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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

COMMISSION ADVISORY  
AND COMPLIANCE DIVISION  
Energy Branch

RESOLUTION E-3380  
May 25, 1994

R E S O L U T I O N

RESOLUTION E-3380. PACIFIC GAS AND ELECTRIC COMPANY REQUESTS APPROVAL OF A PILOT THIRD-PARTY FINANCING PROGRAM FOR NONRESIDENTIAL AND MULTI-FAMILY CUSTOMERS FOR ENERGY EFFICIENCY IMPROVEMENTS.

BY ADVICE LETTER NO. 1826-G/1461-E filed on January 18, 1994.

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SUMMARY

1. In this advice letter, Pacific Gas and Electric Company (PG&E) requests approval to participate in a pilot third-party financing program for nonresidential and multi-family customers for energy efficiency improvements. PG&E states that its involvement will encourage lenders to offer more attractive loan terms to customers and increase customer acceptance of energy efficiency at lower ratepayer cost compared to traditional rebate programs.
2. This resolution authorizes PG&E to participate in the pilot financing program with certain modifications.
3. The Division of Ratepayer Advocates (DRA) filed a timely protest to this advice letter. DRA's protests have been considered and certain aspects are granted. This program will not be eligible for shareholder incentive earnings. A cap is placed on program expenditures and PG&E is directed to develop guidelines to evaluate the effectiveness of the program.

BACKGROUND

1. PG&E is requesting approval to test the use of third-party financing by partnering with traditional financing sources to stimulate energy efficiency in its service territory. According to PG&E, the pilot program will provide its nonresidential and multi-family customers with access to low-cost third-party funds for implementing energy efficiency measures. Under the pilot program, the financing sources will originate and service the loans for customers' nonresidential and multi-family energy efficiency projects or measures. Only measures eligible for a PG&E Commercial, Industrial, and Agricultural (CIA) or Multi-Family Property retrofit rebate will be eligible for financing. PG&E will market this program in conjunction with its rebate

programs. A customer may participate in either the loan program or the traditional rebate program, but not both.

2. PG&E expects that this type of financing program will increase the rate of penetration and customer adoption of energy efficient measures, reducing the cost of DSM programs for non-participating customers. PG&E believes that this program will overcome many of the market barriers associated with traditional rebate programs, allowing more customers to invest in energy efficiency.

3. As proposed, PG&E participation in the third-party financing program is a pilot effort. If approved, the program is scheduled to be offered to customers in one or more operating divisions and then be expanded system wide through December 31, 1995, which is the end of the current General Rate Case (GRC) cycle. The pilot program will be monitored to identify and correct any necessary program changes to ensure that the program is operating effectively. Measures of success include cost-effectiveness, customer convenience and satisfaction, and increased customer participation. At a minimum, the financed measures will be subject to the same Measurement and Evaluation (M&E) protocols as rebated measures. If the financing program is determined to be successful, PG&E will propose that it be incorporated in its DSM programs in the 1996 Test Year GRC proceeding.

4. As proposed, program costs for the pilot program would utilize currently-authorized funding for the nonresidential and multi-family rebate programs. Funds available for the financing option would initially be capped at 75 percent of what would otherwise be paid out to an individual customer in the form of a rebate.

5. PG&E anticipates that loan amounts will range from \$5,000 to \$50,000 for terms of two to seven years. PG&E will verify that the measures are eligible for financing. The lender retains responsibility for billing the customer, processing payments, and collecting on delinquent accounts. The initial interest rate will be established after the lender determines the costs for originating and servicing the loans. Options for customers for this type of loan would typically be a small business loan or credit line with an interest rate in the 9 to 16 percent range or an equipment lease with interest in the range of 12 to 20 percent.

6. The financing source will originate and service the energy efficiency financings, and recourse for nonpayment would revert to the customer only, with no liability to the utility. PG&E may chose to utilize the funds set aside for the financing option to buy down the interest rate on the loans, fund a portion of the financing source's loss reserve pool, or other enhancement features. PG&E anticipates that most of the funds will be utilized to buy down the effective interest rate. If the interest rate is bought down to zero percent, funds could be applied towards the principal of the loan. Determination of the

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amount of money available for financing will be made on an individual customer basis.

7. As proposed by PG&E, in order to qualify for participation in this program, the loan package of proposed energy efficiency investments must pass all applicable cost-effectiveness standards (i.e., the Total Resource Cost (TRC) test and Utility Cost (UC) test) and satisfy program guidelines associated with PG&E's nonresidential and multi-family DSM programs.

8. Originally, PG&E proposed that all cost-effective measures financed under this program be eligible for the same shareholder incentive mechanism currently applicable to such measures. In its response to DRA's protest, PG&E withdrew its request for shareholder earnings associated with the pilot financing program. PG&E submitted revised 1994 shareholder incentive targets in Advice Letter 1800-G-B/1446-E-B, filed on March 1, 1994, removing the shareholder earning impacts of the proposed financing pilot.

9. PG&E filed Advice Letter 1826-G/1461-E on January 18, 1994.

#### NOTICE

The Advice Letter was noticed in accordance with section III of General Order 96-A by publication in the Commission Calendar and distribution to PG&E's advice filing service list.

#### PROTESTS

1. The Commission Advisory and Compliance Division (CACD) received one timely-filed protest from the Division of Ratepayer Advocates (DRA) on February 7, 1994. PG&E responded to DRA's protest on February 15, 1994.

2. DRA raised three issues in its protest: 1) PG&E should not receive any shareholder incentives from this program, 2) PG&E's involvement will increase costs to participants, and 3) the belief that PG&E's involvement in this program is not a necessity.

3. DRA believes that it is inappropriate for PG&E to earn shareholder incentives via the shared savings mechanism on measures installed through the financing program. DRA states that this program is conceptually quite different from the Nonresidential Energy Efficiency Incentive programs (EEI), on which PG&E has been allowed to earn shared savings incentive dollars, and asserts that PG&E's guarantee of a portion of the loan losses does not "lead to the installation of a more efficient appliance than would have been installed in the absence of the program."

4. DRA also states that PG&E failed to include appropriate Measurement, Forecasting and Regulatory Reporting (MFRR) plans that are consistent with the protocols adopted in D.93-05-063.

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5. DRA believes that PG&E's involvement with the loan program will increase the costs to participants. Although the interest rate will be reduced because PG&E absorbs some of the risk, DRA points out that the incremental cost of this risk will be borne by ratepayers. In addition, there is the potential for increased earnings and duplicative administrative costs.

6. Finally, DRA claims that PG&E's involvement with this program is not necessary. DRA states that PG&E has failed to provide any proof that its proposed involvement in the process would be the most cost effective and efficient approach. DRA also describes the history of the nonresidential rebate programs as an indicator of the success of those programs without a financing option.

7. In response to DRA's protest, PG&E responded with certain modifications to the original advice letter. PG&E has modified its proposed pilot to be ineligible for shareholder incentive treatment and to track pilot program costs separately using the appropriate Commission-defined program categories. In addition, PG&E will develop a comprehensive measurement plan to determine the pilot's success in terms of producing net benefits, to determine the value of PG&E's involvement in financing energy efficiency improvements, and the size of the market potential.

#### DISCUSSION

1. PG&E has presented the pilot loan program as continuing through December 31, 1995, using existing funds (and therefore causing no rate increase) and not resulting in withdrawal of service. CACD believes that this request can be handled through the Advice Letter forum, but as stated in Resolution E-3342 (in which the Commission authorized a financing option for San Diego Gas & Electric Co.), CACD cautions PG&E, and all utilities interested in presenting new DSM programs to the Commission, to consider carefully the appropriateness of the Advice Letter forum for new programs. CACD recommends that PG&E be allowed to operate the pilot, as modified below, from the effective date of this Resolution through December 31, 1995.

2. CACD recommends that PG&E fully involve its DSM Advisory Committee in discussions involving DSM program changes and implementation and incorporate members' comments and concerns prior to filing advice letters. The Advisory Committee process was established to augment effective program implementation and to expedite the regulatory process. CACD believes that the Advisory Committee process is important and should not be circumvented. Had Advisory Committee members been fully consulted, CACD believes that concerns regarding this advice letter could have been effectively resolved in a more timely manner.

3. PG&E states that its involvement in the pilot financing program is designed to respond to barriers that have prevented traditional DSM programs from achieving more customer investment in cost-effective energy efficient measures and services. PG&E

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hopes to increase participation by nonresidential and multi-family customers who may not have the up-front capital to install energy efficient equipment. In addition, this program, as proposed, is designed to capture lost opportunities. Rebate programs, while effective, may not completely overcome the first cost barrier. CACD recommends that the financing program be explored on a pilot basis, since it provides a new delivery mechanism for energy efficiency.

4. CACD views this pilot program as a step which fits into the Commission's overall policy framework for DSM: we have moved from an era of command-and-control regulation to one of decentralized incentive regulation. The Commission has expressed interest in limiting general ratepayer involvement in DSM, lowering existing market barriers to DSM, and testing an emerging marketplace for such up-front financing programs. The pilot financing program, as modified, provides an additional delivery mechanism for achieving these goals in a very cost-effective manner. As stated in Public Utilities Code Section 701.1, "a principal goal of electric and natural gas utilities' resource planning and investment shall be to minimize the cost to society of reliable energy services and to encourage the diversity of energy sources through improvements in energy efficiency and development of renewable energy resources." In addition, the utilities are directed to "exploit all practicable and cost-effective conservation and improvements in the efficiency of energy use and distribution that offer equivalent or better system reliability, and which are not being exploited by any other entity."

5. In response to DRA's objections of this pilot's eligibility for earnings based on PG&E's shared savings mechanism, PG&E has modified its request to exclude shareholder earnings. In its protest, DRA recommended that, as an alternative, this pilot be authorized to receive cost plus treatment (also called performance adder treatment). CACD has weighed this option carefully. Performance adder mechanisms apply to programs which may not be cost-effective or programs in which the link between programs and savings is difficult to measure. In this case, measures installed under the pilot are only eligible if they are cost-effective and currently eligible for rebates, which are by definition, measurable. PG&E's participation in the financing program may directly influence the customer's installation of a more efficient device. This issue must be addressed as part of the evaluation of the pilot if PG&E seeks to continue this program. In the interim, CACD agrees that PG&E should not receive shareholder incentive treatment for the pilot program.

6. CACD believes it is reasonable to establish a cap on program expenditures for the pilot. In establishing a cap, we seek to provide PG&E with enough flexibility to successfully implement the pilot so that the impact of this alternate delivery mechanism can be evaluated, while shielding the ratepayers from additional risk. Currently, PG&E has budgeted approximately \$64 million for its 1994 rebate program for the market sectors targeted by this pilot and anticipates a similar

level for 1995. CACD proposes that PG&E's expenditures for this program be capped at \$10 million over the entire pilot period (1994-1995). This is less than 10% of PG&E's planned budget over the two year period. PG&E is still obligated to market its rebate programs in order to achieve the goals established in its 1994 forecast filing. CACD believes this will limit the ratepayer risk of this pilot to a reasonable level.

7. Classifying PG&E's pilot financing program as a non-earnings resource program is an appropriate interim solution to the uncertainty over the appropriate final earnings treatment of this program should PG&E seek to continue the program. At a minimum, the financed measures will be subject to the same M&E protocols as rebated measures. Should PG&E decide to include this program in its request for 1996 funding of nonresidential and multi-family resource programs, the burden of proof will be on PG&E to have demonstrated the appropriate earnings treatment for this program in a manner that is satisfactory to, and verifiable by, the Commission. In addition, a thorough analysis of the risks and rewards related to financing programs must be included in PG&E's request for continued funding, as well as a discussion of the pros and cons of financing delivery mechanisms versus traditional rebate programs.

8. In addition to the modifications recommended above, CACD recommends ratepayer expenditures for the pilot be subject to Commission review of reasonableness. A Commission finding of imprudence, a violation of program conditions or guidelines, or other misuse of ratepayer funds in the the loan pilot could lead to discontinuance of the program, disallowance, and/or penalty. CACD fully expects that PG&E will make its best effort to minimize the use of ratepayer funds for this pilot while maximizing ratepayer benefits. Funds utilized for this program will be subject to the same reasonableness review as all other ratepayer-financed DSM programs.

9. Finally, CACD recommends that PG&E develop specific criteria for evaluating the success of this program before the program is implemented. The evaluation should include both process, market, and impact evaluation criteria. The criteria should be developed early so that questions about the pilot program's effectiveness can be addressed and the correct data collected. CACD recommends that PG&E develop these criteria and its evaluation design in consultation with DRA and CACD.

#### FINDINGS

1. PG&E filed Advice Letter 1826-G/1464-E on January 18, 1994, to request Commission approval to participate in a pilot third-party financing pilot for nonresidential and multi-family energy efficiency improvements. The pilot financing program would use existing authorized DSM funds.

2. PG&E's proposed use of currently authorized DSM funds is intended to improve the utility's ability to capture demand-side resources in its service territory.

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3. This request can be addressed through a Commission Resolution because of its pilot nature.

4. Ratepayer expenditures for PG&E's participation in the pilot loan program should be limited to \$10,000,000 for the duration of the pilot program. Expenditures for this program should not be eligible for shareholder incentive treatment.

5. All ratepayer funds used for the pilot loan activities shall be subject to Commission review of reasonableness. A Commission finding of imprudence, a violation of program conditions or guidelines, or other misuse of ratepayer funds in the pilot could lead to discontinuance of PG&E's participation in the program, disallowance, and/or penalty.

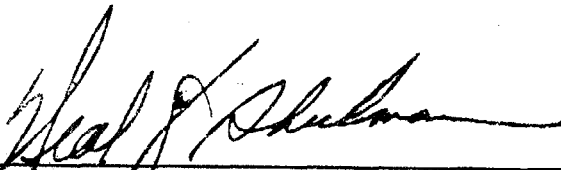
5. Thorough analysis and evaluation of the use of ratepayer funds is essential before moving beyond a pilot loan program.

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**THEREFORE, IT IS ORDERED that:**

1. Pacific Gas and Electric Company is authorized to establish a pilot demand-side management third-party financing program. The pilot program is approved as described in Advice Letter 1826-G/1464-E, and as modified herein. The pilot is authorized from the effective date of this Resolution through December 31, 1995.
2. Pacific Gas and Electric Company is authorized to participate in the pilot financing program using existing funds and applying the appropriate fund shifting guidelines.
3. The Division of Ratepayer Advocates' protest regarding appropriate treatment of the shared savings mechanism is granted, which incorporates its concerns regarding complete and proper Measurement, Forecasting and Regulatory Reporting. All other aspects of its protest are denied.
4. If Pacific Gas and Electric Company plans to pursue its participation in the pilot financing program, as modified in this Resolution, it must file a supplemental Advice Letter to incorporate our orders regarding shareholder incentive treatment and establishment of a spending cap within thirty days from the effective date of this Resolution. The supplemental advice letter shall be effective on the date filed through December 31, 1995.
5. This Resolution is effective today.

I hereby certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on May 25, 1994. The following Commissioners approved it:

  
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NEAL J. SHULMAN  
Executive Director

DANIEL Wm. FESSLER  
President  
PATRICIA M. ECKERT  
NORMAN D. SHUMWAY  
P. GREGORY CONLON  
JESSIE J. KNIGHT, Jr.  
Commissioners