BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of an Investigation into the	)	
Coordination of State and Federal Regulatory	)	
Policies for Facilitating the Deployment of all	)	File No. EW-2010-0265
Electric Customers of All Classes Consistent	)	
With the Public Interest	)	

LEGAL MEMORANDUM OF NRDC, GRELC, MCE, MEEA, MVC AND SIERRA CLUB

The Natural Resources Defense Council, Great Rivers Environmental Law Center, the Missouri Coalition for the Environment, Missouri Votes Conservation, the Midwest Energy Efficiency Alliance and the Sierra Club submit this legal memorandum to address the legal issues raised in this docket concerning the scope and interpretation of SB 376.

Statutory Authority: Cost Recovery

The Commission's authority to allow cost recovery outside a general rate case is delegated by SB 376, which requires the PSC to allow "timely cost recovery" for DSM programs. § 393.1075.3(1). It would be unnecessary to specify this unless it meant something other than recovery in a general rate case.

The issue invites comparison to *State ex rel. UCCM v. PSC,* 585 S.W.2d 41 (Mo. Banc 1979), which held that the Commission did not have statutory authority to allow periodic recovery of fuel costs through an FAC. No law then permitted such a departure from general rate making in a proceeding that allowed consideration of all relevant factors. 585 S.W.2d at 51–8. Rate making procedure is statutory, however, and may be amended by a subsequent statute.

UCCM lays out the guiding principles. The Commission has only the powers conferred on it by statute, "either expressly, or by clear implication as necessary to carry out the powers specifically granted." The Commission statutes are to be liberally construed to effectuate their remedial purpose, but convenience, expediency and even necessity are not to be considered in determining whether an act of the Commission is authorized. If the commission does have the authority to act, then it has broad discretion in setting just and reasonable rates. 585 S.W.2d at 49. This discretion operates only within the circumference of the powers granted by the legislature; the Commission's general supervisory authority over utilities does not give it the authority to change the legislative rate making scheme. 585 S.W.2d at 56.

Unlike § 386.266, RSMo (FAC and ECRM) and §§ 393.1000–1015, RSMo (ISRS), the Missouri Energy Efficiency Investment Act (MEEIA) does not expressly say that costs can be recovered outside a general rate case, but it does so by clear implication.

Every clause of a statute must be given meaning. The legislature is not presumed to have intended a useless act. In enacting a new law, the intent of the legislature is ordinarily to effect some change in existing law. *Cub Cadet Corp. v. Mopec, Inc.*, 78 S.W.3d 205, 214–5 (Mo.App. WD 2002).

The MEEIA is the legislature's first specific delegation of PSC authority over DSM. It aims to give demand-side investments equal value with supply-side, § 393.1075.3, "with a goal of achieving all cost-effective demand-side savings." § 393.1075.4. Cost-recovery must be "timely," § 393.1075.3(1), which contemplates that the interval between rate cases may not be timely enough, or it would not need to be stated. Cost recovery is contingent on Commission approval of demand-side programs, but is not explicitly tied to rate cases. § 393.1075.4.

The law gives the Commission discretion to “develop cost recovery mechanisms to further encourage investments in demand-side programs including, in combination and without limitation” certain examples. § 393.1075.5. The Commission “may adopt rules and procedures…as necessary, to ensure that electric corporations can achieve the goals of this section.” § 393.1075.11. This acknowledges that special mechanisms are needed that are different from those found in traditional rate making. These are left to the discretion of the Commission.

The MEEIA carves out a limited exception to the general rate making scheme. It would not, for example, authorize retroactive rate making. See *State ex rel. AG Processing v. PSC,* WD 70799 (Mo.App. March 23, 2010). It does, however, recognize that demand-side investments are different from traditional supply-side investments and require separate treatment. To that extent, the statute does authorize “single-issue rate making,” or more accurately cost recovery that considers all factors relevant to demand-side rate making. Cost recovery under the MEEIA is contingent on many factors not normally present in rate cases. It involves incentives, earnings opportunities tied to energy savings, a cost-effectiveness test, low-income programs that need not meet a cost-effectiveness test, savings that are beneficial to all customers in a class even if not all customers utilize the programs, exemption of opt-out customers from demand-side charges only, and annual reports specific to demand-side programs.

Successful efficiency programs reduce sales. “The more uncertain the process for determining the prudence of expenditures, and the longer the time between an expenditure and its recovery, the greater the perceived financial risk and the less likely a utility will be to aggressively pursue energy efficiency.” The National Action Plan for Energy Efficiency, “Aligning Utility Incentives with Investments in Energy Efficiency” (2007), p. ES-2. Such a result would be contrary to the explicit goals of the MEEIA.

Read as a whole, the statute delegates authority to the Commission to oversee utility demand-side programs, and within that authority is broad discretion to determine what cost recovery mechanisms are “timely” and advance the goal of promoting demand-side investments.

The originally introduced version of SB 376 provided for a “cost adjustment clause.” This was later removed. However, the original bill did not include “timely cost recovery.” The effect of the substitution was to broaden, not narrow, the Commission’s discretion.

Applicable precedents are very sparse, but see *Georgia Power Co. v. Georgia Industrial Group,* 214 Ga.App.196, 447 S.E.2d 118 (1994). The court upheld a demand-side cost recovery rider under a statute that allowed recovery of costs and incentives “in rates.” The court reasoned that the statute was a departure from traditional rate-of-return rate making, though the statute did not explicitly authorize a rider. 447 S.E.2d at 120–1.

Decoupling: Statutory Authority and Rate Design

The Energy Independence and Security Act of 2007, § 532, added the following standard to the PURPA § 111(d)(26 USCA § 2621(d)) standards that a state must consider:

(17) RATE DESIGN MODIFICATIONS TO PROMOTE ENERGY EFFICIENCY INVESTMENTS.—

(A) IN GENERAL.—The rates allowed to be charged by any electric utility shall—

(i) align utility incentives with the delivery of cost-effective energy efficiency; and

(ii) promote energy efficiency investments.

(B) POLICY OPTIONS.—In complying with subparagraph (A), each State regulatory authority and each nonregulated utility shall consider—

(i) *removing the throughput incentive* and other regulatory and management disincentives to energy efficiency;

(ii) **providing utility incentives** for the successful management of energy efficiency programs;

(iii) including the impact on adoption of energy efficiency as 1 of the goals of retail rate design, recognizing that energy efficiency must be balanced with other objectives;

(iv) **adopting rate designs that encourage energy efficiency** for each customer class;

(v) **allowing timely recovery of energy efficiency-related costs**; and

(vi) offering home energy audits, offering demand response programs, publicizing the financial and environmental benefits associated with making home energy efficiency improvements, and educating homeowners about all existing Federal and State incentives, including the availability of low-cost loans, that make energy efficiency improvements more affordable.

The policies highlighted in bold are incorporated in the Missouri Energy Efficiency Investment Act, particularly subsection § 393.1075.3, making this docket the proper forum for consideration of the new PURPA standard, including removal of the throughput incentive.

Section 410 of the American Recovery and Reinvestment Act of 2009 (ARRA) made it a condition of receiving grant money ("stimulus funds") that the governor of a state assure the Secretary of Energy that these policies will actually be implemented.

SEC. 410. ADDITIONAL STATE ENERGY GRANTS. (a) IN GENERAL.—

> Amounts appropriated under the heading ‘‘Department of Energy—Energy Programs—Energy Efficiency and Renewable Energy’’ in this title shall be available to the Secretary of Energy for making additional grants under part D of title III of the Energy Policy and Conservation Act (42 U.S.C. 6321 et seq.). The Secretary shall make grants under this section in excess of the base allocation established for a State under regulations issued pursuant to the authorization provided in section 365(f) of such Act only if the governor of the recipient State notifies the Secretary of Energy in writing that the governor has obtained necessary assurances that each of the following will occur:
>
> (1) The applicable State regulatory authority will seek to implement, in appropriate proceedings for each electric and gas utility, with respect to which the State regulatory authority has ratemaking authority, **a general policy that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently and that provide timely cost recovery and a timely earnings opportunity for utilities associated with cost-effective measurable and verifiable efficiency savings, in a way that sustains or enhances utility customers’ incentives to use energy more efficiently.**

The bolded language, slightly rearranged, is incorporated almost verbatim in the Missouri Energy Efficiency Investment Act, subsection 3, especially subdivisions (1)–(3). The MEEIA also refers to “rate design modifications” as a way to encourage demand-side investments. § 393.1075.5.

Even independently of federal law, Missouri law includes under the heading of “rate design” mechanisms that decouple revenue from sales and remove the utility’s incentive to sell more gas or electricity. *State ex rel. OPC v. PSC,* 293 S.W.3d 63, 73–4 (Mo.App. S.D.2009);

State ex rel. Public Counsel v. PSC, 289 S.W.3d 240, 251 (Mo.App. W.D. 2009). See also *Ohio Consumers' Counsel v. PUC,* 2010 Ohio 134, 2010 WL 323283 (Ohio Jan. 26, 2010), which considers a sales decoupling rider as a rate design mechanism (p. 3 ¶ 3; p. 11 ¶ 37).

The MEEIA's derivation from federal law makes this conclusion inescapable. Decoupling is a matter of both rate design and aligning utility and customer incentives by removing the throughput incentive. The "Reference Manual and Procedures for Implementation of the 'PURPA Standards' in the EISA of 2007" (APPI, EEI, NARUC and NRECA 2008; http://www.naruc.org/resources.cfm?p=145) treats decoupling under the "rate design modification" standard (pp. 47, 52–3). Whatever it may mean elsewhere, in the context of § 111(d)(17) rate design includes decoupling.

Even if decoupling is not considered a matter of rate design, it falls under § 393.1075.3(2), aligning utility financial incentives with energy efficiency. The National Action Plan for Energy Efficiency, "Aligning Utility Incentives with Investments in Energy Efficiency" (2007), Chapter 5, deals with decoupling as an important part of aligning incentives because it removes the throughput incentive.

Lost revenue recovery is usually considered as an alternative to decoupling. However, it does not remove the throughput incentive. NAPEE, "Aligning Utility Incentives," p. 5-10. It does not meet the goals of the PURPA standard, ARRA or the MEEIA and should not be considered in this rulemaking.

Cost Recovery and EM&V

Staff takes the position that cost-recovery is not allowed by SB 376 until evaluation, measurement and verification of programs has been completed (4/8/10 draft rule §§ 7B, 9A.vi). This must be based on the clause in 393.1075.4, "Recovery for such programs shall not be permitted unless the programs…result in energy or demand savings…” This phrase does not say “have resulted in” savings; does not say savings must be proved by EM&V; does not mention EM&V. Taking the statute as a whole and considering the context, it does not lead to the conclusion Staff has drawn.

The MEEIA requires the Commission to provide “timely cost recovery” and “timely earnings opportunities associated with cost-effective measurable and verifiable [not measured and verified] efficiency savings,” § 393.1075.3(1) and (3). There is no reason why earnings opportunities, but not cost recovery, should be allowed without EM&V. That is not the intent of the law.

Cost recovery mechanisms are dealt with in 393.1075.5, and the list of such mechanisms includes “capitalization of investments in and expenditure 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.” There is no separation of cost recovery from earnings opportunities here. Instead, various kinds of earnings opportunities are treated under the heading of cost recovery.

The intent becomes clear when we consider the source of 393.1075.3, ARRA § 410: “provide timely cost recovery and a timely earnings opportunity for utilities associated with cost-effective measurable and verifiable efficiency savings.” For both cost recovery and earnings opportunities, only “measur*able* and verifi*able*” savings are required. The separation of phrases from ARRA into 393.1075.3(1–3) appeared to break the link, but that was not intended.

The purpose of cost recovery mechanisms is “to further encourage investments in demand-side programs.”§ 393.1075.5. The only reference to evaluation is in 393.1075.11:

"independent evaluation of demand-side programs…to ensure that electric corporations can achieve the goals of this section." Promoting DSM is the guiding purpose of the MEEIA.

There may be a time lag of several years between roll-out of a program and completion of EM&V. Delaying recovery, especially as programs start to move up the cost curve, might lead utilities not to propose or implement cost-effective programs. That would be directly contrary to the intent of the MEEIA.

MEDA: EUIC

MEDA in its "Working Draft" rule proposes to include in demand-side programs electric utility infrastructure projects (EUIC), defined in (1)H.i as:

> Electric utility infrastructure projects means projects owned by an electric utility that:
> i .Replace or modify existing electric utility infrastructure, including utility-owned buildings, if the replacement or modification is shown to conserve energy or use energy more efficiently

We disagree. EUIC is not within the scope of SB 376, which defines demand-side programs to mean only programs that "modify the net consumption of electricity on the retail customer's side of the electric meter," § 393.1075.2(3). It defines energy efficiency in terms of end-use efficiency. § 393.1075.2(4). However desirable EUIC may be, more efficient delivery of energy by the utility does not in itself affect customers' net consumption. Nothing in MEDA's proposed treatment of EUIC in § (6) of its working draft ensures or requires that this condition will be met.

There may be system benefits or costs from EUIC that could indirectly cause customers to reduce — or increase — consumption. That would merely be incidental to EUIC, whereas under SB 376 reducing customers' energy consumption must be the purpose of the program.