BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION

In the Matter of the Consideration and Implementation of Section 393.1075, the Missouri Energy Efficiency Investment Act

Docket ## EX-2010-0368

Comments of the Natural Resources Defense Council

December 20, 2010

Good morning and thank you for providing an opportunity for public comments on these important proposed rules, which have been the subject of an extensive public process over the past year. NRDC considers it a privilege to have been part of that process. We would like to commend the Commission and the staff on its diligence in working through contentious and complex issues with stakeholders in an attempt to forge consensus where possible, and address areas of disagreement.

It is important maintain focus on the reason these rules are so important to the residents of Missouri. There is tremendous untapped potential for energy efficiency to reduce customer bills, and avoid the need for more polluting forms of electric resources. According to a 2009 analysis by the Midwest Energy Efficiency Alliance, if Missouri utilities were to meet the goals contained in proposed 4 CSR 240-20.094, ratepayers would save, cumulatively, more an estimated $4.5 billion on their energy bills between over a fifteen year ramp-up period, net of program costs. This savings could be used by consumers to create economic growth as residential ratepayers have more to spend on goods and services, and business customers have more to spend on production and workers.

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The Missouri legislature recognized the benefits of energy efficiency in passing the Missouri Energy Efficiency Investment Act, which establishes a goal of capturing "all cost-effective demand side savings." The legislature further recognized that central to achieving this goal was to encourage electric utilities to invest in efficiency, and did so by requiring the Commission to provide utilities with timely cost recovery for energy efficiency program investment, provide utilities with an opportunity for earnings on that investment, and ensure that utility financial incentives are "aligned with helping utility customers use energy more efficiently..."

NRDC, along with several other stakeholders, submitted written comments in this docket on December 15, addressing a number of provisions in the proposed rules. In the interest of time, I will not reiterate each of these comments today, but refer you to that written submission. My comments today are in two parts. The first part concerns how the proposed rules seek to ensure that utility plans are sufficiently aggressive to lead to the capture of all cost-effective potential for energy savings in Missouri. The second part concerns how the proposed rules seek to ensure that utilities are able to recover their costs, overcome financial disincentives to energy efficiency, and earn a return on their investment in efficiency.

A. **All Cost-Effective Energy Efficiency**

The statute is clear that in considering utility energy efficiency plans, the Commission must evaluate whether the plans will meet the goal of capturing all cost-effective efficiency potential. Therefore, the Commission must have some guidelines by which it makes that assessment. The proposed rules properly give the Commission two sets of inputs for that determination. The first is a set of gradually increasing goals that mirror the level of savings that have been adopted in other Midwestern states by statute or by Commission order. The second is the potential studies performed by Missouri utilities. NRDC agrees that with these two sets of inputs, the Commission should be able to evaluate whether a proposed program portfolio is designed to achieve the goal of capturing the cost-effective potential for energy savings.

Several stakeholders have argued that the numerical goals in section 4 CSR 240-20.094(2)(A) should be omitted. They argue that goals set by other states are not relevant to the realities of Missouri, and that the utility potential study alone can guide the Commission in this determination. We strongly disagree. Utilities should not be in the position of designing a study, the outcome of which will be a energy efficiency target against which their own performance incentives will be awarded. Such an arrangement would inevitably result in studies that underestimate the efficiency potential so that higher performance incentive rewards can be earned. This outcome does not serve utility customers and will not result in the accomplishment of the statutory goal of achieving all of the cost effective potential that exists.

The goals in 20.094(2)(A) provide an important and reasonable backstop to the temptation by utilities to manipulate the assumptions in their potential studies.[1] The goals are not mandatory, and no penalty is assessed as a result of failure to meet them. However, they do reflect the trajectory that many other utilities in the region and around the nation have set for electric utilities. There is nothing about Missouri that would suggest that these goals are inappropriate here. The Commission should seriously question a utility efficiency portfolio that fell

1 NRDC provided documentation on June 14, 2010 in docket EW-2010-0265 (Response to Ameren) of other state's energy efficiency goals, including Iowa, Illinois, Indiana, and Ohio.

significantly short of these goals, and the proposed rules appropriately require the utilities to provide documentation as to the reason why a portfolio fails to achieve this level of savings.

B. Utility Financial Incentives to Invest in Energy Efficiency

NRDC generally supports the use of the demand side investment mechanism to allow utilities to recover program costs and to earn an incentive for excellent performance toward the savings targets set by the Commission in the plan approval process. However, as we have stated previously and will reiterate here, we do not believe that the proposed rules adequately address the throughput incentive currently faced by utilities, and therefore the rules fall short of faithfully implementing the statutory directive.

It is well understood and extensively documented that under traditional ratemaking policy, utility revenues rise when sales rise, and the converse is equally true – declining sales mean declining revenues. Thus, Missouri utilities can earn more than their authorized fixed costs revenue requirement if sales are higher than was projected during a rate case. This "throughput incentive" amounts to a strong disincentive for utilities to invest in energy efficiency or to support energy saving policies and measures outside their control, and the magnitude of the disincentive is substantial. In a 2008 Report to the Minnesota Public Utility Commission on decoupling, the Regulatory Assistance Project (RAP) provided an example to illustrate the effect of changes in sales, both up and down, on a utility's earnings.[2] In the hypothetical, a 1% change in revenues had an effect about ten times greater on utility earnings; for example, a 2% gain or loss in revenues caused a 23.76% gain or loss in earnings.

2 Regulatory Assistance Project, *Revenue Decoupling: Standards and Criteria, A Report to the Minnesota Public Utilities Commission*, 36 (2008).

The statutory direction to the commission to align utility financial incentives such that utilities are encouraged to support energy efficiency investments that save customers money is rendered meaningless if this powerful disincentive is not addressed in a meaningful and timely manner in this rulemaking.

The current proposed rules purport to address this misalignment of incentives by offering the utilities an opportunity to file a mechanism by which it can recover "lost revenues." However, under such a mechanism, utilities would continue to see higher levels of revenue recovery with higher sales. Therefore the utility will find itself facing the same conflict it currently faces at the prospect of taking actions or supporting policies to save energy and thereby save their customers money, knowing that such actions would cause their shareholders to miss out on the benefit from higher sales. Under such a mechanism, utility management would face this conflict at the prospect of supporting state building codes for energy efficient construction, federal appliance standards that have successfully transformed the market for products ranging from refrigerators and televisions to air conditioners and lighting, or any action outside its own programs for advancing the use of increasingly efficient technologies. Such a mechanism would ultimately fail to align the utilities' financial incentives with the goals of the statute to capture all cost-effective energy efficiency for the benefit of ratepayers.

Our view is that the rules should be less prescriptive regarding the way in which a utility might propose to address the throughput incentive. The rulemaking process did not attempt to forge consensus on this matter, rather, it should be for the Commission to decide in the context of a specific proposal by a utility during a DSIM filing. In our written comments filed last week, we described a simple change in the rule language that would allow utilities to file and the Commission to either approve or reject a mechanism that works for their specific needs. Rather than repeating that change in wording here, I simply direct you to that December 15 submission in this docket.

In conclusion, again on behalf of the thousands of NRDC members residing in Missouri, we would like to commend the Commission and the staff on its work to implement the provisions of the Missouri Energy Efficiency Investment Act and thank you for allowing our participation. I look forward to working together to review and refine the programs and plans submitted pursuant to these rules, and realizing the goal of maximizing the potential for energy efficiency for Missouri ratepayers.