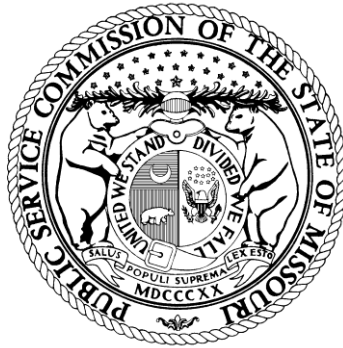


**MISSOURI PUBLIC SERVICE COMMISSION**

**STAFF REPORT ON THE MATTER OF AN  
INVESTIGATION OF THE EFFECTS OF RATE  
DESIGN MODIFICATIONS  
ASSOCIATED WITH DEMAND-SIDE COST  
RECOVERY**



**FILE NO.  
EW-2011-0372**

*Jefferson City, Missouri  
January 11, 2013*

**Staff Report**  
**File No. EW-2011-0372**  
***In the Matter of an Investigation of the Effects of Rate Design Modifications***  
***Associated with Demand-Side Cost Recovery***

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**January 11, 2013**

**BACKGROUND**

On August 28, 2009, the Missouri Energy Efficiency Investment Act (“MEEIA”)<sup>1</sup> went into effect, thus establishing “...the policy of the state to value demand-side investments equal to traditional investments in supply and delivery infrastructure and allow recovery of all reasonable and prudent costs of delivering cost-effective demand-side programs.”<sup>2</sup> The Commission subsequently promulgated rules to establish the framework for implementing various provisions of MEEIA. Those rules became effective May 30, 2011.<sup>3</sup>

On May 13, 2011, Staff filed a motion to open File No. EW-2011-0372. In its motion Staff focused on the last sentence of section 393.1075.5, RSMo. (Supp. 2010), which provides:

Prior to approving a rate design modification associated with demand-side cost recovery, the commission shall conclude a docket studying the effects thereof and promulgate an appropriate rule.

Staff noted it would be beneficial to obtain input from stakeholders on the meaning of this language (“Rate Design Language”) and how the Commission might carry out this legislative directive. On May 26, 2011, the Commission established this File as the repository for documents and comments regarding the effects of rate design modifications associated with demand-side cost recovery.

On December 12, 2012, Staff brought the issue back to the Commissioners in Agenda, seeking guidance on how to proceed. The Commissioners asked for a written report of activities to date, recommendations on how to proceed, and what rate design modification proposals have been sufficiently studied and those requiring further study. Activities related to this File are summarized and discussed below.

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<sup>1</sup> Section 393.1075 RSMo. Supp. 2011

<sup>2</sup> Section 393.1075.3

<sup>3</sup> 4 CSR 240-3.163; 4 CSR 240-3.164; 4 CSR 240-20.093; 4 CSR 240-20.094

## **ACTIVITIES TO DATE**

### **Workshop Regarding Rate Design Modifications for Demand-Side Programs**

On June 29, 2011, Staff led a workshop regarding Rate Design Modifications for Demand-Side Programs. Staff asked stakeholders<sup>4</sup> for technical and legal perspectives regarding the meaning of the Rate Design Language, specifically soliciting comments to the following questions:

- Meaning of Statutory Language
- What is meant by “rate design modification”?
- What is decoupling?
- Is decoupling a rate design modification?
- Is decoupling lawful in Missouri?
- What is meant by “cost recovery”?
- What is meant by “study the effects”? What are we to study the effects on?  
Rates, utility earnings, customer savings etc.?
- Other issues related to statutory language
- How to Fulfill Legislative Directive:
- What is the relationship of a rate design modification to the MEEIA rules?
- How does this process start: Does the statutory language mean that we first need a specific proposal to study?
- Other issues related to how to fulfill legislative directive

Stakeholders were asked to submit written comments by July 22, 2011, addressing the questions and discussing next steps. A summary of workshop and written comments received is discussed later in this Report.

### **In-House Rate Design Training**

On November 22, 2011, at the Commission Agenda session, Staff presented a summary of the various stakeholder comments and the Commission began discussing its interpretation of the Rate Design Language. The Commission provided direction that it would be beneficial to receive in-house training designed to educate Commissioners and Staff on various rate design options that could be considered in addressing the need to promulgate a general rule implementing the Rate Design Language.

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<sup>4</sup> Several stakeholders participated in the process, including Staff, Noranda, Missouri Industrial Energy Consumers (MIEC), Great Rivers Environmental Law Center (GRELC), Kansas City Power and Light (KCP&L), The Empire District Electric Company, Jim Fischer, Honeywell, Missouri Department of Natural Resources (MDNR), Finnegan, Conrad and Peterson L.C., Missouri Office of Public Counsel (OPC), David Linton, Landis+Gyr, Ameren Missouri, Morgan Marketing, Missouri Energy Development Association (MEDA), Renew Missouri, Wal-Mart, Ag Processing Inc., Missouri Energy Group (MEG)

On December 22, 2011, the Staff sought input from stakeholders concerning which rate design modifications should be included in the educational workshop and suggestions on who should make presentations at the workshop. The Commission released an Invitation for Bid and selected Electric Utility Consultants, Inc. (EUCI) to provide the requested training.

On March 20, 2012, the Commission hosted the training, with Dr. Michael R. Schmidt presenting “Electric Rate Design Modifications Associated With Demand-Side Cost Recovery.” The rate design training included the following design options: flat block rates, straight-fixed variable, inclining and declining block rates, customer class specific rate structures, time-of-use rates, seasonal rates, real time pricing and decoupling.

#### MEEIA Filings

Since the March 2012 workshop, the Commission has approved MEEIA stipulations and agreements for Ameren Missouri<sup>5</sup> and KCP&L Greater Missouri Operations Company.<sup>6</sup> While both stipulations contained variances from the Commission’s MEEIA rules on such things as retrospective recovery and recovery based on evaluation, measurement and verification, the stipulations did not incorporate any modifications to Commission-approved rate designs. Instead, recovery of the companies’ program costs and lost fixed costs will occur through the companies’ base rates or a rider.

#### **SUMMARY OF STAKEHOLDER COMMENTS - RATE DESIGN LANGUAGE**

Following is a general summary of stakeholder comments concerning rate design modifications associated with demand-side cost recovery. For more specific details and supporting documents, Staff refers the Commission to each stakeholder’s comments in File No. EW-2011-0372 and the archived webcast of the June 29, 2011 workshop.

#### Ag Processing Inc.:

1. Revenue decoupling should not be a consideration because it:
  - a. Represents a significant departure from traditional cost of service principles;
  - b. Immunizes utility earnings from sales fluctuations;
  - c. Undermines customer energy efficiency efforts;
  - d. Penalizes ratepayers for their own investments in energy efficiency and conservation;
  - e. Shifts business risk from utility to customer;
  - f. There is no good evidence that decoupling drives utilities to invest in energy efficiency;
  - g. Utilities will still want 10%+ rate of return despite decreased business risk.
2. If a utility is truly hurt by a decrease in revenues caused by energy efficiency, then it has the option to file for a rate increase in today’s regulatory arena. Under a contested case, all issues can be reviewed to determine if a rate increase is warranted.
3. Decoupling supports single-issue ratemaking and runs contrary to the regulatory process where a utility is allowed a fair rate of return and not a guaranteed level of revenues.

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<sup>5</sup> See: Case Number EO-2012-0142.

<sup>6</sup> See: Case Number EO-2012-0009.

### Honeywell<sup>7</sup>:

1. Honeywell's comments generally address the overall policy for demand-side management programs and cost recovery rather than the questions specifically posed in the June 29, 2011 workshop.
2. It is imperative that utilities receive timely program cost recovery and timely earnings opportunities associated with cost-effective energy efficiency savings. Utilities should be properly incentivized for the costs associated with their energy efficiency and demand response programs to enhance their overall energy efficiency portfolio.
3. Demand-side programs take time to implement and savings are realized over time. Implementers like Honeywell commit significant resources to ramp up and deliver programs with the expectation that program funding will continue. Frequent changes stemming from interpretation of legislation or rulemaking, unclear or unattainable goals or intermittent programs impede progress and significantly undermine the demand side momentum in the marketplace.

### MEG:

1. The MEG does not support decoupling, because it does not meet several standards of MEEIA and is therefore not lawful in Missouri.
2. Decoupling will not provide a utility with a financial incentive to continue investing in demand-side management programs, results in much lower risk for the utility and shifts that risk to its customers, reduces customers' incentives to use energy more efficiently, and may result in little-to-no reduction in energy usage.
3. Cost recovery should include costs expended by the utility to invest in energy efficiency programs. It does not include recovery of fixed costs.
4. To reduce the throughput disincentive<sup>8</sup> created by energy efficiency programs, an incentive sharing mechanism should be created that allows a utility to share the benefits of reduced energy with customers.

### MEDA:

1. Rate design modification refers to changes in the rate design by modifying the specific structure of the charges for a customer rate. Structure changes can mean changing the proportion of the various rate components, modifying the rate blocks, creating new billing elements, etc. For customers who may qualify for alternative rates, a rate design modification may cause customers to re-evaluate the rate they have chosen. In all instances, however, the charges within a specific rate classification are established such that the application of these individual charges to the total annual customer class customer counts, usage/demand units, kVAR units, etc., will result in the collection of the targeted annual revenue requirements of the utility's rate classes.

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<sup>7</sup> Honeywell is the implementer of Ameren Missouri's residential Multifamily Low Income Program and Home Energy Performance Program.

<sup>8</sup> Traditional regulation may lead to unintended disincentives for the utility promotion of end-use efficiency, because revenues are directly tied to the throughput of electricity and gas sold. To counter this "throughput disincentive," a number of States are considering alternative approaches intended to align their utilities' financial interests with the delivery of cost-effective energy efficiency programs.

2. Defines decoupling as, “A separation of revenues and profits from the volume of energy sold” and “A form of regulated ratemaking that separates cost recovery from the changes in the volume of sales.”
3. Decoupling is lawful in Missouri. MEEIA specifically allows for rate design modifications and, in fact, required a docket to study proposed rate design modifications - indicating decoupling is allowed under MEEIA. No law exists which precludes decoupling for electric utilities.
4. Cost recovery is, “The utility’s ability to timely recover (collect) the direct and indirect program costs along with lost fixed costs resulting from energy efficiency programs. Cost recovery results in no financial detriment to the utility implementing energy efficiency programs.”
5. There is no need to set minimum requirements of what constitutes “studying the effects.” MEDA suggests that no new rule or rule modifications are needed. Utilities should be able to file a MEEIA application and that, if rate design modifications are recommended by the utility or other parties, supporting studies must be included.
6. Recommends that the next workshop be held later in the year (referencing 2012) to discuss rate design modifications. The workshop should include presentations by parties on rate design modifications being implemented throughout the country.

#### Renew Missouri and GRELC:

1. A threshold issue is whether this portion of the law contemplates a workshop and rulemaking process or whether rate design modifications should be left to individual rate cases and/or DSIM dockets. These latter cases result in orders, not rules. We can see no interpretation of “promulgate an appropriate rule” that does not mean a rule of general application.
2. Decoupling comes within the definition of rate design modification as intended by the statute.

#### MDNR:

1. Decoupling is not a rate design modification.
2. Implies that decoupling may be lawful.
3. Cost recovery is not specifically defined.
4. Studying the effects could mean a review of decoupling and other rate designs to encourage energy efficiency in both Missouri and other states. Could also mean a review of existing studies.
5. The process of “studying the effects of a cost recovery mechanism” begins with a utility’s DSIM filing.

#### MIEC:

1. Decoupling is not rate design.
2. Decoupling is unlawful under MEEIA.
3. Rate design and rate modifications cannot be addressed appropriately in workshops or other generic forums but rather in an evidentiary proceeding.
4. The Commission should promulgate a rule specifying that rate design impacts cannot be evaluated on a generic basis, but in an evidentiary proceeding when a utility makes a filing involving a change in its rate design.

#### Noranda:

1. Rate design is discussed in every rate case where a lot of information is presented. In the rate case context, rate design is looking at changing the relationships between the rates and the underlying costs.
2. Every rate case has testimony that addresses rate design and rate design principles. Energy efficiency has little impact on those principles. We should have a rule that says we are going to rely on long standing principles and consider the things we have always considered. We shouldn't elevate energy efficiency above all else. That would be a mistake. We could study a couple approaches- but, in a rate proceeding the same things have to be considered. If a rate case is not a good time, parties can ask the Commission for a docket to work through the issues.
3. The meaning of the term "study" is in the eye of the beholder. Ratepayers are looking for fair rates and don't want to pay more than costs. Utilities are interested in their ability to earn a return. Another aspect to be looked at is the integrated resource planning (IRP) impact. We could compile previous testimony and provide to Commission as a study. To study something that may or may not happen down the road would not be productive.

#### OPC:

1. There are various rate elements that are used to collect a revenue requirement. The term, "rate design modification" means a change in the elements of a rate.
2. Decoupling usually means adjustments between rate cases. The problem is that there is nothing in statute that authorizes adjustments between rate cases. MEEIA rulemaking has provisions for adjustments between rate cases. We are going to run into the same impasse here until there is clarification from the courts or legislature.
3. Don't think any rate design modification, even in a MEEIA filing, could occur without studying in a docket and promulgating a rule.
4. The "docket" could also be an individual rate case proceeding. Substantial changes such as a shift in class revenue requirement sometimes have a separate rate design docket because it is too complex to deal with in a rate case. But, it cannot be done in a rate case unless there is a MEEIA filing as part of that rate case. Would need to have a docket prior to a MEEIA filing to study the effects of that rate design and then promulgate a rule prior to a MEEIA filing.
5. Want all utilities to come in with a MEEIA filing when it makes sense. They think it makes sense after this docket has been completed. If there are MEEIA filings without a docket, OPC will point out the legal defect of their proposal.
6. Study could look at other states, case studies, other studies, etc. Looking at other state experiences would be the type of study envisioned, assuming we went down that road.

### **UTILITIES' AND STAKEHOLDERS' RECOMMENDATIONS**

Utilities and stakeholders generally suggested three recommendations for next steps. Staff identified various questions the Commission may need to consider with each recommendation.

- I. Recommendation 1:** A workshop process should be established to complete a generic study of various rate design modifications. The workshop process could result in a report to the Commission and/or a new rule.

Questions for consideration:

- Will final work product be a report to the Commission, proposed rule or something else?
- Which rate design modifications will be studied? Proposals included in the June 29, 2011 workshop and comments include: decoupling, straight fixed variable, reduced customer charges, customer class specific rate structures, inclining block rates, studying the impact of declining block rates, time of use rates and/or seasonally adjusted rates.
- Is decoupling a rate design modification and/or is it lawful?

## **II. Recommendation 2:** Workshop/rulemaking process to modify existing MEEIA rules.

Questions for consideration:

- Would proposed rate design modifications be studied as part of the MEEIA filings?
- Which rate design modifications will be included in the MEEIA rules? Proposals included in the June 29, 2011, workshop and comments include: decoupling, straight fixed variable, reduced customer charges, customer class specific rate structures, inclining block rates, studying the impact of declining block rates, time of use rates and/or seasonally adjusted rates.
- Have proposed rate design modifications been “studied” sufficiently to meet the mandate of MEEIA?
- Is decoupling a rate design modification and/or is it unlawful?
- What would modifications to existing MEEIA rules address? (i.e. addition of a definition of rate design modification, framework for proposing a specific rate design modification in a DSIM filing and supporting documentation, etc.)

## **III. Recommendation 3:** Rate design modification proposals must be addressed in an evidentiary proceeding.

- A. Recommendation 3(A): Address specific rate design modification proposals in an evidentiary proceeding (i.e. rate case and/or MEEIA filing).

Questions for consideration:

- Would proposed rate design modifications be studied at the time of the evidentiary proceeding or in a separate proceeding?
- Should MEEIA rules be modified to require that rate design modification proposals only occur in an evidentiary proceeding?
- Is decoupling a rate design modification and/or is it lawful?
- Can a rate design modification be proposed in a rate case if it is not part of a MEEIA filing?

- B. Recommendation 3(B): Rate design modification proposals should occur only in rate cases, then a subsequent study shall be conducted and, finally, the Commission shall promulgate an appropriate rule.

Questions for consideration:

- Can electric utilities file for a rate design modification under MEEIA without the Commission first studying them in a docket and promulgating an additional rule?



- Is decoupling a rate design modification and/or is it lawful?
- Can a rate design modification be proposed in a rate case if it is not part of a MEEIA filing?

## **STAFF RECOMMENDATIONS**

Staff recommends the Commission choose one of the following two options:

**I. Option 1:** Issue an order soliciting verified pleadings seeking input on the following questions from all stakeholders regarding rate design modifications in Missouri (decoupling, straight fixed variable, reduced customer charges, customer class specific rate structures, inclining block rates, studying the impact of declining block rates, time of use rates and/or seasonally adjusted rates) or any other rate design modifications the utilities and stakeholders would like to propose:

- Is it legal in Missouri? If not, which statute would need to be modified?
- How does it fit within PURPA 111(d)(17) Rate Design Modifications to Promote Energy Efficiency Investments?
- What have been the experiences with that rate design in other states?
- How will it change the risk incurred by shareholders and customers?
- How does it compare from the utility's perspective and from the customers' perspective to the DSIMs approved in Case Nos. EO-2012-0142 and EO-2012-0009?

**II. Option 2:** Convene an on-the-record presentation directing the utilities and stakeholders to address certain questions. The Commission could seek input on the following questions from all stakeholders regarding rate design modifications in Missouri (decoupling, straight fixed variable, reduced customer charges, customer class specific rate structures, inclining block rates, studying the impact of declining block rates, time of use rates and/or seasonally adjusted rates) or any other rate design modifications the utilities and stakeholders would like to propose:

- Is it legal in Missouri? If not, which statute would need to be modified?
- How does it fit within PURPA 111(d)(17) Rate Design Modifications to Promote Energy Efficiency Investments?
- What have been the experiences with that rate design in other states?
- How will it change the risk incurred by shareholders and customers?
- How does it compare from the utility's perspective and from the customers' perspective to the DSIMs approved in Case Nos. EO-2012-0142 and EO-2012-0009? and

### **Applicable with either option:**

The Commission makes a determination on the lawfulness of decoupling, straight fixed variable, reduced customer charges, customer class specific rate structures, inclining block rates, declining block rates, time of use rates and/or seasonally adjusted rates in Missouri; and,

Modifies its MEEIA rules to include the specific rate design modifications that meet all relevant statutory requirements, allowing utilities and stakeholders to propose these rate design

modifications associated with demand-side cost recovery in future MEEIA filings. In the future, utilities or stakeholders could request the Commission open a new proceeding to consider additional rate design modifications associated with demand-side cost recovery.