BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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

SAN DIEGO GAS & ELECTRIC COMPANY (U 902 M) AND SOUTHERN CALIFORNIA GAS COMPANY (U 904 G) REPLY COMMENTS ON ASSIGNED COMMISSIONER'S RULING SOLICITING COMMENTS REGARDING EFFICIENCY SAVINGS AND PERFORMANCE INCENTIVE DESIGN FOR ENERGY EFFICIENCY 2013-2014 PORTFOLIO

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May 3, 2013

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I. INTRODUCTION

Pursuant to the Assigned Commissioner's Ruling Soliciting Comments Regarding Efficiency Savings and Performance Incentive Design for Energy Efficiency 2013-2014 ("ACR"), dated April 4, 2013, San Diego Gas & Electric Company ("SDG&E") and Southern California Gas Company ("SoCalGas") (also referred to as the "Joint Utilities") respectfully provide replies to parties' opening comments in the above captioned proceeding. Opening comments were received from the following parties: Southern California Edison Company ("SCE"), (Pacific Gas and Electric Company ("PG&E"), Natural Resources Defense Council ("NRDC"), California Energy Efficiency Industry Council ("Efficiency Council"), Women's Energy Matters ("WEM"), The Utility Reform Network ("TURN"), Marin Energy Authority ("MEA"), and Division of Ratepayer Advocates ("DRA"). [1]

II. EXECUTIVE SUMMARY

The Joint Utilities reviewed and appreciate the views parties offered in opening comments concerning the form and substance of the Commission's contemplated Energy

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[1] Opening comments were submitted by DRA on April 26, 2013. On April 29, 2013, revised opening comments were filed by DRA with direction to parties to disregard their April 26 submittal.

Savings and Performance Incentive ("ESPI") mechanism. The ACR was commended by multiple parties, including the Joint Utilities for varying features, with support contingent on suggestions to enhance its framework to consistently reflect to core principles of any incentive mechanism.[2] The ACR should be commended for bringing such diverse parties together in broad strokes for such a complex matter. As stated in opening comments, the ESPI mechanism components described by the Joint Parties are the Commission's best option to ensure a transparent, reliable, useful and minimally controversial incentive mechanism as a tool to meet the Commission's many and varied energy efficiency goals.

Additionally, the Joint Utilities respond below to four specific issues raised in the ACR and dealt with in parties' comments which, if not addressed in the manner suggested by the Joint Utilities and other parties as set out below, would result in the Commission adopting an ESPI mechanism design that would likely fail to mirror its objectives.

III.
COMMENTS ON SPECIFIC ISSUES

The Joint Utilities comments focus on three specific issues in response to parties' comments.

A. ENERGY SAVINGS AND PEFORMANCE INCENTIVE SHOULD RELY ON AN EX ANTE APPROACH

The Joint Utilities agree with NRDC and PG&E that an ex ante approach to the ESPI will create a more optimal incentive mechanism. NRDC states: "Instead, we urge the CPUC to use ex-ante savings estimates (but still verifying the installations and expenditures) for the 2013-14 transition period, while setting up a process for an improved approach to determining energy savings estimates in the future."[3] The Joint Utilities agree, in tandem with a cost-effectiveness guarantee as discussed below, an ex ante approach will focus IOU efforts towards operating an

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[2] As have been discussed in depth in earlier comments by the Joint Parties, and as expounded upon by the Commission in its *White Paper*. See "Proposed Energy Efficiency Risk-Reward Incentive Mechanism and EM&V Activities," prepared by the Energy Division, April 1, 2009.
[3] NRDC Opening Comments, p. 2.

efficient and cost-effective portfolio. That is because it would establish a series of metrics that will remain constant and known through the end of the program cycle, allowing utility management to respond to the savings signals those values provide, and eventually receiving an incentive consistent with those actions taken. It will also remove unnecessary subjectivity, whereas an ex post approach will create an overly complex and contentious mechanism which lacks transparency.

In DRA's Opening Comments it is acknowledged: "that it is difficult to determine whether these actions will adequately lessen this contention, because awards are still contingent on controversial calculations (such as savings estimates and Net-to-Gross [NTG] ratios)."[4] DRA accurately points out California's experience with ex post mechanisms over time, as it was implemented throughout the 2006-2008 program cycle, the Commission marginalized the emphasis on ex post until it was removed completely in favor of a more stable, and fair, ex ante approach.

The ACR instead revisits the elements of contention that the Commission once strived to remove. DRA continues to state that: "…the goal of limiting contention on EM&V is critical to the success of any incentive mechanism."[5] NRDC echoes similar concerns in their comments, stating: "…an ex post approach for an incentive mechanism will not be able to succeed until the Commission addresses the underlying problems with the EM&V system."[6] The ex ante approach proposed by the Joint Utilities, coupled with verification of measure installations and annual audit of IOU expenditures, will meet the desires of parties, including DRA, and the objectives of the Commission.

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[4] DRA Opening Comments, p. 12.
[5] DRA Opening Comments, p. 12.
[6] NRDC Opening Comments, p. 3.

B. JOINT UTILITIES SUPPORT THE IMPLEMENTATION OF A COST-EFFECTIVENESS GUARANTEE

The Joint Utilities support the use of a cost-effectiveness guarantee for the resource component of the ESPI mechanism. A cost-effectiveness guarantee is an appropriate component of the mechanism given the Commission's focus on pursuing all cost-effective energy efficiency. The Joint Utilities are committed to achieving the Commission's goal and have put forth a plan for its 2013-2014 programs, pending approval by the Commission that would accomplish this task. In their Opening Comments, NRDC and DRA embrace this proposal. DRA states: "The Commission should include a Cost Effective Guarantee, instead of a cost effectiveness multiplier, in order to better protect ratepayer investment."[7] The Joint Utilities agree.

As originally put forth in the October 1, 2012 comments in this Rulemaking, the Joint Utilities present the following proposal to ensure that IOUs are rewarded only if there are positive net benefits for customers:

1. Cost-effectiveness guarantee calculated using the Program Administrator Cost (PAC) test
2. Cost-effectiveness guarantee calculated on an ex ante basis
3. Cost-effectiveness guarantee applied to the resource component of the ESPI, and does not affect the non-resource, Codes & Standards, or EAR mechanisms
4. Earnings accrue if the individual IOU portfolio exceeds a PAC ratio of 1.0
5. No penalties would accrue if the individual IOU portfolio's cost-effectiveness is below a PAC ratio of 1.0

This approach will allow the Commission to balance the intent of the mechanism to pursue long-lived and persistent energy savings with the desire to implement a cost-effective portfolio to customers. While DRA supports the use of a cost-effectiveness guarantee as proposed by the Joint Utilities, with no penalties and only applicable to the resource mechanism

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[7] DRA Opening Comments, p. 10.

component, , DRA would also implement such a guarantee calculated on an ex post basis using the Total Resource Cost ("TRC") test.

The Joint Utilities strongly disagree with this approach. As put forth in their Opening Comments, adopting a mechanism predicated on ex post adjustments creates a complex, un-transparent, and contentious mechanism. This should be avoided, especially given the pitfalls experienced in similar past mechanisms. Instead, a cost-effectiveness guarantee should be implemented on an ex ante basis, where the Commission can measure IOU performance relative to the approved plans. Such an approach is straightforward, transparent, and fair, and similar to how the Commission measures the success of the core IOU business. The cost-effectiveness guarantee should be measured using the PAC test, which values energy efficiency measure costs on equal footing with other supply-side investments from a customer perspective. The IOU should be measured on how effectively it was able to execute its plan and not be held to evaluation metrics that are outside of IOU control.

Furthermore, insertion of the TRC test to measure cost-effectiveness does not provide the direct linkage to the IOU business as the PAC test does. The TRC diverts the focus of the IOU from achieving the lifecycle energy savings the ACR strives to incent by injecting diversionary inputs, such as incremental costs, which are difficult to measure, subjective, and outside of IOU control. NRDC agrees, and states: "These are some of the sources of complexity and controversy that the Commission intended to move away from in considering alternatives to the shared savings approach."[8] In order to achieve a transparent mechanism, ex ante parameters and a PAC threshold for a cost-effectiveness guarantee should be utilized.

[8] NRDC Opening Comments, p. 10.

C. JOINT UTILITIES SUPPORT EARNINGS CAP RECOMMENDED IN ACR AS IT STRIKES AN APPROPRIATE BALANCE BETWEEN SHARING NET BENEFITS WITH CUSTOMERS AND RECOGNIZING MANAGEMENT'S EFFORTS IN PURSUING LONG-TERM COST EFFECTIVE SAVINGS

DRA and TURN recommend that the Commission lower the overall statewide cap of approximately $159 million. The Joint Utilities believe that the ACR proposal, , provides a reasonable balance between sharing the net benefits with its customers and adequately recognizing management's efforts in aggressively pursuing long-term cost effective savings with the various adjustments to the shared savings mechanism. This proposed lowered cap recognizes the concerns regarding the elevated level of earnings to utilities from the past mechanisms. It should also move all stakeholders towards the arrangement of a mechanism that is less complicated and administratively burdensome to measure and authorize awards, while still providing the appropriate oversight by Commission staff.

D. WEM'S PROPOSED INCENTIVE MECHANISM IS CONTRARY TO ACR'S GOAL OF SIMPLYFING THE MECHANISM AND HAS THE POTENTIAL TO CREATE NEGATIVE UNINTENDED CONSEQUENCS.

Regarding WEM and Rockwood Consulting's ("WEM/Rockwood") proposed Limited Incentive Mechanism for the Use of Energy Efficiency as a Distribution Resource, the Joint Utilities believe the approach is very similar to the proposed ESPI except that it is limited to deferring distribution costs only and takes an aggregate measurement approach. While the mechanism has some of the desirable characteristics of ESPI, it has more measurement difficulties and several undesirable characteristics.

The approach starts with the same premise as ESPI, tying the incentive to deferring supply-side investments. However, the WEM/Rockwood proposal would focus on peak capacity distribution benefits and only reward EE investments that lower peak load on a subset of circuits within the utility service area. The reward would be tied to an aggregate measurement of reduced load behind each designated substation and the potential deferred costs. While on the face of it this approach seems reasonable, it has some unintended and undesirable consequences. First, it would lead to focus on customers in particular locations and likely unequal incentives for similar energy reductions throughout the utility service area given the distribution costs would not be spread to all EE as in ESPI, but concentrated on particular circuits. The approach would be perceived as unfair to those not on preferred circuits. Second, it may lead to lost opportunities in areas with no immediate distribution upgrade needs. Third, it will lead to an undue focus on deferring distribution costs to the detriment of other major EE benefits such as reducing generation peaks and reducing energy use in general, which are considered on an equal basis in ESPI.

Respectfully submitted

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May 3, 2013