

COMMONWEALTH OF PENNSYLVANIA



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July 6, 2009

James J. McNulty
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

RE: Compliance of Commonwealth of
Pennsylvania with Section 410(a) of the
American Recovery and Reinvestment
Act of 2009
Docket No. I-2009-2099881

Dear Secretary McNulty:

Enclosed are Comments of the Office of Consumer Advocate, in the above-referenced proceeding.

Should you have any questions, please contact me at the number above.

Respectfully Submitted,

A handwritten signature in cursive script that reads "Tanya J. McCloskey".

Tanya J. McCloskey
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50044

Enclosure

cc: Steven Bainbridge, Law Bureau – e-mail only
Ed Berzonsky, FUS – e-mail only

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Compliance of Commonwealth of	:	
Pennsylvania with Section 410(a)	:	Docket No. I-2009-2099881
of the American Recovery and	:	
Reinvestment Act of 2009	:	

COMMENTS OF THE
OFFICE OF CONSUMER ADVOCATE

I. INTRODUCTION

On May 16, 2009, the Commission’s Investigation Order concerning Compliance of Commonwealth of Pennsylvania with Section 410(a) of the American Recovery and Reinvestment Act of 2009 was published in the Pennsylvania Bulletin. Through this Order, the Commission initiated an investigation to consider whether any Commission policies or actions should be implemented to ensure compliance with the requirements of Section 410(a) of the American Recovery and Reinvestment Act of 2009 (ARRA or Recovery Act). Specifically, the Commission stated that the investigation will consider the various policies and actions the Commission should implement to ensure that appropriate incentives are in place to align utility financial incentives with the promotion of energy efficiency and conservation by consumers. Investigation Order at 3. The Commission also stated that it anticipates that proposed federal energy legislation may mandate that Pennsylvania electric and natural gas utilities reduce the amount of energy that they sell in order to conserve resources and protect the environment. The

Commission requested that comments also consider the potential effect that such federal energy legislation may have on the business models of Pennsylvania electric and natural gas utilities.

The American Recovery and Reinvestment Act of 2009 was designed to stimulate the United States economy in several ways. One element of the Act was intended to enhance energy efficiency programs, with much of the funding for such programs to go to the States. In order to qualify for a portion of that funding, Section 410(a) of the Act requires the Governor of a recipient State to notify the Secretary of Energy that the Governor has obtained certain assurances regarding that State's energy efficiency policies. Among the assurances that the Governor must provide is the following:

- (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 the 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 customer's incentives to use energy more efficiently.

Section 410(a)(1) of ARRA.

In response to this provision, Governor Rendell sent a letter to the Commission asking that the Commission:

[C]onsider additional steps the Commonwealth can take to establish appropriate incentives in electric and natural gas utility rates for energy efficiency programs, consistent with State law, the attached statute [the Recovery Act], and relevant PURPA requirements. These include policies to align interests of utilities to support conservation without raising the cost of conservation and increasing the cost to ratepayers of measurable, verifiable efficiency savings.

Investigation Order at 3, quoting Letter of Governor Edward G. Rendell.

The OCA submits that through prior enactments of the General Assembly and Commission policies, the Commonwealth already meets the requirement that the interests of

customers and utilities to support conservation are properly aligned. As Governor Rendell notes in his Letter, it is critical to support conservation without increasing the cost to ratepayers associated with these efficiency savings. The statutes and policies of the Commonwealth have achieved this necessary balance in a manner that will enable customers to use energy more efficiently, provide timely cost recovery for utilities, and provide a reasonable opportunity for the utility to earn a fair rate of return. As discussed further in these comments, the OCA submits that there is no need for any wide scale changes in Pennsylvania law or Commission ratemaking policies to meet the requirements of Section 410(a) of the Recovery Act, as current laws and ratemaking treatment properly align the financial incentives of customers and utilities.

II. PENNSYLVANIA LAWS, REGULATIONS AND POLICIES MEET THE REQUIREMENTS OF SECTION 410(a) OF ARRA

A. Several Pennsylvania Statutes Currently Address Energy Conservation Measures In A Manner that Aligns Utility Financial Incentives With Helping Consumers Use Energy More Efficiently.

Both the Commission and the General Assembly long ago recognized the importance of energy conservation and energy efficiency measures to Pennsylvania's future. In 1986, the General Assembly included several provisions in the Pennsylvania Public Utility Code to address the implementation of energy conservation measures, to provide for timely cost recovery of any implemented measures, and to provide for performance factor considerations related to actions (or failure to act) to encourage the development of conservation and load management measures. Specifically, through the 1986 amendments known as Act 114 of 1986, the following sections were included in the Public Utility Code:

Section 1505(b)—Authority to order conservation and load management: This section provides that the Commission may order the utility to establish a conservation and load management program as part of determining or prescribing safe, adequate and sufficient service.

Section 1319—Financing of energy supply alternatives (specifically conservation and load management programs): This section provides for the recovery of all prudent and reasonable costs of conservation and load management programs.

Section 523(b)(4)—Performance factor considerations related to conservation and load management: This section provides for consideration for actions or failure to act to encourage the development of cost effective conservation and load management programs when determining just and reasonable rates.

66 Pa. C.S. §§523(b)(4), 1319, 1505(b).¹

Additionally, the Commission's regulations recognized the importance of providing weatherization and other conservation measures for low income customers in the 1980s when the Commission established the requirement that each electric and natural gas utility establish usage reduction programs for their low income customers, programs that have become known as the Low Income Usage Reduction Program (LIURP). 52 Pa. Code Chapter 58. Importantly, as Pennsylvania subsequently undertook the restructuring of its electric industry to introduce retail choice for customers, and expanded retail choice for its natural gas customers in 1996 and 1999, respectively, the General Assembly took care to ensure the continuation of these energy conservation programs and to ensure the full and current recovery of dollars spent on the programs. 66 Pa.C.S. §§2802(17); 2804(8) and (9); and 2203(6), (7), and (8). A recent study of Pennsylvania's LIURP programs found that since 1988, over \$330 million has been spent on weatherization treatments for more than 292,071 households. Long Term Study of Pennsylvania's Low Income Usage Reduction Program, John Shingler, Consumer Services Information Project, Penn State University (January 2009). In the most recent reporting year of 2007, Pennsylvania residential ratepayers have supported the LIURP programs at an annual level

¹ The OCA would also note that Section 524 requires electric utilities to supply data to the Commission on, among other things, the potential for promoting and ensuring the full utilization of all practical and economical energy conservation and how the utility has integrated demand-side measures in its resource mix. 66 Pa.C.S. §524(a)(3) and (4). While many of the requirements of Section 524 have become inapplicable as a result of restructuring, these reports are still required to be filed with the Commission. Additionally, Section 511.1 authorizes the Commission to apply for the use of federal funds related to energy conservation research and development. 66 Pa.C.S. §511.1.

of about \$28 million, reaching approximately 24,753 low income homes annually with some form of energy efficiency service. 2007 Bureau of Consumer Services Universal Service Report, pp. 33-34. As provided for by the statute, full and timely cost recovery for these programs is provided through reconcilable surcharge mechanisms for most Pennsylvania electric and gas companies.

The General Assembly also recognized the importance of energy efficiency when enacting Pennsylvania's Alternative Energy Portfolio Standards (AEPS) Act in 2004. Under the AEPS Act, energy efficiency technologies and demand response or load management technologies are specifically recognized as alternative energy sources. 73 P.S. §1648.2. These resources can be used to meet the Tier II requirements. 73 P.S. §§1648.2 and 1648.3. As such, alternative energy credits associated with energy efficiency and demand response programs would be recoverable on a full and current basis through an automatic adjustment clause pursuant to Section 1307. 73 P.S. §1648.3(a)(3).

The most significant development in Pennsylvania statutes and policies regarding energy efficiency occurred last year through the passage of Act 129 of 2008. Act 129 of 2008 ensures that the State regulatory authority, the Pennsylvania Public Utility Commission, will implement energy efficiency programs in a manner that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently and in a manner that provides timely cost recovery and an opportunity to earn a fair rate of return. Act 129 requires each major electric distribution company (EDC) in Pennsylvania to reduce energy consumption by a minimum of 1% by May 31, 2011 and by a minimum of 3% by May 31, 2013. 66 Pa.C.S. §2806.1(c). Each EDC was required to file a plan on July 1, 2009 designed to achieve these reductions. The Commission is required to review the plans and issue Orders with regard to the

plan in 120 days. The failure of an EDC to achieve the specified reduction targets results in a financial penalty of not less than \$1,000,000 and not more than \$20,000,000. 66 Pa.C.S. §2806.1(f)(2). If an EDC fails to achieve the required reductions, the Commission is authorized to implement a plan to achieve the reductions and contract with a conservation service provider to implement the plan. 66 Pa.C.S. §2806.1(f)(2)(ii).

The OCA submits that Act 129 of 2008 assures that the Commission has ratemaking authority, and will implement the policies of Act 129 to assure that utility financial incentives are aligned with helping customers use energy efficiently, that timely cost recovery is provided, and that a timely earnings opportunity remains. Act 129 provides for the recovery of all prudent and reasonable costs associated with energy efficiency measures through a reconcilable surcharge recovery mechanism. 66 Pa.C.S. §2806.1(k). Such a recovery mechanism ensures timely recovery of all prudent and reasonable costs incurred by the utility.

Act 129 also provides a timely earnings opportunity for the utility in several ways. First, the reconcilable surcharge recovery mechanism ensures that the earnings opportunity for the utility is preserved. Second, Act 129 specifically allows for any decreased revenue and reduced energy consumption related to the programs to be reflected in the revenue and sales data used to calculate rates in the next distribution base rate proceeding. 66 Pa.C.S. §2806(k). This, too, will ensure that the impacts of energy conservation on the utility's operations and ability to earn a return is reflected in rates. While Act 129 does not permit the recovery of lost revenues from conservation measures to be recovered as part of the reconcilable surcharge, the ARRA does not require such rate treatment. In Pennsylvania, the General Assembly has determined that such a mechanism is not needed to properly incentivize energy efficiency and demand response programs.

Finally, the General Assembly has imposed mandatory penalties on electric utilities who do not meet the requirements of the Act. These prospective penalties assure that the electric utility has the proper financial incentive to perform. Failure to perform as required by the Act would result in penalties that would not be recovered from ratepayers, *i.e.*, they would be at shareholder expense. Assuring that the shareholders have a stake in the outcome of these programs through the penalty provisions will align the financial interests of the utility with those of its customers.

While Act 129 applies only to electric companies, the Commission is authorized through various sections of the Public Utility Code to order energy efficiency programs for natural gas companies and to provide timely cost recovery and earnings opportunity associated with such programs. As noted above, through Section 1505(b), the Commission is authorized to order a utility to establish conservation and load management programs.² Section 1319 provides that the Commission shall allow the recovery of conservation or load management programs implemented by a natural gas or electric utility that are found to be prudent and cost effective. The Commission is also required to consider a natural gas utility's efforts in pursuing cost-effective conservation and load management opportunities when determining just and reasonable rates. 66 Pa.C.S. §523; 52 Pa. Code §69.35. With these provisions of the Public Utility Code, and the additional guidance provided to the Commission in Act 129, the Commission has full ratemaking authority to align the interests of natural gas utilities and customers as it concerns using energy more efficiently.

The OCA submits that the Public Utility Code already gives the Commission the authority to meet the requirements of Section 410(a) of the ARRA. From a review of the Public

² The OCA would note that Section 1505(b) refers to the Commission's authority to prescribe safe, adequate and sufficient service. Section 1501 provides, among other things, that every public utility must provide safe, adequate, efficient, safe and reasonable service. 66 Pa.C.S. §1501.

Utility Code, the OCA submits that the Commission need not recommend any changes or new efforts to the General Assembly to meet the requirements of Section 410(a) of ARRA.

As discussed below, through its regulations, Orders, implementation of Act 129, and implementation of other Sections of the Public Utility Code, the Public Utility Commission's efforts ensure that utilities and customers have the proper incentives to use energy more efficiently. The Commission should continue with its current initiatives as they assure full compliance with Pennsylvania Law and the requirements of Section 410(a) of ARRA.

B. The Commission's Ratemaking Authority, Regulations And Policies Provide For Proper Financial Incentives, Timely Cost Recovery And An Opportunity To Earn A Fair Rate Of Return.

1. Through its Regulations, Policy Statements and Orders, The Commission Has Sought To Advance Energy Efficiency In The Commonwealth.

The statutory provisions and guidance of the General Assembly are not the only means by which the Commission meets, or can meet, the requirements of Section 410(a) of ARRA. While the statutes ensure proper authority to the Commission to meet the requirements set forth in Section 410(a) of ARRA, the Commission has also promulgated regulations, issued Policy Statements and issued Orders to sustain or enhance the incentives of customers and utilities to use energy more efficiently, to provide timely cost recovery and an opportunity for a utility to earn a fair rate of return.

As an initial matter, the OCA again notes that the Commission's support of energy efficiency as a means to assist low income customers in affording their energy service has been strong. Through Chapter 58 of the Commission regulations addressing the Low Income Usage Reduction Programs (LIURP), Pennsylvania electric and natural gas companies have implemented some of the best programs in the Nation for delivering weatherization, efficiency

and conservation measures to low income customers. 52 Pa. Code Chapter 58. As noted earlier, since 1988, Pennsylvania's natural gas and electric companies were able to provide weatherization treatment to 292,071 low income households. Residential ratepayers have supported this effort with over \$330 million. Currently, residential ratepayers are supporting these programs mostly through dollar-for-dollar cost recovery mechanisms.

The Commission has also taken steps to encourage the use of energy efficiency as a means to mitigate the bill impact of the anticipated rate increases that will occur at the end of the rate cap period in 2010 and 2011. The Commission has directed each electric distribution company to initiate a consumer education and awareness campaign in anticipation of the end of the rate cap period. Some of the key messages of that education campaign are to inform customers of the benefits of energy efficiency in managing their bills and providing customers with information on energy efficiency measures and opportunities. The Commission specified the following Education Standards:

- Customers can control the size of their electric bills through energy efficiency, conservation and demand response measures. Customers can benefit from utilizing these measures now, even if the rate cap is still in effect where they reside.
- Cost-effective energy efficiency, conservation and demand side response programs and technologies have been identified and information about them is readily available.

Policies to Mitigate Potential Price Increases, Docket No. M-00061957, *slip op.* at 6 (Order entered May 17, 2007).

The OCA would also note that the Commission has regulations and policy statements in place that allow the Commission to monitor energy conservation efforts, ensure that certain conservation standards are met, and provide for the timely recovery of cost-effective energy conservation programs. For example, the Commission's regulations call for reporting on

energy conservation initiatives through its universal service and energy conservation reporting requirements for both electric and natural gas companies. 52 Pa. Code §54.71-78 (electric) and §62.5 (natural gas). The Commission also requires Annual Resource Planning Reports by electric and natural gas companies with such reports required to contain information on the conservation and load management programs implemented by the utility. 52 Pa. Code §57.141-149 (electric) and §59.81-84 (natural gas). Through these reports, the Commission can assess the on-going efforts of the companies in energy efficiency programs.

The OCA would also note that the Commission has issued Policy Statements addressing various aspects of energy efficiency, conservation and load management. For example, as early as 1983, the Commission adopted a Policy Statement on the financing of energy supply alternatives. 52 Pa. Code §§69.31 to 69.36. Among the energy supply alternatives included in the policy statement were conservation and load management initiatives. 52 Pa. Code §69.31 and §69.34. The policy statement provides for the rate treatment of the reasonable and prudent costs incurred for cost-effective conservation and load management to be at least on par with any supply option. 52 Pa. Code §69.35. Additionally, the policy statement allows the Commission to consider the utilities' efforts when the Commission establishes just and reasonable rates. 52 Pa. Code §69.35. Finally, the policy statement requires the utilities to annually provide customers with information on specific means to efficiently utilize energy services. 52 Pa. Code §69.35(1).

The Commission also has in place a Policy Statement regarding Building Energy Conservation Standards. 52 Pa. Code §§69.101-107. Under the Commission's Policy Statement, the Commission requires an electric utility to receive a certification of compliance with the applicable Building Energy Conservation Standards before establishing new service to a

residential building. In this way, the Commission assures that building energy conservation standards are being met as new service is established.

In the OCA's view, the Commission's efforts have been directed toward the development of cost-effective energy efficiency programs as a critical means of providing affordable bills for all customers. The Commission should continue these efforts, and along with the opportunities presented by Act 129 and the funding provided by ARRA, these efforts should allow customers and utilities to realize the benefits of energy efficiency measures.

2. The Commission Need Not Further Consider Rate Decoupling As A Response To Section 410(a) of ARRA.

The Commission has asked parties to comment on the issue of rate decoupling to encourage utility energy efficiency and conservation. Investigation Order at 5. The OCA submits that rate decoupling is not necessary to encourage energy efficiency, and, as became clear when National Fuel Gas Distribution Company proposed a rate decoupling mechanism in 2006, such mechanisms may not be well received by customers and may cause customers to have a negative impression of utility conservation programs. See, Pa. PUC v. National Fuel Gas Distribution Corporation, Docket No. R-00061493 (Order entered December 4, 2006)(Adopting Recommended Decision of ALJs Corbett and Moyer recounting public input testimony of 168 witnesses). More to the point, the General Assembly made clear in Act 129 of 2008 that such mechanisms are not to be used to address the potential for decreased revenues between base rate cases as a result of energy efficiency programs implemented by electric companies. 66 Pa.C.S. §2806.1(k). Rather, the General Assembly specifically provided in Act 129 that decreased revenues and reduced energy consumption are to be addressed prospectively in the context of a base rate proceeding. 66 Pa.C.S. §2806.1(k)(3).

As discussed above, the Commission has the statutory authority necessary to meet the requirements of Section 410(a) of the ARRA. The Commission also has full ratemaking authority to address the proper incentives for energy efficiency and can do so in many ways in the ratesetting process without introducing rate decoupling mechanisms. Energy efficiency initiatives can impact a utility in several ways as they relate to the rate setting process. First, the expenses associated with energy efficiency measures found to be reasonable, cost-effective and prudent must be reflected in rates. The Commission is authorized to reflect these reasonable expenses in rates and has recently approved a settlement for a natural gas utility including the cost of energy efficiency programs in distribution base rates.³ Pa. PUC v. PECO Energy Company - Gas Division, Docket No. R-2008-2028394, Joint Settlement ¶7.g (Order entered October 29, 2008). As discussed earlier, for electric companies, the Commission is authorized to establish a surcharge to provide for this cost recovery. 66 Pa.C.S. §2806.1(k).

Second, the impact of the efficiency program on future sales used to set rates can be properly reflected on a prospective bases in the rate setting process. In the context of a base rate case, the impact of the implementation of energy efficiency programs can be reflected in the prospective *pro forma* revenue and sales estimates when determining a just and reasonable level of rates. By reflecting the impact on sales in the context of the base rate case, the Commission can assure that prospective rates reflect the anticipated energy efficiency consumption reductions without unduly burdening ratepayers. This methodology is the approach set forth by the General Assembly for electric utilities. 66 Pa.C.S. §2806.1(k)(3). The OCA would also again note that the Commission is required to consider the energy efficiency efforts of a utility when setting just

³ As noted above, the Commission must also consider energy conservation and load management initiatives in determining just and reasonable rates in the ratemaking process. 66 Pa.C.S. §523(b)(4).

and reasonable rates. Section 523(b)(4) specifically requires the Commission to consider actions, or failure to act, in this regard.

Finally, in a base rate proceeding, the Commission must determine the appropriate rate design for each class. In particular, the design of the usage charges for both distribution rates and supply rates can have a significant impact on the conservation incentive provided to the customer. Historically, some Pennsylvania natural gas companies and Pennsylvania electric companies used a declining block rate structure. This form of rate structure, however, may no longer be consistent with current energy pricing and the need to implement energy efficiency. Through the base rate process, the Commission has recognized this point and exercised its authority to approve rate designs that are more aligned with conservation initiatives.⁴ See, e.g., Pa. PUC v. PG Energy, Docket No. R-00061365 (Order entered November 30, 2006) (Statement of then Vice Chairman Cawley noting that “the significant reduction in residential customer service charges from those in the case as filed, combined with the reduction or elimination of declining block charges for certain Honesdale customers, should help to provide strong incentives and rewards for energy conservation for these customers.”); Pa. PUC v. Duquesne Light Company, Docket No. R-00061346 (Order entered November 30, 2006)(Statement of then Vice Chairman Cawley regarding the reduction or elimination of declining block charges as an incentive for conservation).

As can be seen, the Commission has ratemaking authority to address issues related to energy efficiency through the ratemaking process, and has taken care to specifically consider these issues. This authority allows the Commission to provide financial incentives,

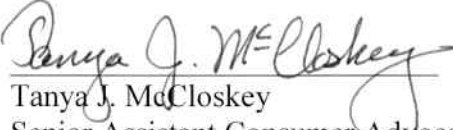
⁴ For electric utilities serving as provider of last resort, the Commission has also issued a policy statement encouraging each EDC to implement rate designs that do not incorporate declining blocks, demand charges or similar elements. The Commission regulation states that rate designs should encourage conservation. 52 Pa. Code §69.1810.

timely recovery and earnings opportunities. Section 410(a) of ARRA does not require any fundamental changes by the Commission to its method or process of setting just and reasonable rates, nor does it require any further consideration of revenue decoupling.

III. CONCLUSION

The OCA submits that the Public Utility Code, the Commission regulations, the Commission Policy Statements and many Commission initiatives already meet the requirements of Section 410(a) of the American Recovery and Reinvestment Act. In the OCA's view, the Commission does not need to make changes or adopt new policies to address the requirements of this new federal statute. Rather, the Commission should continue its efforts, particularly its role in the implementation of Act 129 of 2008, to continue to assure energy efficiency measures are a part of Pennsylvania's energy future.

Respectfully Submitted,


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