

National Standard Practice Manual for Energy Efficiency Cost-Effectiveness

**Prepared by
The National Efficiency Screening Project**

**Presentation to the New Hampshire
Energy Efficiency and Sustainable Energy Board**

**Tim Woolf, Synapse Energy Economics
May 18, 2018**

NATIONAL STANDARD PRACTICE MANUAL

Published May 2017

New guidelines for cost-effectiveness testing

Drivers... |

The traditional tests often do not capture or address pertinent state policies.

The traditional tests are often modified by states in an ad hoc manner, without clear principles or guidelines.

Efficiency is not accurately valued in many jurisdictions.

There is often a lack of transparency on why tests are chosen and how they are applied.

NSPM - BACKGROUND

NSPM Stakeholders

- National Efficiency Screening Project (NESP) includes stakeholders working to improve EE cost-effectiveness.
- Over 75 organizations representing a range of perspectives.

NSPM Authors

- Tim Woolf, Synapse Energy Economics
- Chris Neme, Energy Futures Group
- Marty Kushler, ACEEE
- Steve Schiller, Schiller Consulting
- Tom Eckman (Consultant and formerly Northwest Power & Conservation Council)

NSPM – BACKGROUND CONTINUED

NSPM Review Committee

- Roughly 40 experts representing a variety of organizations from around the country.
- Provided several rounds of review/feedback on draft manual.

NSPM Funding, Coordination, and Advisors

- Coordinated and funded by E4TheFuture
- Managed by Julie Michals, E4TheFuture
- Advisory Committee input on outreach & education
- Earlier work on the NESP and NSPM was managed by the Home Performance Coalition

For more information:

<http://www.nationalefficiencyscreening.org/>

NSPM: Purpose

- Defining policy-neutral *principles* for developing cost-effectiveness tests.
- Establishing a framework for selecting and developing a *primary test*.
- Providing guidance on *key inputs*.

NSPM: Scope

- Focus is on utility customer-funded energy efficiency resources.
- Addresses 1st order question: “which EE resources merit acquisition?”
- Principles and framework apply to all other resources (including other types of distributed energy resources).
- *NSPM provides a foundation on which jurisdictions can develop and administer a cost-effectiveness test, but does not prescribe “the answer”*

What's Covered -- NSPM Outline

Executive Summary

Introduction

Part 1: Developing Your Test

1. Principles
2. Resource Value Framework
3. Developing Resource Value Test
4. Relationship to Traditional Tests
5. Secondary Tests

Part 2: Developing Test Inputs

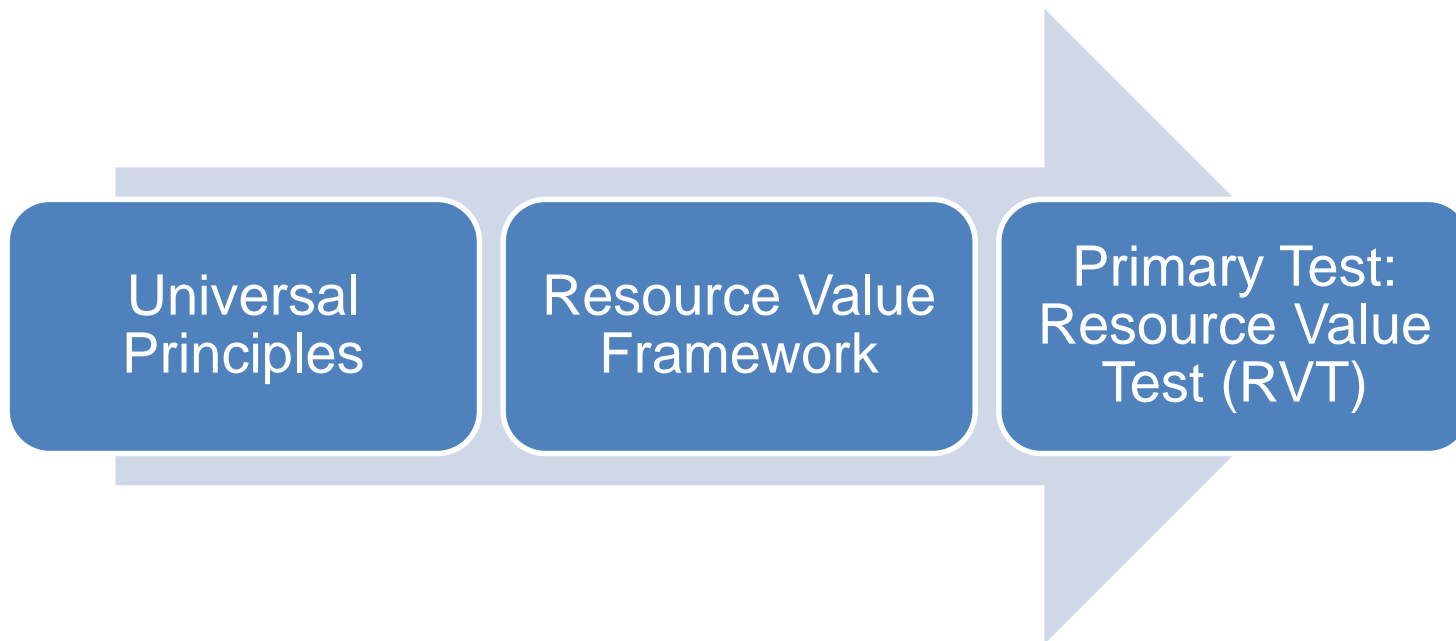
6. Efficiency Costs & Benefits
7. Methods to Account for Costs & Benefits
8. Participant Impacts
9. Discount Rates
10. Assessment Level
11. Analysis Period & End Effects
12. Analysis of Early Retirement
13. Free Rider & Spillover Effects

Appendices

- A. Summary of Traditional Tests
- B. Cost-Effectiveness of Other DERs
- C. Accounting for Rate & Bill Impacts
- D. Glossary

Part I

Developing the Primary Cost-Effectiveness Test Using the Resource Value Framework



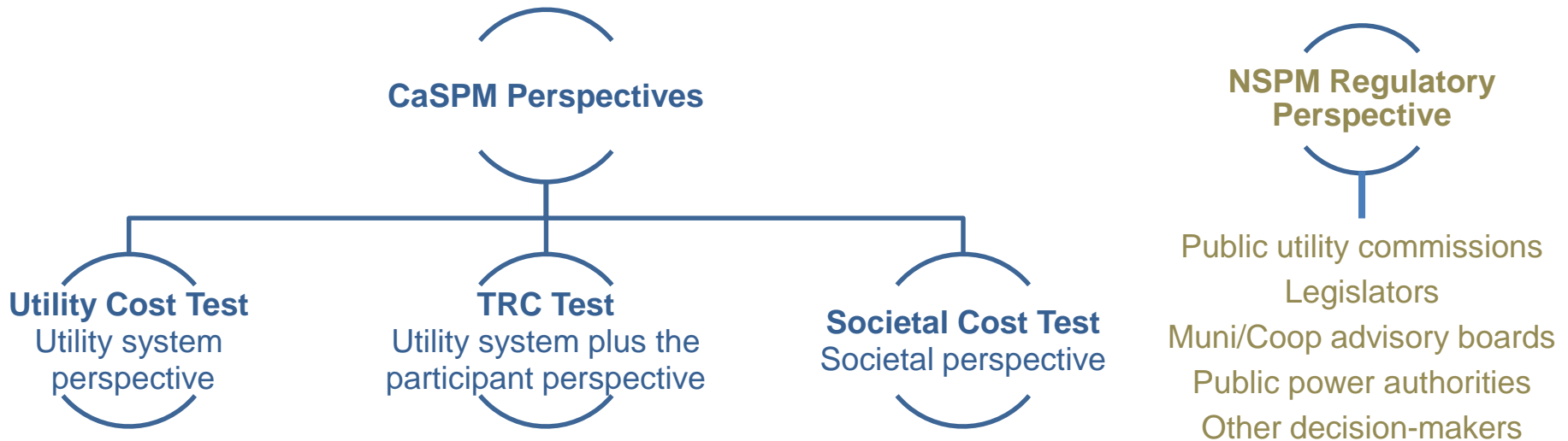
NSPM Principles

1. Recognize that energy efficiency is a resource.
2. Account for applicable policy goals.
3. Account for all relevant costs & benefits, even if hard to quantify impacts.
4. Ensure symmetry across all relevant costs and benefits.
5. Conduct a forward-looking, long-term analysis that captures incremental impacts of energy efficiency.
6. Ensure transparency in presenting the analysis and the results.

Implementing the Resource Value Framework Involves Seven Steps

Step 1	Identify and articulate the jurisdiction's applicable policy goals.
Step 2	Include all utility system costs and benefits.
Step 3	Decide which additional <i>non-utility</i> system costs and benefits to include in the test, based on applicable policy goals.
Step 4	Ensure the test is symmetrical in considering both costs and benefits.
Step 5	Ensure the analysis is forward-looking, incremental, and long-term.
Step 6	Develop methodologies and inputs to account for all impacts, including hard-to-quantify impacts.
Step 7	Ensure transparency in presenting the analysis and the results.

Cost-Effectiveness Perspectives



- California Standard Practice Manual (CaSPM) – test perspectives are used to define the scope of impacts to include in the ‘traditional’ cost-effectiveness tests
- NPSM introduces the ‘regulatory’ perspective, which is guided by the jurisdiction’s energy and other applicable policy goals

STEP 1

Identify and Articulate Applicable Policy Goals

Laws, Regulations, Orders:	Policy Goals Reflected in Laws, Regulations, Orders, etc.					
	Low-Cost	Fuel Diversity	Risk	Reliability	Environmental	Economic Development
PSC statutory authority	X			X		
Low-income protection						X
EE or DER law or rules	X	X	X	X	X	X
State energy plan	X	X	X	X	X	X
Integrated resource planning		X	X		X	X
Renewable portfolio standard		X	X		X	X
Environmental requirements					X	

- Each jurisdiction has a constellation of energy policy goals embedded in statutes, regulations, orders, guidelines, etc.
- The table illustrates how laws, regulations, orders, etc. might establish applicable policy goals.

STEP 2

Include All Utility System Costs and Benefits

Illustrative Utility System Costs	Illustrative Utility System Benefits
• EE Measure Costs (utility portion – e.g. rebates)	• Avoided Energy Costs
• EE Program Technical Support	• Avoided Generating Capacity Costs
• EE Program Marketing/Outreach	• Avoided T&D Upgrade Costs
• EE Program Administration	• Avoided T&D Line Losses
• EE Program EM&V	• Avoided Ancillary Services
• Utility Shareholder Performance Incentives	• Wholesale Price Suppression Effects
	• Avoided Costs of RPS Compliance
	• Avoided Costs of Environmental Compliance
	• Avoided Credit and Collection Costs
	• Reduced Risk
	• Increased Reliability

The principle of treating energy efficiency as a resource dictates that utility system costs and benefits serve as the foundation for all tests

Market Price Suppression Impacts (aka DRIPE)

- Price suppression impacts are a utility system impact.
 - They should be included in all cost-effectiveness tests.

- EE savings in NH will have impacts for all customers in New England.
- Several options for treating these impacts:
 1. Include impacts for the utility only.
 2. Include impacts for the entire state.
 3. Include impacts for all of New England.

- Decision depends upon policy goals.
 - Do you want to consider just the utility impacts, the state impacts, or the regional impacts?

- Societal perspective:
 - Are the price suppression benefits netted out by the costs to generators?

STEP 3

Include Non-Utility System Impacts Based on Jurisdiction's Applicable Policy Goals

Applicable policy goals include all policy goals adopted by a jurisdiction that could have relevance to the choice of which energy resources to acquire.

Examples include:

Common Overarching Goals:	Provide safe, reliable, low-cost electricity and gas services; protect low-income and vulnerable customers; maintain or improve customer equity.
Efficiency Resource Goals:	Reduce electricity and gas system costs; develop least-cost energy resources; promote customer equity; improve system reliability and resiliency; reduce system risk; promote resource diversity; increase energy independence (and reduce dollar drain from the jurisdiction); reduce price volatility.
Other Applicable Goals:	Support fair and equitable economic returns for utilities; provide reasonable energy costs for consumers; ensure stable energy markets; reduce energy burden on low-income customers; reduce environmental impact of energy consumption; promote jobs and local economic development; improve health associated with reduced air emissions and better indoor air quality.

These goals are established in many ways:

- Statutes
- Regulations
- Commission Orders
- EE Guidelines
- EE Standards
- Directives
- And Others

STEP 3

Illustrative Non-Utility System Impacts

Impact	Description
Participant impacts	Impacts on program participants, includes participant portion of measure cost, other fuel savings, water savings, and participant non-energy impacts
Impacts on low-income customers	Impacts on low-income program participants that are different from or incremental to non-low-income participant impacts. Includes reduced foreclosures, reduced mobility, and poverty alleviation
Other fuel impacts	Impacts on fuels that are not provided by the funding utility, for example, electricity (for a gas utility), gas (for an electric utility), oil, propane, and wood
Water impacts	Impacts on water consumption and related wastewater treatment
Environmental impacts	Impacts associated with CO2 emissions, criteria pollutant emissions, land use, etc. Includes only those impacts that are not included in the utility cost of compliance with environmental regulations
Public health impacts	Impacts on public health; includes health impacts that are not included in participant impacts or environmental impacts, and includes benefits in terms of reduced healthcare costs
Economic development and jobs	Impacts on economic development and jobs
Energy security	Reduced reliance on fuel imports from outside the jurisdiction, state, region, or country

This table is presented for illustrative purposes, and is not meant to be an exhaustive list.

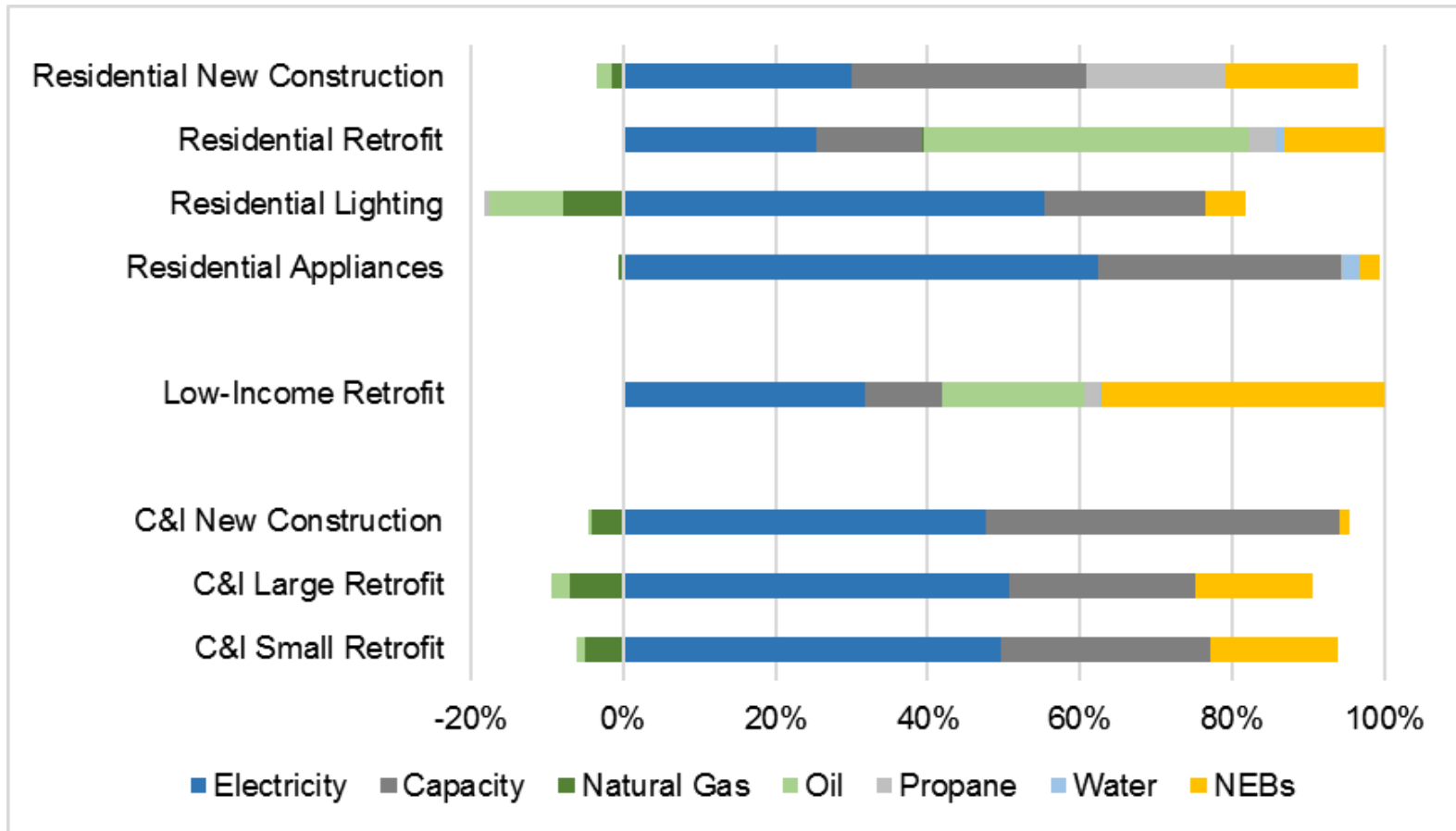
STEP 3

Whether to Include Participant Impacts

- Is a policy decision (based on jurisdiction's policy goals)
 - Policies may support inclusion of certain participant impacts (e.g., low-income, other fuels, etc.), but not necessarily all participant impacts
- If participant costs are included, participant benefits should also be included (to ensure symmetry and avoid bias), even hard to quantify benefits
- Key Questions:
 - Why does it matter what participants pay?
 - Why should non-participants pay for benefits to participants?

STEP 3

Implications of Including Participant Impacts



STEP 3

Reasons for Including Participant Impacts

- Participant impacts should be included to account for the impacts on all utility customers: participants and non-participants.
- Participant impacts should be included to account for the total cost of the resource, which is necessary to avoid uneconomic outcomes.
- Participant impacts should be included to protect program participants.
- Participant impacts should be included so that low-income participant benefits can be included.
- Participant impacts should be included so that other fuel and water impacts can be included.

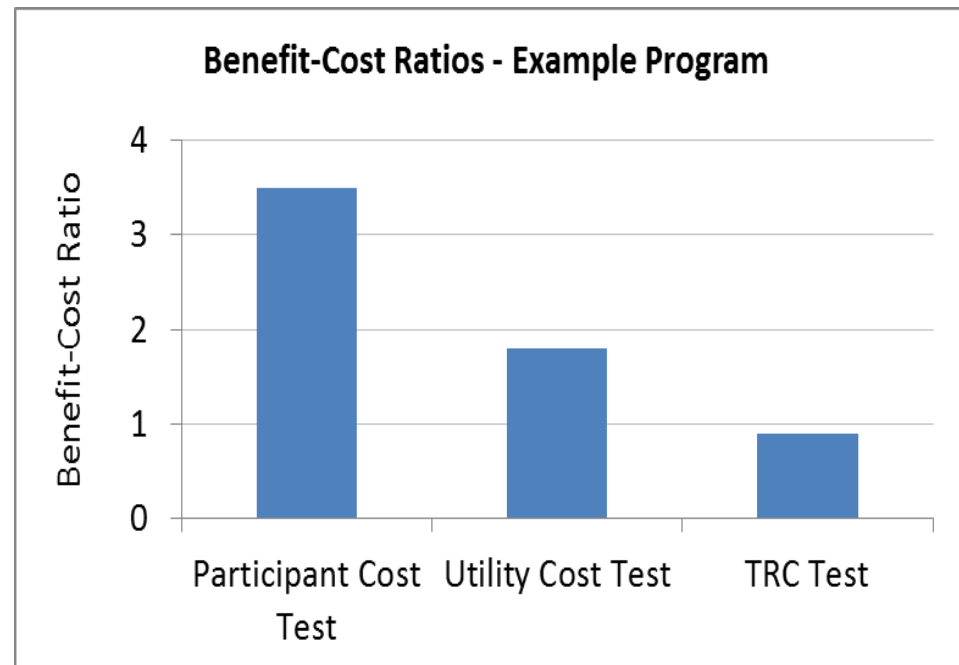
Question:

What are the counter-points?

STEP 3

Impacts on the Utility + Participants?

- The Total Resource Cost test supposedly indicates the utility system impacts plus the participant impacts.
- However:
 - Utility benefits = avoided costs
 - Participant benefits = avoided prices
 - Therefore the TRC test does not indicate impacts on participants
- The TRC test is really the Societal Cost test without the societal benefits



STEP 3

Avoiding Uneconomic Outcomes

Hypothetical Example:

- Retail electric rates = 14 ¢/kWh
- Total avoided costs = 10 ¢/kWh
- EE measure cost = 11 ¢/kWh
- EE measure rebate = 5 ¢/kWh

	<u>Total Resource Cost</u> With Participant Cost	<u>Utility Cost</u> Without Participant Cost	<u>Participant Cost</u> Without Utility Cost
Cost (¢/kWh)	11	5	6
Benefit (¢/kWh)	10	10	14
Benefit -Cost Ratio	0.91	2.0	2.3

Would excluding the participant cost result in an uneconomic outcome?

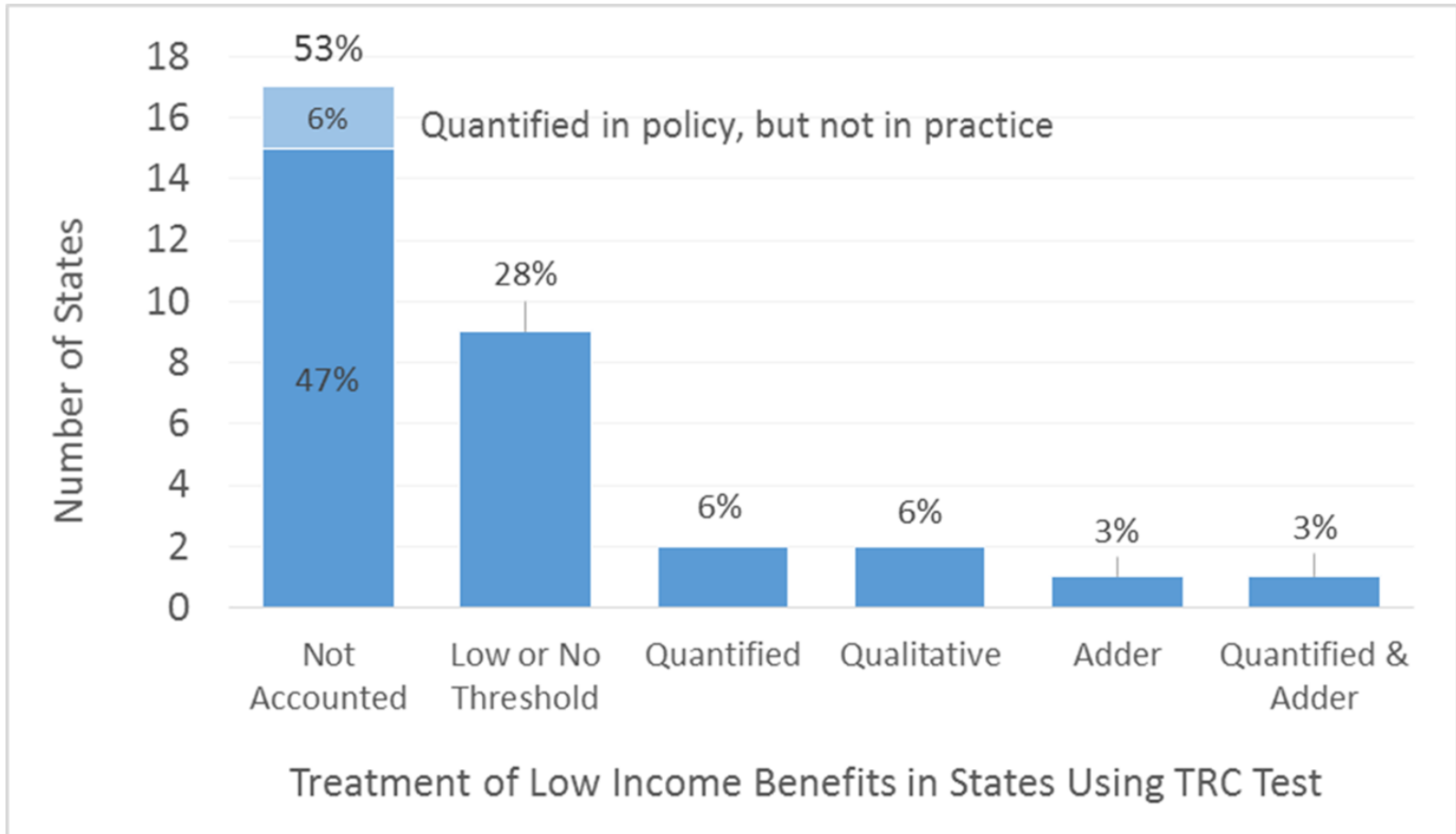
STEP 3

Impacts on Low-Income Customers

Affected Party	Costs	Benefits
Efficiency Program Participant	<p>Typically, none.</p> <p>Well-designed low-income programs cover all costs and remove all barriers to low-income customers.</p>	<p>Reduced energy burden</p> <p>Reduced O&M costs</p> <p>Increased comfort</p> <p>Increased health & safety/reduced medical costs</p> <p>Increased productivity</p> <p>Improved aesthetics</p> <p>Property improvements</p> <p>Reduced home foreclosures</p> <p>Reduced need to move/relocate due to unpaid bills</p>
Society	<p>Typically, none.</p>	<p>Alleviating poverty</p> <p>Improving low-income community strength and resiliency</p> <p>Reduced home foreclosures</p>

STEP 3

Treatment of Low-Income Impacts: States using TRC Test



STEP 3

Treatment of LI Impacts: States with Utility Cost Test

State	Summary	Details
Connecticut	No Threshold	Low-income programs that do not pass the cost-effectiveness test are still approved due to additional benefits that accrue to low-income customers. CT DPUC 1999; CT DPUC 2010.
Michigan	No Threshold	Low-income program offerings are excluded from the cost-effectiveness requirement. Act 295, § 71(3)(g).
New Mexico	Quantified, but very narrow definition	"In developing [the Utility Cost] test for energy efficiency and load management programs directed to low-income customers, the commission shall either quantify or assign a reasonable value to reductions in working capital, reduced collection costs, lower bad-debt expense, improved customer service effectiveness and other appropriate factors as utility system economic benefits."
Texas	Different Test	The cost-effectiveness of measures eligible to be installed [in low income programs] and the overall program shall be evaluated using the Savings-to-Investment (SIR) ratio (i.e., the ratio of the present value of a customer's estimated lifetime electricity cost savings from energy efficiency measures to the present value of the installation costs, inclusive of any incidental repairs, of those energy efficiency measures).
Utah	Adder, but very small	The total resource cost test plus a 10 percent benefit adder to account for non-quantified environmental and non-energy benefits of conservation resources over supply side alternatives. 2013 DSM Report.

STEP 3

Other Fuel Impacts

When an efficiency program paid for by electricity customers also reduces (or increases) consumption of other fuels (gas, oil, propane, wood).

Program Options	Examples
Multi-Fuel Measures and Programs	To address new construction, home energy retrofits, HVAC measures
Fuel-Optimization Programs	To switch fuels use to the most efficient or least carbon intensive
Fuel-Neutral Programs	To offer whole-building programs and one-stop-shopping
CHP Programs	To make process heat as efficiently as possible
Strategic Electrification Programs	To reduce carbon emissions from space heating and electric vehicles

Question: Why should electricity customers pay for other fuel savings that accrue to gas, oil, and other customers?

Participant Non-Energy Impacts

Category	Examples
Asset value	<ul style="list-style-type: none"> • Equipment functionality/performance improvement • Equipment life extension • Increased building value • Increased ease of selling building
Productivity	<ul style="list-style-type: none"> • Reduced labor costs • Improved labor productivity • Reduced waste streams • Reduced spoilage/defects • Impact of improved aesthetics, comfort, etc. on product sales
Economic well-being	<ul style="list-style-type: none"> • Fewer bill-related calls to utility • Fewer utility intrusions & related transactions costs (e.g., shut-offs, reconnects) • Reduced foreclosures • Fewer moves • Sense of greater “control” over economic situation • Other manifestations of improved economic stability
Comfort	<ul style="list-style-type: none"> • Thermal comfort • Noise reduction • Improved light quality
Health & safety	<ul style="list-style-type: none"> • Improved “well-being” due to reduced incidence of illness—chronic (e.g., asthma) or episodic (e.g., hypothermia or hyperthermia) • Reduced medical costs (emergency room visits, drug prescriptions) • Fewer sick days (work and school) • Reduced deaths • Reduced insurance costs (e.g., for reduced fire, other risks)
Satisfaction/pride	<ul style="list-style-type: none"> • Improved sense of self-sufficiency • Contribution to addressing environmental/other societal concerns

STEP 3

Participant Non-Energy Impacts

- There are many such impacts.
- Some of them can be very large.
- Some of them are more important to customers than energy benefits.
- They vary significantly across programs.
- They can be difficult to measure, quantify, and monetize.
- Estimates are often uncertain.
- Symmetry Principle:
 - If participant costs are included, then participant NEIs should be also.
 - If participant NEIs are not included, participant costs should not be.
- Hard-to-Quantify Principle:
 - Relevant impacts cannot be ignored just because they are difficult to quantify.
- The choice of whether to include participant NEIs is up to each jurisdiction, based on policy goals and considerations above.

STEP 3

Economic Development and Job Impacts

Job Impact estimates must be sound:

- Reflect the net impact, relative to supply-side options
- Be clear about boundaries (typically this means state impacts)

Three types of job impacts:

- a) Implementation of EE measures
- b) Jobs created by supplying and supporting EE implementation
- c) Jobs created as a result of utility bill savings

Whether to include job impacts is a policy decision.

How to include job impacts is challenging:

- Potential for double counting
- Can the job dollars be added to the other dollars?

Safest option is to present the job impact results alongside the other results.

STEP 4

Ensure Symmetry Across Benefits and Costs

- Ensure that the test includes costs and benefits symmetrically
 - If category of cost is included, corresponding benefits should be too (e.g., if participant costs included, participant benefits should also be included)
- Symmetry is necessary to avoid bias:
 - If some costs excluded, the framework will be biased in favor of EE;
 - If some benefits excluded, the framework will be biased against EE.
 - Bias in either direction can result in misallocation of resources (over or under investment)
 - higher than necessary costs to meet energy needs
 - too little or too much investment in actions to achieve jurisdiction's energy related policies goals

STEP 5

Conduct Incremental, Forward Looking and Long-Term Analysis

- Incremental: What would have occurred relative to baseline.
 - Has implications for avoided costs.
- Forward looking: Sunk costs and benefits are not relevant to cost-effectiveness analysis.
 - Has implications regarding the Rate Impact Measure (RIM) test.
- Long-term: Analysis should capture full remaining lifecycle costs and benefits.
 - Has implications for the length of the study period.

STEP 5

Limitations of the Rate Impact Measure Test

- The RIM Test not appropriate for cost-effectiveness analyses:
 - Is inconsistent with economic theory. The RIM test includes sunk costs, which should not be used for choosing new investments
 - Does not provide meaningful information about the magnitude of rate impacts, or customer equity
 - Will not result in lowest costs to customers
 - Can lead to perverse outcomes, where large benefits are rejected to avoid de minimus rate impacts
 - Can be misleading. Results suggest that customers will be exposed to new costs, which is not true
- Other approaches should be used to assess rate and equity issues.

STEP 5

Better Options for Assessing Rate Impacts

A thorough understanding of rate impacts requires a comprehensive analysis of three important factors:

- Rate impacts, to provide an indication of the extent to which rates for all customers might increase.
- Bill impacts, to provide an indication of the extent to which customer bills might be reduced for those customers that install distributed energy resources.
- Participation impacts, to provide an indication of the portion of customers that will experience bill reductions or bill increases.

Taken together, these three factors indicate the extent to which customers will benefit from energy efficiency resources.

Participation impacts are also key to understanding the extent to which energy efficiency resources are being adopted over time.

STEP 5

Example Bill Impact Analysis – Rhode Island

Table 2: Residential Bill Impact Analysis – A16 (2018 EE Plan vs. No EE)

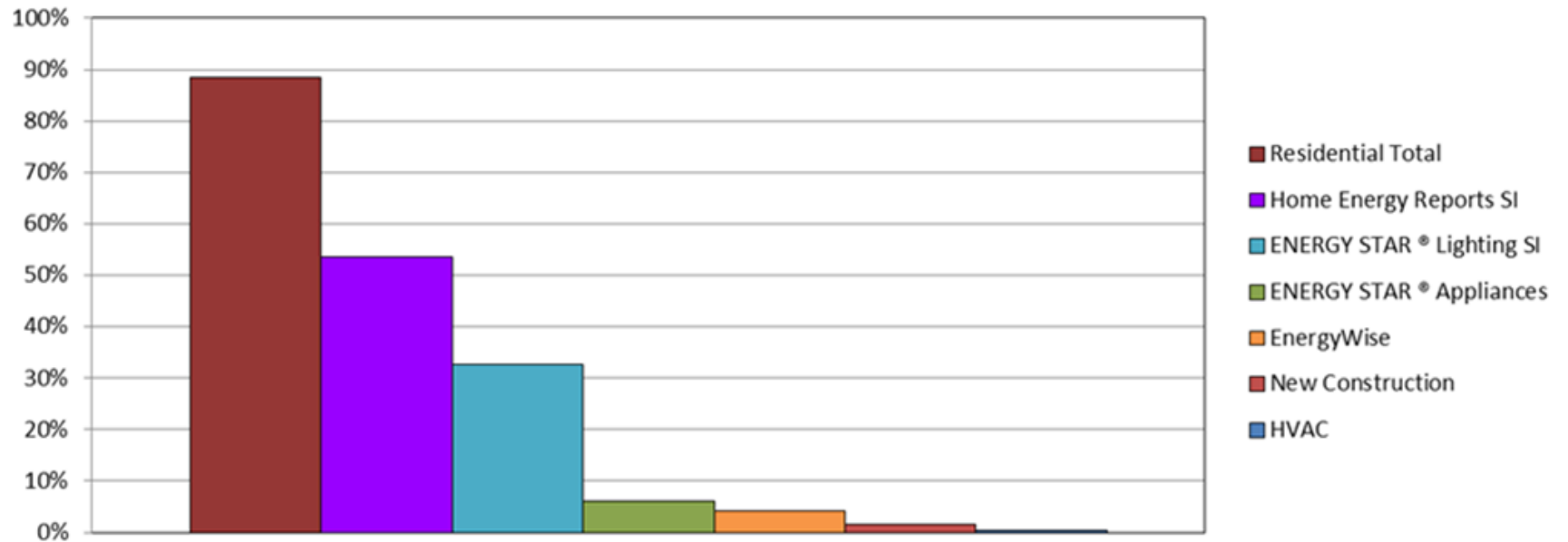
Residential	Long-Term Rate Impacts	Typical Energy Savings	Typical Bill Savings
	(% of Total Rate)	(% per Participant)	(% of Total Bill)
Average Participant	1.31%	2.02%	1.56%
Non-Participant	1.31%	0.00%	-1.31%
Average Customer	1.31%	1.87%	1.35%

Table 4: Small Commercial Bill Impact Analysis – C06 (2018 EE Plan vs. No EE)⁵

	Long-Term Rate Impacts	Typical Energy Savings	Typical Bill Savings
	(% of Total Rate)	(% per Participant)	(% of Total Bill)
Small C&I Participant	0.54%	17.60%	15.80%
Non-Participant	0.54%	0.00%	-0.54%
Average Customer	0.54%	1.45%	0.81%

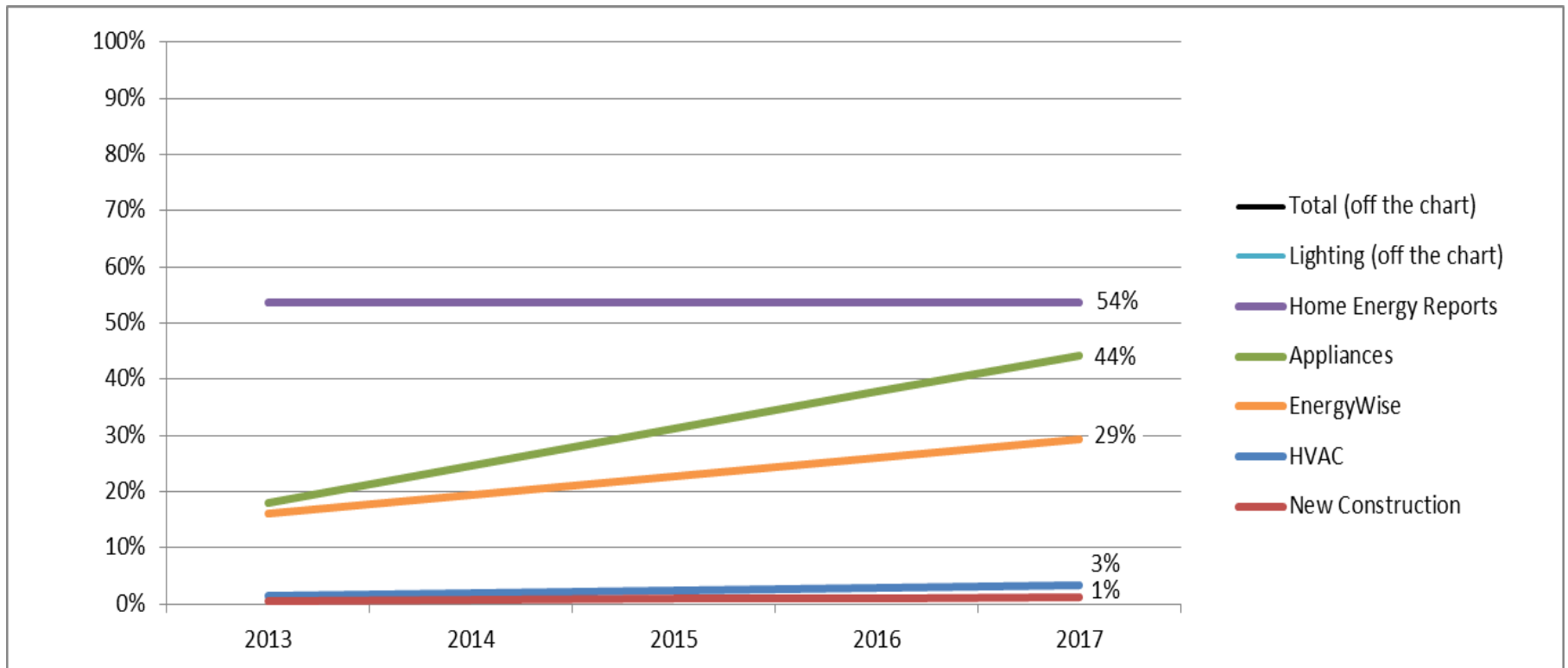
STEP 5

Rhode Island EE Participation - Annual



STEP 5

Rhode Island EE Participation - Cumulative



STEP 5

Participation Can be Increased by Program Design

- EE programs should address all end-uses.
- EE programs should address all customer types.
- EE programs should address all relevant markets:
 - retrofit, new construction, point-of-sale, upstream, etc.
- All customers should have an opportunity to participate.
- Customer incentives and support should be tailored to assist all customers in overcoming barriers to energy efficiency.
- Program Administrators should actively pursue the non-participants and those who have not participated in a while.

STEP 5

Participation Can Be Increased by Policy Directives

- Increase budgets to increase participation.
 - This is the exact opposite of the typical response to rate impact concerns.
- Require program administrators to gather better data on participation.
- Require program administrators to analyze participation rates when designing programs.
- Include participation requirements in efficiency plans and goals.
- Incorporate participation rates in utility shareholder incentives.
- Make the participation goal explicit:
 - Achieving all cost-effective energy efficiency means serving all customers.

STEP 6

Develop Methodologies and Inputs to Account for All Impacts, Including Hard-to-Quantify Impacts

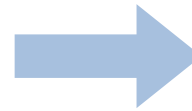
Approach	Application
Jurisdiction-specific studies	Best approach for estimating and monetizing relevant impacts.
Studies from other jurisdictions	Often reasonable to extrapolate from other jurisdiction studies when local studies not available.
Proxies	If no relevant studies of monetized impacts, proxies can be used
Alternative thresholds	Benefit-cost thresholds different from 1.0 can be used to account for relevant impacts that are not monetized.
Other considerations	Relevant quantitative and qualitative information can be used to consider impacts that cannot or should not be monetized.

STEP 7

Ensure Transparency in Reporting

Sample Template

Efficiency Cost-Effectiveness Reporting Template			
Program/Sector/Portfolio Name:		Date:	
A. Monetized Utility System Costs		B. Monetized Utility System Benefits	
Measure Costs (utility portion)		Avoided Energy Costs	
Other Financial or Technical Support Costs		Avoided Generating Capacity Costs	
Program Administration Costs		Avoided T&D Capacity Costs	
Evaluation, Measurement, & Verification		Avoided T&D Line Losses	
Shareholder Incentive Costs		Energy Price Suppression Effects	
		Avoided Costs of Complying with RPS	
		Avoided Environmental Compliance Costs	
		Avoided Bad Debt, Arrearages, etc.	
		Reduced Risk	
Sub-Total Utility System Costs		Sub-Total Utility System Benefits	
C. Monetized Non-Utility Costs		D. Monetized Non-Utility Benefits	
Participant Costs		Participant Benefits	
Low-Income Customer Costs	<i>These impacts would be included to the extent that they are part of the Resource Value (primary) test.</i>	Low-Income Customer Benefits	<i>These impacts would be included to the extent that they are part of the Resource Value (primary) test.</i>
Other Fuel Costs		Other Fuel Benefits	
Water and Other Resource Costs		Water and Other Resource Benefits	
Environmental Costs		Environmental Benefits	
Public Health Costs		Public Health Benefits	
Economic Development and Job Costs		Economic Development and Job Benefits	
Energy Security Costs		Energy Security Benefits	
Sub-Total Non-Utility Costs		Sub-Total Non-Utility Benefits	
E. Total Monetized Costs and Benefits			
Total Costs (PV\$)		Total Benefits (PV\$)	
Benefit-Cost Ratio		Net Benefits (PV\$)	
F. Non-Monetized Considerations			
Economic Development and Job Impacts	<i>Quantitative information, and discussion of how considered</i>		
Market Transformation Impacts	<i>Qualitative considerations, and discussion of how considered</i>		
Other Non-Monetized Impacts	<i>Quantitative information, qualitative considerations, and how considered</i>		
Determination:	Do Efficiency Resource Benefits Exceed Costs? [Yes / No]		



B. Monetized Utility System Benefits	
Avoided Energy Costs	
Avoided Generating Capacity Costs	
Avoided T&D Capacity Costs	
Avoided T&D Line Losses	
Energy Price Suppression Effects	
Avoided Costs of Complying with RPS	
Avoided Environmental Compliance Costs	
Avoided Bad Debt, Arrearages, etc.	
Reduced Risk	
Total Utility System Benefits	



D. Monetized Non-Utility Benefits	
Economic Development and Job Benefits	
Energy Security Benefits	
Sub-Total Non-Utility Benefits	
Total Benefits (PV\$)	
Net Benefits (PV\$)	
<i>Quantitative information, and discussion of how considered</i>	
<i>Qualitative considerations, and discussion of how considered</i>	
<i>Quantitative information, qualitative considerations, and how considered</i>	
Do Efficiency Resource Benefits Exceed Costs? [Yes / No]	

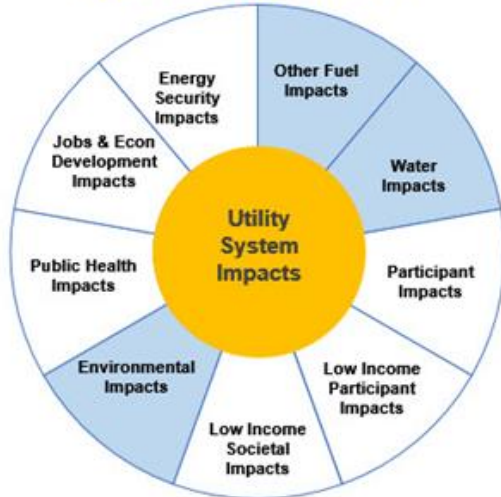
STEP 7

Ensure Transparency in Decisions on Which Non-Utility System Impacts To Include

- Process should be open to all stakeholders.
- Stakeholder input can be achieved through a variety of means:
 - rulemaking process,
 - generic jurisdiction-wide docket,
 - working groups or technical sessions,
- Address objectives based on current jurisdiction policies
 - However, be flexible to incorporate evolution of policies through time.
- Policy goals may require consultation with other government agencies
 - Environmental protection
 - Health and human services
 - Economic development

Relationship of Resource Value Test (RVT) to Traditional Tests – Results May Align or Not

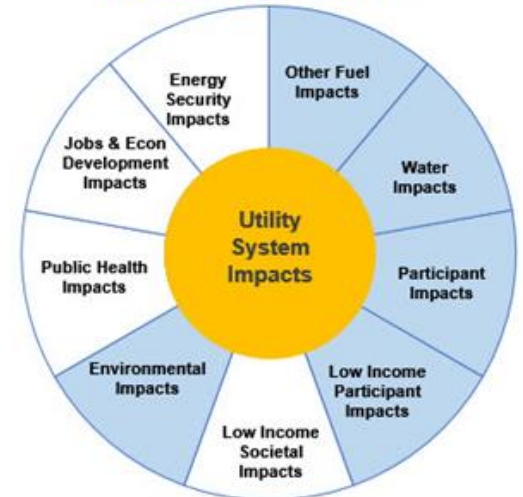
JURISDICTION 1: RVT



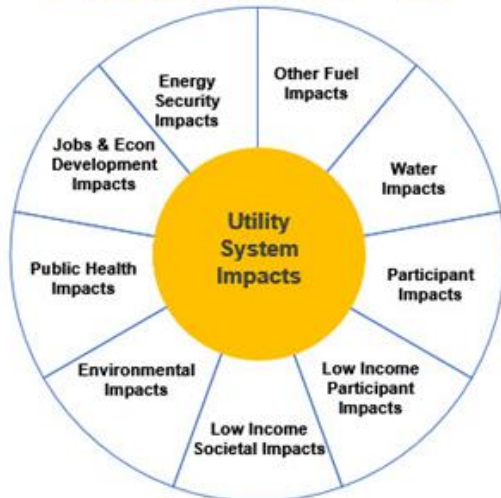
JURISDICTION 2: RVT



JURISDICTION 3: RVT



JURISDICTION 4: RVT = UCT



JURISDICTION 5: RVT = TRC



JURISDICTION 6: RVT = SCT



Relationship of RVT to Traditional Tests (2)

Impacts	Jurisdiction					
	1 RVTs Differ from Any Traditional Test	2	3	4 RVT = UCT	5 RVT = TRC	6 RVT = SCT
Utility System	✓	✓	✓	✓	✓	✓
Other Fuels	✓	✓	✓		✓	✓
Water	✓		✓		✓	✓
Participants			✓		✓	✓
Low-Income Participants		✓	✓		✓	✓
Low-Income Societal		✓				✓
Environmental	✓		✓			✓
Public Health		✓				✓
Economic Development		✓				✓
Energy Security		✓				✓

- Each cost-effectiveness test should include the utility system impacts.
- The other impacts included should be based on a jurisdiction’s applicable policy goals.
- In some jurisdictions, this may result in a Resource Value Test equal to one of the traditional tests.
- In other jurisdictions, the RVT may be different.

Part II

Developing Inputs for Cost-Effectiveness Tests

Part II

6. Efficiency Costs and Benefits
7. Methods to Account for Costs & Benefits
8. Participant Impacts
9. Discount Rates
10. Assessment Level
11. Analysis Period and End Effects
12. Analysis of Early Retirement
13. Free Rider and Spillover Effects

Steps for Choosing a Discount Rate

Choice of discount rate should reflect analysis objective: *to identify resources that will best serve customers over the long term, while achieving applicable policy goals*

Step A	<u>Articulate the jurisdiction's applicable policy goals.</u> These should be the same goals used in developing the RVT.
Step B	<u>Consider the relevance of a utility's weighted average cost of capital.</u> Is the utility investor time preference consistent with the jurisdiction's policy goals?
Step C	<u>Consider the relevance of the average customer discount rate.</u> Should the discount rate be based on the average utility customer time preference? Does this time preference adequately address applicable policy goals and future customers?
Step D	<u>Consider the relevance of a societal discount rate.</u> Is a societal time preference and use of a societal discount rate consistent with the jurisdiction's policy goals and associated regulatory perspective?
Step E	<u>Consider an alternative discount rate.</u> Given that the regulatory perspective may be different from the utility, customer, and societal perspective, the discount rate does not need to be tied to any one of these three perspectives.
Step F	<u>Consider risk implications.</u> Consider using a low-risk discount rate for EE cost-effectiveness, if the net risk benefits of EE resources are not somehow accounted for elsewhere in the cost-effectiveness analysis

Additional Foundational Information

<h2>Assessment Level</h2>	<ul style="list-style-type: none"> • Analysis at all levels can provide valuable insight/value - but focus should be only on program, sector, or portfolio level for making “yes or no” investment decisions • EE program costs should be included at the level at which they are truly variable
<h2>Analysis Period and End Effects</h2>	<ul style="list-style-type: none"> • Should be long enough to cover lifecycle costs and benefits • 2nd best alternative is to amortize/annualize costs • Comparable portions of costs/benefits over shorter analysis period
<h2>Analysis of Early Replacement</h2>	<ul style="list-style-type: none"> • Should reflect that up-front cost is partially offset by value of deferring the next replacement (e.g., replacing now means not having to replace in 5 years) • May need to also account for shifting efficiency baseline and resulting different savings levels in different future years
<h2>Free-Riders and Spillover</h2>	<ul style="list-style-type: none"> • Treatment should be a function of categories of impacts included in RVT • Free-riders: participant rebates are only a cost if test excludes participant impacts • Spillover: is an additional cost only if test includes participant impacts

Appendix A

The Traditional Cost-Effectiveness Tests

Test	Perspective	Key Question Answered	Summary Approach
Utility Cost	The utility system	Will utility system costs be reduced?	Includes the costs and benefits experienced by the utility system
Total Resource Cost	The utility system plus participating customers	Will utility system costs plus program participants' costs be reduced?	Includes the costs and benefits experienced by the utility system, plus costs and benefits to program participants
Societal Cost	Society as a whole	Will total costs to society be reduced?	Includes the costs and benefits experienced by society as a whole
Participant Cost	Customers who participate in an efficiency program	Will program participants' costs be reduced?	Includes the costs and benefits experienced by the customers who participate in the program
Rate Impact Measure	Impact on rates paid by all customers	Will utility rates be reduced?	Includes the costs and benefits that will affect utility rates, including utility system costs and benefits plus lost revenues

Appendix B

EE vs Distributed Energy Resources Utility System Impacts

		Energy Efficiency	Demand Response	Distributed Generation	Distributed Storage
Costs					
Utility System	Measure costs (utility portion)	●	◐	○	○
	Other financial incentives	●	●	◐	◐
	Other program and administrative costs	●	◐	◐	◐
	Evaluation, measurement, and verification	●	●	●	●
	Performance incentives	◐	◐	◐	◐
	Interconnection costs	○	○	●	●
	Distribution system upgrades	○	○	●	●
Benefits					
Utility System	Avoided energy costs	●	◐	●	◐
	Avoided generation capacity costs	●	●	●	●
	Avoided reserves or other ancillary services	●	●	●	●
	Avoided T&D system investment	●	●	●	●
	Avoided T&D line losses	●	●	●	●
	Wholesale market price suppression	●	●	●	●
	Avoided RPS or EPS compliance costs	●	◐	●	◐
	Avoided environmental compliance costs	●	◐	●	◐
	Avoided credit and collection costs	◐	◐	◐	◐
	Reduced risk	●	●	◐	◐

Appendix B

EE vs Distributed Energy Resources **Non-Utility System Impacts**

		Energy Efficiency	Demand Response	Distributed Generation	Distributed Storage
Costs					
Non-Utility	Measure costs (participant portion)	●	●	●	●
	Interconnection fees	○	○	◐	◐
	Annual O&M	○	○	●	●
	Participant increased resource consumption	◐	◐	◐	◐
	Non-financial (transaction) costs	◐	●	○	○
Benefits					
Non-Utility	Reduced low-income energy burden	◐	◐	◐	◐
	Public health benefits	●	◐	●	◐
	Energy security	●	◐	●	◐
	Jobs and economic development benefits	●	●	●	●
	Environmental benefits	●	◐	●	◐
	Participant health, comfort, and safety	◐	○	○	○
	Participant resource savings (fuel, water)	◐	○	○	○

Appendix C

Limitations of the Rate Impact Measure Test

- The RIM Test not appropriate for cost-effectiveness analyses:
 - Does not provide meaningful information about the magnitude of rate impacts, or customer equity
 - Will not result in lowest costs to customers
 - Is inconsistent with economic theory. The RIM test includes sunk costs, which should not be used for choosing new investments
 - Can lead to perverse outcomes, where large benefits are rejected to avoid de minimus rate impacts
 - Can be misleading. Results suggest that customers will be exposed to new costs, which is not true
- Other approaches should be used to assess rate and equity issues.

Appendix C

Better Options for Assessing Rate Impacts

A thorough understanding of rate impacts requires a comprehensive analysis of three important factors:

- Rate impacts, to provide an indication of the extent to which rates for all customers might increase.
- Bill impacts, to provide an indication of the extent to which customer bills might be reduced for those customers that install distributed energy resources.
- Participation impacts, to provide an indication of the portion of customers that will experience bill reductions or bill increases.

Taken together, these three factors indicate the extent to which customers will benefit from energy efficiency resources.

Participation impacts are also key to understanding the extent to which energy efficiency resources are being adopted over time.

For more information visit:
<http://www.nationalefficiencyscreening.org/>