and IOU)

	PG&E	SCE	SDG&E	SCG	Total
Non-resource program Management Fee	$3,323,861	$3,157,556	$633,494	$377,033	$7,491,944
Ex Ante Compliance Performance Award	$8,852,465	$ 5,842,049	$1,062,660	$1,050,941	$16,808,116
Codes and Standards program Management Fee	$1,224,832	$1,009,646	$189,785	$151,178	$2,575,441
Ex Post Savings Performance Award (Target Scenario)	$23,655,621	$19,071,422	$6,496,475	$6,973,429	$56,196,948
Total 2013-14 Payment (Target Scenario)	**$37,056,780**	**$29,080,674**	**$8,382,415**	**$8,552,580**	**$83,072,449**

3. Responses to Specific Questions Posed in the ACR

The ACR poses a number of questions concerning each of the four incentive components. To the extent these have not been addressed in the comments above, TURN provides additional responses below.

<u>Management Fee for Non-Resource Programs</u>

1. Should non-resource based programs be a component of the ESPI for the 2013-2014 energy efficiency portfolio?

TURN does not oppose the management fee approach for the 6% of the budget allocated for non-resource programs, though TURN strongly suggests that the IOUs do not require an incentive to spend this money, when non-resource activities and programs are often managed by other entities. The IOUs are not the most appropriate entities to achieve non-resource market transformation. A reasonable alternative would be to eliminate this category and allocate the proposed award to Ex Ante Review Compliance and/or the C&S management fee.

2. Does a management fee, paid as a fixed percentage of expenditures of non-resource programs, adequately incent utilities for successful implementation and investment in quality non-resource programs?

See response to No. 1 above.

3. In lieu of a management fee, should the Commission reward utilities for non-resource based programs using specific *program performance metrics as a more appropriate measure of nonresource program performance?*

Such a mechanism would be quite complicated and would require changes in each portfolio cycle. TURN supports the management fee approach as a reasonable and simple alternative. See response to No. 1 above.

4. If program performance metrics (e.g., number of whole home retrofit projects in hot climate zones; number of measures adopted into the portfolio from the Emerging Technology Program) are utilized rather than a management fee based on expenditures, which program performance metrics should be utilized? Are there specific programs that should be targeted over others? What level of incentive earnings potential should be offered for specific performance metrics and for non-resource programs in the aggregate?

See response to Question 13 below.

Management Fee for Codes and Standards

5. Is rewarding codes and standards program activity via a management fee is appropriate?

Yes. TURN completely agrees with the rationale in the ACR (p. 5) that code and standards work and savings calculations are significantly different from other program work. It would be inequitable to include the C&S savings as presently measure as a basis for an award based on *ex post* savings.

The utilities codes and standards programs consist of five separate spending categories, as summarized in below.

Table 5: 2013-2014 Proposed Budgets for C&S Programs

	Total Budget	Building Codes	Appliance Standards	Reach Codes	Planning Coordination	Compliance Improvement	Compliance % Total
PG&E	$12,762,470	$6,471,030	$3,620,202	$974,397	$738,386	$958,455	8%
SCE	$11,761,477	$3,421,521	$3,421,521	$1,069,224	$2,245,373	$1,603,838	14%
SDG&E	$2,098,460	$541,940	$425,173	$189,518	$299,943	$641,886	31%
SCG	$1,674,228	$417,252	$332,773	$169,652	$255,423	$499,128	30%
TOTAL	$28,296,635	$10,851,743	$7,799,669	$2,402,791	$3,539,125	$3,703,307	13%

Source: IOUs' 2013-2014 Applications, Appendix C: Statewide Codes and Standards Program, PIPs, Table 1

Over one-third of the total budget for all utilities is for "building codes," and for PG&E this component is approximately 50% of the budget. The category "building codes" includes a number of work tasks related to providing technical and administrative support to the CEC to develop the next generation (2016) of changes to Title 24 building codes. While the IOUs are apparently important in the process by which the CEC is supposed to revise and amend building codes, these activities primarily involve technical work of expert consultants. There is no absolutely no "performance risk" to the utility based on either measure installation or measure performance. Any savings will materialize only in future program year cycles.

Even more importantly, the estimation and attribution of savings is extremely suspect due to the high uncertainty in estimated compliance rates. Current estimates of C&S savings are based on EM&V findings from previous cycles which yielded compliance rates averaging 83%-95%. Given the more stringent nature of recently adopted codes and standards, we do not think that it is appropriate to assume such high compliance rates for the 2013-2014 cycle; in our estimation, actual compliance rates are more likely to be in the range of 50% to 70%. We suggest that for 2013-2014 C&S savings estimates be based on rigorous and comprehensive EM&V data, not assumptions derived from previous studies.[14] Both the CPUC[15] and the CEC[16] have recognized that one of the primary barriers to achieving the forecast savings for C&S is the low compliance rate, especially lack of compliance with building codes builders and contractors.

6. Is the fixed percentage of 10% an appropriate level to set the management fee?

---

[14] For a discussion of high compliance rate assumptions for 2013-2014 and the need for rigorous EM&V see: The Division of Ratepayer Advocates' Comments in Response to Scoping Memo and Ruling of Administrative Law Judge and Assigned Commissioner, A.12-07-01, September 14, 2012, page 9-12: http://docs.cpuc.ca.gov/PublishedDocs/Efile/G000/M028/K154/28154882.PDF

[15] See, for example, Administrative Law Judge's Ruling Regarding Program Guidance for the 2013-2014 Energy Efficiency Portfolio, Attachment A: Proposed Changes to Utility Energy Efficiency Portfolios for the 2013-2014 Transition Period, R.09-11-014, December 7, 2011, page A27.

[16] Brook M., B. Chrisman, P. David, T. Ealey, D. Eden, K. Moore, K. Rider, P. Strait, G. D. Taylor, and J. Wu. July 2011. ***Draft Staff Report: Achieving Energy Savings in California Buildings (11-IEP-1F).*** California Energy Commission, Efficiency and Renewables Division. Publication No. CEC-400-2011-007-SD, page 26-29. Available at http://www.energy.ca.gov/2011publications/CEC-400-2011-007/CEC-400-2011-007-SD.pdf

TURN does not object to the 10% fee given the level of spending in this category; however, we caution that if spending on CEC support activities (building codes, appliance standards) increases, this level of a fee may be inappropriate. There are at least two issues. One is the question of why the utilities should be in charge of research and analyses that primarily support codes and standards development by the CEC? The second is the fact that, as discussed in No. 5 above, one of the primary barriers to achieving savings from C&S appears to be the level of compliance, rather than technical success in improving actual building codes or appliance standards. Given that presently only 13% of the utility budgets are targeted for compliance improvement, a 10% management fee based on spending for the total C&S category would be excessive under any higher spending levels.

Award for Conformance with Ex Ante Review Process

7. Are the ex ante metrics included in the Appendix adequately designed to provide objective assessment of utilities' ex ante review performance? Are there other benchmarks that should be utilized to objectively measure utilities' ex-ante review performance?

No comment at this time.

8. Parties have expressed concern over rewarding utilities for process conformance since it is not results (i.e., energy savings) oriented and other Commission processes are not, and historically have not been, assessed under any incentive mechanism. Which Commission energy efficiency policy goals would be compromised or unattainable in the event that an incentive is based on process conformance?

TURN did not support an "incentive" mechanism for process conformance; however, there are no policy goals that would be "compromised or unattainable" by rewarding utilities for complying with their responsibility to provide data and cooperate with CPUC regulatory staff. The accuracy of EM&V savings calculations is important to achieving state policies and goals linked to EE and GHG reduction. The EAR process conformance incentive component is a reasonable response to the challenges during the past years with accurate and timely calculation of *ex ante* parameters and *ex post* true-ups.

Incentive Earning for Energy Savings and Demand Reduction Achievements

9. What are the pros and cons associated with calculating the savings award based on net benefits, using a modified version of the original PEB calculus, versus using NRDC's approach, as modified, which multiplies energy and demand savings by coefficients that would be derived from the adopted savings goals and the predetermined savings component cap?

TURN supports shifting from awards based on net benefits to awards based on demand and energy savings. The primary advantage is to reduce the temptation by the IOUs to focus on less expensive measures that provide cheap and easy savings and to focus on measures with higher long-term savings. The use of NTG and EUL to convert first-year savings into lifecycle savings is important in promoting long-term savings.

The primary disadvantage for ratepayers is the potential for reduced cost-effectiveness. However, as discussed in Section 2.1 and the response to Question 13 below, TURN is concerned that the E3 cost effectiveness calculator overstates the avoided cost values of EE savings because it does not reflect the present-day reality driving utility supply-side investments. Thus, TURN is less concerned about actual TRC values, as long as the portfolios are cost-effective in total. Decision 12-11-015 appropriately reminded the utilities that cost-effectiveness must be met based on both the TRC and PAC tests.

An ongoing concern is the need to better review prospective cost-effectiveness calculations made in the applications to adjust spending and program design prior to implementation. The Commission did an admirable job in D.12-11-015; however, the adjustments were fairly high-level and there was insufficient time to thoroughly evaluate individual programs. TURN hopes that the EAR incentive mechanism will improve such review in the future. However, additional process changes, such as rolling program cycles, would need to be implemented to address this problem.

TURN has proposed an adder based on incentive/total spending as another mechanism to ensure program performance.

10. Given the focus on deeper, longer-lived energy savings, is the use of proposed "target" EULs and NTG ratio of 12 years (electric EUL), 15 years (gas EUL), and 0.8 (NTG) appropriate as goals for utilities to achieve in the 2013-14 or future portfolio cycles?

Absolutely. The use of the target EULs and NTG ratio is critical to promoting longer-lived energy savings and shifting to measures that have not been already adopted in the marketplace. It is important not to reward utilities just for gross 1st year savings. Achieving higher EULs and higher NTG ratios accounts for a majority of the difference between the maximum reward amounts and the business as usual reward amounts.

11. One potential unintended consequence of using the proposed approach is that customers are exposed to some risk that the utilities will make changes to the measure mixes in their adopted portfolios that maximize total savings rather than maximizing total cost-effective savings. What is the magnitude of the risk that implementation of a non-cost effective (i.e., TRC < 1.0) portfolio would result from a net savings-based approach? Does the TRC calculated for the authorized portfolio based on ex ante savings estimates and utility proposed measure mix, in combination with the *existing fund-shifting rules, adequately protect against this risk? What other steps could be taken to protect customers from this risk if the Commission adopted a net savings, rather than net benefits, based savings component of the incentive mechanism?*

The risk of reducing portfolio cost-effectiveness is a valid concern with a net savings mechanism. TURN does not have any estimate of the "magnitude of the risk."

TURN notes that capping the maximum incentive based on achieving 110% of the first-year savings goal is essential to limiting the risk of portfolio cost-effectiveness deterioration. Moreover, TURN continues to recommend that cost-effectiveness analyses and issues should be better addressed prospectively by ensuring more regulatory review time for program applications for the next program cycle.

Another step that could be taken to protect customers is to continue a form of a "cost-effectiveness" guarantee. This was a component of the prior RRIM. Given the structure of the ESPI, a cost-effectiveness guarantee could provide for a dollar-for-dollar reduction in incentive payments (starting with the *ex post* payments first) until total incentives equal zero. TURN does not recommend a "shareholder penalty" due to non cost-effectiveness. If programs turn out to be not cost-effective on a portfolio basis, this problem should be addressed through significant redesign for the next program cycle.

12. Will the differences identified between the 2006-08 mechanism and the mechanism proposed herein sufficiently reduce the risk of contention associated with an ex post savings basis to warrant using an ex post approach rather than an ex ante approach, which resulted in unintended consequences related to the ex ante lockdown?

TURN generally supports using *ex post* values for actual utility shareholder incentives, partly due to the gaming and process issues identified in the ACR (p. 11-12), and partly due to the importance of accurate attribution for performance related to shareholder incentives. However, any shareholder incentive mechanism for energy efficiency performance (i.e. savings or net benefits), whether ex ante or ex post, will likely create opportunities for gaming due to the inherent uncertainties with measuring EE results.

13. Should the Commission include bonus "adders" for results not captured explicitly by the four proposed components (e.g., Energy Upgrade California projects in hot climate zones, increases in portfolio average Effective Useful Lives, etc.)? If so, which ones, and how should they be calculated?

TURN has previously proposed a performance metric designed to reward utilities for targeting the EUC to hot climate zones due to the significantly higher cost effectiveness of EUC in those climate zones. In general, TURN strongly recommends that EE investments be locationally targeted based both on climate and transmission or distribution circuit constraints. Such targeted EE maximizes benefits and is more consistent with utility supply-side investments.

As discussed in Section 2.1 above, the current cost-effectiveness model assumes only system-wide energy and capacity values. In reality, supply-side generation investments are driven primarily by either local reliability needs or by renewable energy mandates, not by a system-wide supply/demand balance. Transmission investments are driven at least partly by the desire to source more renewable energy. And distribution investments are driven by local circuit peak demand analyses. The net result is that an energy efficiency investment on a circuit that has excess capacity and is not in a constrained local capacity zone may not in reality displace or defer any G/T/D investments.

Nevertheless, on balance TURN does not propose a performance metric or incentive adder at this time to promote locational deployment of EE. The Commission did order the IOUs to target a percentage of marketing funds to customers in hot climate zones. TURN recommends that greater attention be paid toward targeted deployment of EE. However, TURN suggests that the proposed combination of a management fee (for non-resource programs) and savings awards (for resource programs) is adequate for 2013-14.

14. Should we include a cost-effectiveness adder in the ESPI? If so, is the proposed approach appropriate, or would a different approach be superior? Is there a need for an explicit cap on the potential resource program award to protect ratepayers? If so, how would we best determine a cap on an adder that is rewarding increases in program cost effectiveness? Should the cost-effectiveness adder be symmetric (i.e., increase or reduce resource program savings benefits) or should it only be applied if ex post cost-effectiveness is greater than the ex ante estimate?

As discussed in Section 2.1 above, TURN recommends against adopting the cost-effectiveness adder.

15. Is it possible that funds used to establish the On-Bill Financing programs in the 2010-2012 portfolio cycle will be re-loaned in the 2013-2014 cycle, and therefore should be included in the savings cap calculation and in ex post savings estimates? Alternatively, should these issues be deferred to future cycles, when the overall financing program designs are better understood? If the former, how should the portion of 2010-2012 On Bill Financing funds that will be available for loans in the 2013-2014 cycle be calculated for inclusion in the cap and savings calculations?

TURN presumes that the period of repayment would be longer, so that there would not be significant funds "re-loaned" in the 2013-2014 cycle; however, we lack actual data and so do not provide any recommendations at this time.

Date: April 26, 2013

Respectfully submitted,

By: __________/s/______________

Marcel Hawiger, Staff Attorney
Cynthia Mitchell, Energy Economics, Inc.

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