BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of a Working Case to Consider Proposals to Create a Revenue Decoupling Mechanism for Utilities	)))	Case No. AW-2015-0282

COMMENTS OF SIERRA CLUB ON DECOUPLING FOR ELECTRIC UTILITIES

Sierra Club appreciates the opportunity to provide comments to the Commission, Staff, and stakeholders on revenue decoupling. Sierra Club limits its comments to addressing revenue decoupling for electric utilities. In addition to the below comments, Sierra Club also joins the comments submitted today by Renew Missouri and other organizations on the legality of revenue decoupling for electric utilities as a rate design modification under the Missouri Energy Efficiency Investment Act ("MEEIA"), which can be implemented pursuant to a Commission rulemaking under § 393.1075.5, RSMo. The below comments note that the Commission also has discretion to utilize revenue decoupling as a form of demand-side investment mechanism ("DSIM") under existing MEEIA rules. Sierra Club also urges the Commission and Staff to focus their efforts in this docket on revenue decoupling adjustment mechanisms that do not involve increases in fixed customer charges or straight-fixed variable ("SFV") rate designs. Finally, Sierra Club commends to the Commission and stakeholders testimony from the pending Kansas City Power & Light rate case, Case No. ER-2014-0370, that addresses how to design a revenue decoupling adjustment mechanism to maximize the benefit to customers and ensure their interests are protected.

I. Decoupling for Electric Utilities Is Authorized under the MEEIA Statute and Rules.

Revenue decoupling for electric utilities is authorized under Missouri law by the language of MEEIA and the decision of the Court of Appeals Western District upholding the Commission's MEEIA rules, *State ex rel. Public Counsel v. PSC*, 397 S.W.3d 441 (Mo.App. W.D. 2013). In that decision, the Court held that MEEIA authorizes the Commission to approve demand-side investment mechanisms ("DSIMs") that allow for rates to be adjusted outside a general rate case proceeding to recover the costs, including lost revenues due to declining sales, of demand-side investments. *Public Counsel*, 397 S.W.3d at 448-453.

The separate comments filed in this docket by Renew Missouri and other organizations on the legality of decoupling for electric utilities, which Sierra Club joins, focus on implementation of a revenue decoupling adjustment mechanism as a "rate design modification" through a rulemaking pursuant to MEEIA, § 393.1075.5, RSMo. As an alternative approach, a revenue decoupling adjustment mechanism can also be structured as a DSIM under the Commission's MEEIA rules as currently promulgated.

MEEIA gives the Commission authority to develop, without limitation, demand-side cost recovery mechanisms:

> To comply with [the statute], the commission may develop cost recovery mechanisms to further encourage investments in demand-side programs *including, in combination and without limitation*: capitalization of investments in and expenditures for demand-side programs, rate design modifications, accelerated depreciation on demand-side investments, and allowing the utility to retain a portion of the net benefits of a demand-side program for its shareholders.

§ 393.1075.5, R.S.Mo (emphasis added).

The MEEIA rules, in turn, give the Commission the authority to approve a broad range of mechanisms, defining the DSIM as:

> A mechanism approved by the commission in a utility's filing for demand-side program approval to encourage investments in demand-side programs. The DSIM *may include,* in combination and *without limitation*:
>
> > 1. Cost recovery of demand-side program costs through capitalization of investments in demand-side programs;
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> > 2. Cost recovery of demand-side program costs through a demand-side program cost tracker;
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> > 3. Accelerated depreciation on demand-side investments;
> >
> > 4. Recovery of lost revenues; and
> >
> > 5. Utility incentive based on the achieved performance level of approved demand-side programs.

4 CSR 240-20.093(1)(M) (emphasis added). This definition makes clear that the structure of the DSIM is not limited to the specific components listed in the rule, but can include "without limitation" any "mechanism . . . to encourage investments in demand-side programs," which would undeniably include decoupling mechanisms, that remove the disincentive from investing in such programs. *Id.* Moreover, even if the list of DSIM components in 4 CSR 240-20.093(1)(M) is construed as exhaustive (notwithstanding the rule's plain language to the contrary), a decoupling mechanism still fits within the current MEEIA rules if it is structured to adjust rates to account for any decline in sales below the utility's authorized revenue requirement due to implementation of demand-side programs. Although decoupling mechanisms can be structured more broadly to account for other changes in revenue that occur between rate cases, removal of the "throughput disincentive" to investing in energy efficiency is a compelling justification for implementing decoupling, and the MEEIA rules provide ample authority for the Commission to adopt this approach for electric utilities.

Moreover, the MEEIA rules provide that "[i]n addition to any other changes in business risk experienced by the electric utility, the commission shall consider changes in the utility's

business risk resulting from establishment, continuation, or modification of the DSIM in setting the electric utility's allowed return on equity in general rate proceedings." 4 CSR 240-20.093(2)(D).

II. Revenue Decoupling Should be Explored as Way to Eliminate the Throughput Disincentive for Electric Utilities and Advance Energy Efficiency.

The pending Ameren MEEIA case, EO-2015-0055, demonstrates the importance of exploring revenue decoupling as a way to remove utility disincentives to pursue energy efficiency under MEEIA. In that case, parties to two contested, non-unanimous stipulations proposed competing throughput disincentive mechanisms. These mechanisms—and how to align Ameren's incentives with promoting energy efficiency more generally—proved to be the most contentious aspect of the case, raising complex technical and policy issues.

Numerous parties in the case, including Ameren, Staff, the Division of Energy, NRDC, Renew Missouri, and Sierra Club, expressed a desire or willingness to explore revenue decoupling as an alternative mechanism to overcome the throughput disincentive. For example, at the evidentiary hearing, Commission Staff testified that the parties "wouldn't be sitting here today if there was a form of revenue decoupling that had been vetted and had become part of this process."[1] Similarly, in response to a question from former Chairman Kenney about whether decoupling for electric utilities would obviate concerns raised in the case, Ameren's counsel stated that decoupling, if done properly, "should remove the throughput disincentive ... it would take great steps to resolving issues" in the case.[2] Revenue decoupling is a cost-recovery mechanism that the Commission "may develop" to comply with MEEIA. § 393.1075.5, RSMo, and the pending MEEIA case illustrates the value in doing so in this docket.

[1] Tr. at 776:19-22, EO-2015-0055, EFIS No. 168.

[2] *Id.* at 39:4-13, EFIS No. 166.

III. A Revenue Decoupling Adjustment Mechanism Is a Far Better Option to Address Concerns Over Flat or Declining Sales Than Increased Fixed Customer Charges or Straight Fixed Variable Rate Design.

Revenue decoupling also recently became an issue in the pending Kansas City Power & Light rate case, Case No. ER-2014-0370. In that proceeding, Sierra Club presented direct and surrebuttal testimony from Tim Woolf of Synapse Energy Economics in opposition to the Company's proposed increase of its fixed charge for residential customers from $9 per month to $25 per month.[3] Mr. Woolf testified that a revenue decoupling adjustment mechanism presents a far better option for managing utility revenue sufficiency and volatility than do increases to fixed customer charges, because a decoupling mechanism both incentivizes energy efficiency and better adheres to fundamental ratemaking principles of efficiency, equity, and gradualism.[4] In response to Mr. Woolf's testimony, KCP&L agreed that revenue decoupling could help address the Company's concerns over flat or declining sales that motivated its proposed fixed charge increase, and the Company expressed support for the Commission investigating a revenue decoupling adjustment mechanism in this docket.[5]

At the hearing in Case No. ER-2014-0370, Mr. Woolf also made clear that, when he uses the term "decoupling," he is not referring to SFV rate designs.[6] A number of Missouri stakeholders appear to consider SFV rate design to be a form of "decoupling," and in particular use that term with respect to rate designs currently in place for natural gas utilities, because

[3] Direct and Surrebuttal Testimony of Tim Woolf, Case No. ER-2014-0370, Exs. 400 and 401, EFIS Nos. 427 and 428.

[4] Direct Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 400, EFIS No. 427, at 24-27.

[5] Tr. at 373:17--374:2, Case No. ER-2014-0370, EFIS No. 297.

[6] *Id.* at 431:1-6, 438:16-441:6.

under a SFV rate design, customers do not pay for service on a primarily volumetric basis.[7] But as both Mr. Woolf's testimony at the hearing in Case No. ER-2014-0370 and the Regulatory Assistance Project white paper make clear, SFV rate designs create a "dramatically diminished" incentive for customers to consume energy efficiently and to invest in energy efficiency.[8] As Mr. Woolf testified, a revenue decoupling adjustment mechanism is "just a more refined, more precise way to match revenues to cost."[9] Accordingly, Sierra Club strongly urges the Commission and Staff to focus their investigation in this docket on revenue decoupling adjustment mechanisms that do not involve increases in fixed customer charges or SFV rate designs.

IV. Concerns Raised about Decoupling Can Be Addressed through the Design of the Mechanism.

A critical question for investigation in this docket is how to design a revenue decoupling adjustment mechanism to maximize the benefit to customers and ensure their interests are protected. In his testimony in Case No. ER-2014-0370, Mr. Woolf recommended that the following customer protection measures be considered as part of the design of any revenue decoupling mechanism:

1. Allowed revenue targets under a decoupling mechanism can be established through a fully-litigated rate case with active participation from stakeholders. Relatively frequent rate cases can be used to ensure that the utility's allowed revenues remain in line with its actual costs.

[7] *See* Regulatory Assistance Project, "Revenue Regulation and Decoupling: A Guide to Theory and Application," at 42 (June 2011).

[8] Tr. at 440:17-21, Case No. ER-2014-0370, EFIS No. 297; *see also* Regulatory Assistance Project, "Revenue Regulation and Decoupling: A Guide to Theory and Application," at 42 (June 2011).

[9] Tr. at 439:22-23, Case No. ER-2014-0370, EFIS No. 297.

2. Decoupling adjustments can be made on a fixed, pre-determined schedule to provide some stability and predictability.
3. Decoupling adjustments can be subject to a cap in order to protect customers from significant rate increases from one period to the next.
4. The utility's allowed return on equity can be reduced to reflect any lower risk that the utility faces as a result of reduced volatility in revenues, as appropriate.
5. The utility can be required to make reasonable commitments toward supporting cost-effective demand-side resources, or other measures to support customers, in return for reducing revenue volatility.[10]

The Regulatory Assistance Project paper that Staff has cited as a resource guide for this docket includes similar recommendations.[11] Indeed, Mr. Woolf included this paper as an exhibit to his testimony in Case No. ER-2014-0370.

In addition, Mr. Woolf's testimony in Case No. ER-2014-0370 responds to a number of commonly raised concerns about revenue decoupling, four of which we highlight here. First, Mr. Woolf testified that a decoupling mechanism can be designed to avoid significant increases in customer risk by managing any increased volatility in customers' bills.[12] In particular, as noted above, a decoupling mechanism can be designed to include a cap on the amount of the adjustment.[13]

[10] Direct Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 400, EFIS No. 427, at 28.

[11] Regulatory Assistance Project, "Revenue Regulation and Decoupling: A Guide to Theory and Application," at 44-50 (June 2011).

[12] Direct Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 400, EFIS No. 427, at 29-30; *see also* Regulatory Assistance Project, "Revenue Regulation and Decoupling: A Guide to Theory and Application," at 45 (June 2011).

[13] Direct Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 400, EFIS No. 427, at 29-30.

Second, Mr. Woolf testified that, rather than reducing a utility's incentive to control its costs, decoupling actually strengthens those incentives.[14] This is because a revenue decoupling adjustment mechanism fixes the utility's revenue to the authorized revenue requirement from its last rate case, leaving cost reduction as the primary way that a utility can increase profits between rate cases.[15]

Third, Mr. Woolf rejected arguments that a revenue decoupling adjustment mechanism would reduce customers' incentive to consume energy more efficiently.[16] According to Mr. Woolf, "[r]evenue decoupling will have essentially no impact on any one customer as a result of his or her efficiency investments because the magnitude of the decoupling adjustment from any one customer's efficiency efforts would be so small as to be unnoticeable by the customer, and would be completely dwarfed by the . . . reduction in the customer's electric bill" as a result of those investments.[17]

Fourth, Mr. Woolf responded in his surrebuttal testimony to MIEC witness Greg Meyer's concern that, with a revenue decoupling adjustment mechanism in place, utilities would have a reduced incentive to restore power after a storm, because their revenues would no longer be tied to sales.[18] Mr. Woolf testified that, although it is theoretically true that utilities' financial

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[14] *Id.* at 30.

[15] *Id. see also* Regulatory Assistance Project, "Revenue Regulation and Decoupling: A Guide to Theory and Application," at 45-46 (June 2011).

[16] Direct Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 400, EFIS No. 427, at 30-31.

[17] *Id.*; *see also* Tr. 424:25-425:14, Case No. ER-2014-0370, EFIS No. 297 (noting a correction to this portion of pre-filed testimony).

[18] Rebuttal Testimony of Greg R. Meyer, Case No. ER-2014-0370, Ex. 559, EFIS No.443, at 9. Mr. Meyer's rebuttal testimony in this case also raised concerns with revenue decoupling that are more legal concerns than policy concerns, such as that revenue decoupling is single-issue ratemaking or retroactive ratemaking. Mr. Woolf responded to those concerns as well in his testimony in his surrebuttal testimony in Case No. ER-2014-0370, Ex. 401, EFIS No. 428. The separate memorandum on the legality of decoupling submitted today in this docket by Renew Missouri and other organizations, which Sierra Club joins, also addresses these concerns.

incentive to restore power would be reduced, "this reduced incentive would not result in prolonged outages."[19] Not only would utilities be motivated to restore power quickly due to concerns over public backlash and criticism from elected officials, but also the Commission would retain authority to investigate outages and impose penalties.[20] The relatively small amount of increased revenue that a utility might collect through a decoupling adjustment mechanism "would not create a meaningful incentive for a utility to delay power restoration" after a storm.[21]

V. Conclusion

Sierra Club urges the Commission, Staff, and other stakeholders to use this docket to develop an appropriate design for a revenue decoupling adjustment mechanism for Missouri electric utilities that regulates utility revenues, incentivizes energy efficiency, and protects customer interests.

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Respectfully submitted,

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[19] Surrebuttal Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 401, EFIS No. 428, at 9.

[20] *Id.*; *see also* Regulatory Assistance Project, "Revenue Regulation and Decoupling: A Guide to Theory and Application," at 49 (June 2011).

[21] Surrebuttal Testimony of Tim Woolf, Case No. ER-2014-0370, Ex. 401, EFIS No. 428, at 9.