Utility Incentive Mechanisms

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Overview

Traditional ratemaking is not designed to encourage regulated utilities to promote energy efficiency.

States and regulators have been exploring ways to make investments in energy efficiency attractive to utilities.

One of the main tasks of utility regulators has been to identify workable financial incentives that are fair to both utilities and customers.

Missouri Energy Efficiency and Investment Act

- Unlike Missouri's statute adopting renewable portfolio standards, the energy efficiency statute does not impose any mandatory energy efficiency requirements on utilities. Participation in energy efficiency or demand side programs is voluntary for the utilities.

Missouri Energy Efficiency and Investment Act

- In 2009, the Missouri legislature passed the Missouri Energy Efficiency and Investment Act
- The stated policy of Missouri is to value investment in demand-side and energy efficiency equally with traditional supply-side investment.
- The legislation directs the Missouri Public Service Commission to align utility financial incentives with helping customers use energy more efficiently.

MEEIA rulemaking authority

- The Missouri Energy Efficiency and Investment Act authorizes the Missouri Public Service Commission to adopt rules to implement the statute. The Commission adopted four rules to implement the statute.
- The rulemaking process in Missouri allows for participation by all interested stakeholders. Utilities, consumer advocates, and large energy consumers all participated in the rulemaking.

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Non-Mandatory Energy Efficiency Goals

- Although Missouri's energy efficiency statute does not impose mandatory targets on utilities, the Commission had adopted non-mandatory energy efficiency goals.

Missouri non-mandatory energy efficiency goals

- 2012: 0.3% of total annual energy and 1% of annual peak demand
- 2013: 0.5% of total annual energy and 1% of annual peak demand
- 2014: 0.7% of total annual energy and 1% of annual peak demand
- 2015: 0.9% of total annual energy and 1% of annual peak demand

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Missouri non-mandatory energy efficiency goals, cont.

- 2016: 1.1% of total annual energy and 1% of annual peak demand
- 2017: 1.3% of total annual energy and 1% of annual peak demand
- 2018: 1.5% of total annual energy and 1% of annual peak demand
- 2019: 1.7% of total annual energy and 1% of annual peak demand
- 2020: 1.9% of total annual energy and 1% of annual peak demand

Cost Recovery under Missouri’s Energy Efficiency and Investment Act

- Cost recovery for demand side or energy efficiency programs is only allowable if the programs are:
  - Approved by the commission
  - Result in energy or demand savings
  - Beneficial to all customers in the customer class, regardless of whether all customers participated in the program

Commission Authority

- The Missouri Commission has been given the statutory authority to approve utility-specific energy efficiency tariffs. The Commission has not yet approved any utility-specific programs under the statute, but plans are currently before the Commission for approval. The first plans should be approved by the end of 2012.

Demand Side Mechanism Approval

- The Missouri Public Service Commission has interpreted the energy efficiency act to allow program approval and cost recovery outside of normal ratemaking proceedings
- The utility submits an application for program approval to the Commission
- Applications must be approved or rejected by the Commission within 120 days; there must be an opportunity for a hearing

Demand Side Investment Mechanism approval, cont.

- The Missouri Public Service Commission shall approve the establishment, continuation, or modification of a demand side investment mechanism if it finds that the programs are:
  - Expected to result in energy and demand savings
  - Beneficial to all customers in the customer class
  - Will assist the Commission’s efforts to implement the state’s energy efficiency policies

Demand Side Investment Mechanism approval, cont.

- Factors the Commission may consider include but are not limited to:
  - The magnitude of the impact on the utility's costs, revenues, and earnings
  - The utility's ability to manage the program
  - The ability to measure and verify the program's impacts
  - Interaction among the various components of the proposed program

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Demand Side Investment Mechanism approval, cont.

- The incentives or disincentives to the utility as a result of the inclusion or exclusion of utility cost recovery component, utility lost revenue component and/or utility incentive component of a demand side investment mechanism

“Disincentive” means any barrier to implementation

Demand Side Investment Mechanism approval, cont.

- To be approved, a proposed demand side investment mechanism with a total resource cost test with a ratio greater than 1 must meet the following criteria:
  - Be consistent with the goal of achieving all cost-effective demand side savings
  - Have reliable evaluation, measurement, and verification plans
  - Are included in the utility's preferred resource plan or have been verified through an integration process showing the impact of the program on the net present value of the utility's revenue requirement

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Demand Side Investment Mechanism approval, cont.

- The Missouri Commission shall approve demand-side programs having a total resource cost ratio of less than 1 for demand-side programs targeted to low-income customers or general education campaigns if the Commission determines the program is in the public interest and all other filing and submission requirements have been met.

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Demand Side Investment Mechanism approval, cont.

- If a proposed demand-side investment mechanism is targeted to low-income customers, the utility must state how it will assess the expected and actual effect of the program on the utility's bad debts, customer arrearages, and disconnections.

Demand Side Investment Mechanism approval, cont.

- The Missouri Commission shall approve demand-side programs with a total cost ratio of less than 1 if filing requirements have been satisfied and the costs of the programs above the level that is determined to be cost-effective are funded by customers participating in the programs or other governmental credits or incentives designed for that purpose.

Tax credits and monetary incentives

- A customer that has received a state tax credit is not eligible for participation in a demand-side programs that offer a monetary incentive to participate.
- A customer participating in a program that offers a monetary incentive shall attest that no tax credits have been received.
- The utility must maintain a database of participants in programs with monetary incentives.
- The customer names must be available to the Commission upon request.

Implementation of a demand side investment mechanism

- Once a demand side investment mechanism is approved, the utility may request deferral accounting using its latest approved weighted average cost of capital until its next rate case.
- An approved program shall not remain in effect more than four years.
- A utility must file a general rate case within four years of having a demand side program approved.
- Any amount charged to customers shall be shown as a separate line item on bills.

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Implementation of demand side investments mechanisms, cont.

- Evaluation, measurement, and verification of demand side programs must be performed by an independent contractor who is hired and paid for out of the Missouri Public Service Commission's annual assessment to utilities.
- The utility must file an annual report.
- The utility must submit surveillance monitoring reports.
- Prudence reviews must be conducted no less frequently than 24-month intervals.

Utility Incentive Mechanisms in Missouri

- When it drafted rules to implement the Missouri Energy Efficiency and Investment Act, the Missouri commission chose three utility incentive mechanisms:
  - Utility cost recovery revenue requirement
  - Utility incentive revenue requirement
  - Utility lost revenue recovery requirement

Utility Cost Recovery Revenue Requirement

- This incentive mechanism is intended to allow the utility to recovery its costs associated with the implementation of demand side or energy efficiency programs.
  - These costs are based on the utility's contemporaneous accounting records
  - Recoverable semi-annually

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Utility Incentive Revenue Requirement

- This incentive mechanism is intended to give the utility an opportunity to share in the annual net shared benefit from energy efficiency or demand-side programs:
  - Benefits of the program are shared between utilities and ratepayers
  - Subject to measurement and verification by an independent evaluator
  - Recovery is possible between rate cases based on the availability of the independent evaluator’s reports

Utility Lost Revenue Recovery Requirement

- This incentive mechanism is intended to allow utilities to recover the revenue that is "lost" as a result of decreased demand:
  - Only allowed if the utility does not earn its revenue requirement as determined in its most recent rate case
  - Subject to measurement and verification by an independent evaluator
  - Recovery is retrospective only and is dependent on the availability of the evaluator's independent reports

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Opt-out for large customers

- Under the rules adopted by the Missouri Public Service Commission to implement the energy efficiency act, large consumers can opt out of participation in energy efficiency programs.

MEEIA Rules

- The Missouri Commission has adopted four rules to implement the Missouri Energy Efficiency and Investment Act
  - The rules were appealed by utilities, by consumer advocates, and by large consumers of electricity
  - The most controversial component of the rules is the lost revenue recovery mechanism
  - It is not known at this time whether the rules will be upheld