

VEIC Study Review Synthesis
Chapter 9 - Utility Performance Incentives
July 5, 2012

Summary of Chapter 9

The VEIC Report explains that under a traditional regulatory structure, such as that in place in New Hampshire, utilities have inherent *disincentives* to pursue energy efficiency which may result in reduced energy sales and shareholder earnings. However, performance incentives can be designed into the efficiency programs to offset and/or overcome these disincentives thus encouraging utilities to pursue energy efficiency resources more aggressively. There are multiple ways to design and implement performance incentives some of which are dependent on the design and implementation approach of the EE programs themselves.

The Core programs and Performance Incentives should be informed by overarching state energy policy goals, which may include specific policy objectives for the State's EE programs. Performance Incentives for EE programs should motivate the utility or other program administrator to meet or exceed goals and objectives agreed upon by the stakeholders or as directed by the PUC.

Chapter Team Findings

The Chapter Review Team used the Recommendation Evaluation methodology developed by the VEIC Report Review Group which consisted of individual tracking of level of agreement, comments, assessment of any required actions, and estimates of the time horizon, impact and cost of implementing recommendations using agreed upon comparative evaluation scales.

In general, the recommendations regarding the PI would take little time to implement, the impact would be low, and the cost to implement would be low using the evaluation scales.

Top Priorities for Early Action.

The Chapter Review Team agreed with many of the VEIC Recommendations in this Chapter but did not believe any of them rise to the level of "Top Priority for Early Action."

Priorities for Medium or Long-Term Action.

The Chapter Review Team believes that the majority of recommendations regarding performance incentives are more appropriately acted upon through the Core energy-efficiency management process, which reviews and modifies the Core EE Programs rather than by the EESE Board directly.

The Chapter Review Team's specific comments on VEIC's recommendations follow the "Background" section below.

Areas for Further Consideration.

The inter-relationship among independent evaluation, monitoring and verification of energy efficiency programs, the setting of appropriately aggressive program savings goals, and potential performance incentive levels that can be earned should be an area of ongoing review by the Core Management Team and EE program stakeholders.

Though there was no specific VEIC recommendation regarding "goal setting," the Chapter Review Team received feedback that it may be useful to review the process by which EE program savings goals are set to ensure that the process is adequately robust. Setting appropriate savings goals is

important as the ratio of actual savings achieved to planned savings goals is used as part of the current PI formula. Further, savings goals should be developed to align with policy goals and available funding.

The Chapter Review Team also received feedback that the “Core Performance Incentive Review Subgroup” actively identify and incorporate market transformation-type metrics into the CORE Programs’ Energy Efficiency Program Performance Incentive metrics and goals structure. While this has not yet been discussed by the entire Review Committee, it is in keeping with item 1.8.5 in the “*Building Blocks that Lead to Market Development and Market Transformation*,” **to which the committee did agree. This “building block” called for allowing** utilities to claim benefit not only for installation of efficiency measures, but also for some of the work they do that helps to develop markets, and helps to promote and support high-efficiency codes and standards

Background

The purpose of a well designed Energy Efficiency Program Performance Incentive (PI) is to encourage performance to achieve and exceed specified program goals and/or metrics. The PI should be well designed to account for the current regulatory structure, policy goals, legislative mandates, and financial impacts on utilities and program administrators of the efficiency programs. The PI should serve as an effective motivator but not be any higher than necessary as costs are borne by ratepayers. The design of any PI should take into consideration regulatory mechanisms such as revenue decoupling and/or lost base revenue recovery which may also be in place¹ as these mechanisms interact with any PI to influence utility behavior and compensate the utility.

Performance Incentives should be reviewed periodically to insure that they are working towards meeting energy policy objectives. There is currently a group of regular participants at Core Quarterly Meetings called the “Core Performance Incentive Review Subgroup” comprised of utility representatives and other stakeholders. This group’s purpose is to discuss/evaluate PI issues and make recommendations for modifications to the Core Management Group. The VEIC Report’s Chapter 9 recommendations will be reviewed by this group. The PUC, in its Order No. 25,315 issued on January 9, 2012 stated “The Settling Parties agree to include in quarterly meetings a discussion of the VEIC Independent Study of Energy Policy Issues Final Report and to work with the EESE Board and subcommittees to reduce duplication of effort. We agree that discussion of the VEIC report is an appropriate subject matter for the quarterly meetings. The quarterly meetings are intended to allow Staff and the parties to review the implementation of the gas and electric energy efficiency programs and issues related to those programs.”

The Chapter 9 review team agreed with most of the VEIC recommendations with the exception of 9.8.3 (tie incentive to budget not actual expenditures) and 9.8.6 (create tiered incentive structure). Regarding Recommendation 9.8.3., the PUC has reviewed and approved the use of “actual” expenditures in the current PI formula. See PUC Order No. 25,189 at pages 22-23 issued December 30, 2010.

¹ Neither of these regulatory mechanisms is currently in place for any NH utility regulated by the PUC. Implementation of either would require review and approval by the PUC.

Review Team’s Comments and Recommendations

9.1 Agree on the various policy objectives of the Core programs.

The Chapter Review Team agreed on the interpretation of this recommendation as: the Core programs *should* be informed by an overarching state energy policy which does not currently exist. The objectives of that policy which the Core programs focus on should be agreed upon by stakeholders. The utility Performance Incentives (PI) should be designed to motivate the electric & gas utilities to meet the policy objectives that apply to the Core Programs. State energy policy should encompass more than regulated fuels/utilities but here we discuss only Core programs.

9.2.2 Market transformation might involve, for example, training and education efforts that do not translate into measurable economic benefits and thus lower the cost-effectiveness of the program.

Market transformation efforts which include training & education can be more cost effectively dealt with by the private sector. Market forces will come into play when the demand exists. Markets transform themselves most efficiently when there is a free flow of information regarding trends. A modest amount of public awareness/education expenditure is acceptable.

9.3 Find measurable and verifiable metrics that can be used to determine the Core program’s success or failure at reaching the goals.

Use of a Logic Model approach to identify program goals and metrics could be a useful component. The programs currently use measurable & verifiable metrics. One member stated that making the “number of contractors trained” a performance metric would perhaps not be the best use of limited funds. Further, subsidized training programs/events may be more appropriate at certain phases of an EE program rather than throughout the full life cycle of the program. Programs should be designed to enable the growth of an energy service industry

9.4 Determine the maximum available incentive and the relative importance of the various performance metrics.

No objection to this recommendation. Should be analyzed and thoughtfully reviewed by Core PI Subcommittee.

9.5 Determine whether to add additional metrics that don’t carry an explicit financial award, but that can affect the size of the overall award.

No objection to this recommendation. Should be analyzed and thoughtfully reviewed by Core PI Subcommittee.

9.6 Determine minimum thresholds in each performance incentive, as well as a method for scaling the incentive with performance

No objection to this recommendation. Should be reviewed analyzed and thoughtfully by Core PI Subcommittee.

9.7 Engage stakeholders to ensure that performance metrics align with the policy and program goals.

The current Core Program docket process at the PUC currently allows for participation by stakeholders. Future efforts should continue, if not enhance, this opportunity for engagement and participation.

9.8.1 Cap maximum incentives for each performance metric

Current PI has a cap and it is appropriate that incentives have a cap.

9.8.2 Use net savings rather than gross savings

NH does not explicitly account for free ridership or spillover in current calculation of energy savings. These two factors, and others, can be used to adjust gross savings to net savings. Program evaluations must be specifically designed to estimate these, and other, adjustment factors. However, it is difficult to produce robust, reliable estimates of these factors. Moreover, as a free ridership adjustment would generally decrease gross savings estimates and a spillover adjustment would increase the gross savings estimate, these factors are in numerical opposition to each other. The Review Team did not feel that use of gross savings without specific adjustments to render “gross savings” into “net savings” in the PI formula was inappropriate (contrary to VEIC recommendation). Two of the members felt we are, in fact, reporting net savings, while another thought that technically we are not doing that, but to the extent that evaluations quantify actual savings, we are, in effect, using something other than pure gross savings.

9.8.3 Tie incentive to budget, rather than actual spending

The Review Team disagreed with this recommendation. The PUC has reviewed this issue and approved use of the “actual spending” in the PI formula. VEIC Report stated use of “actual spending” could create opportunity for intentional overspending by utilities to earn more PI. However, the Review Team felt that because the SBC funding is limited and finite and because budgets are approved by PUC with specific limitations on overspending, such concerns were not well founded.

9.8.4 Raise minimum performance thresholds

There were multiple views but the final consensus was to AGREE with this recommendation.

9.8.5 Begin incentive at lower amount

No objection to this recommendation. Should be analyzed and thoughtfully reviewed by Core PI Subcommittee.

9.8.6 Create a tiered incentive structure

The Review Team disagreed with this recommendation as they believed it could encourage unintended consequences.

9.8.7 Implement independent third party evaluations

The current program evaluation process uses third party evaluators and thus meets this goal. Programs are evaluated on a schedule that meets utilities needs and reporting requirements of ISO-

NE. The PUC has directed Staff to move forward with an RFP process to retain a contractor to perform a comprehensive review of current evaluation efforts and to create a long term evaluation plan.

9.8.8 Consider changing cost-effectiveness metric or adding weighting factor

Lowering the cost effectiveness goal is a good idea. This would allow a larger portion of the PI to be based on energy savings to be achieved. However, eliminating it altogether could be counterproductive as such a change could waste money and may not maximize carbon reduction. It would require changes to existing regulation (PUC approval of PI changes is required). A review of the impact that any such change would have on the previously earned PI amounts would be reasonable prior to any such change.

9.8.9 Consider adding additional metrics:

Having the PI formula include other metrics is a reasonable way to encourage program administrators to focus on additional program goals – a worthwhile thing to consider.

Regarding the specific metrics highlighted in the Report:

1. the Review Team believed the idea of incentives to "train contractors" to be an inefficient use of limited program funds as contractors can send their employees to tech schools and other programs offered by the energy services industry. This is an employee development issue which contractors in the marketplace should readily embrace on their own.
2. Product buy downs - Review Team ambivalent on this (more information from other jurisdictions would be useful). Team felt this should definitely reserved for early stages of market transformation – should not be done the way it is being implemented currently in MA
3. Review Team felt "community awareness" would not be an efficient use of limited program funds.