



SEE Action
STATE & LOCAL ENERGY EFFICIENCY ACTION NETWORK

Concept Paper for Regulatory Policy Navigation Guide

Purpose of this Paper

Electric and natural gas utilities can play a vital role in deploying all of our nation's available cost-effective energy efficiency. Well-documented barriers exist, however, to aggressive and sustained utility investment in, and support of, energy efficiency programs.¹ The *Regulatory Policy Navigation Guide* (The *Guide*) is a resource for new regulators (or regulators new to energy efficiency) to plot a course through the array of regulatory options available to surmount those barriers. The purpose of this paper is to describe the concept of the *Guide*, and to solicit feedback from potential users (regulators) to inform development of the *Guide*.

When utilities deliver energy efficiency programs², traditional utility business models can conflict with effective program delivery unless three key challenges are addressed:

- **Program Funding.** Effective programs require sustained and predictable funding of direct costs associated with energy efficiency program administration. How will this be accomplished?
- **The Throughput Incentive.** Under traditional rate design, utilities recover fixed costs from volumetric fees. When sales are reduced, utilities may not recover all of their fixed costs. When sales are increased, utilities may over-recover their fixed costs. Motivated by this Throughput Incentive, utilities may face conflict in fully supporting energy efficiency. How can regulation take this into account?
- **The Utility's Bottom Line.** Most utilities are regulated in a traditional way that rewards investment in infrastructure and the sale of electricity. How can the utility's and investors' interests align with customer interests? Can the overall effect of utility regulation similarly reward utilities that engage in successful energy efficiency programs that deliver value for consumers?

The *Guide* will empower a regulator to answer these questions in the manner that works best for their jurisdiction. It will use an interactive, simulated real-world decision-making process involving stakeholders and their interests such that the regulator can explore regulatory choices within the consequence-free environment of an exercise. The *Guide* will include a reading list of recommended resources (papers, docketed materials) to enable users to go as deeply into the subject matter as their interest takes them.

Format of the *Guide*

There are three options for the format of the *Guide*:

Option 1: A group, in-person role-play exercise. The in-person role play exercise is an educational tool similar to The National Association of Regulatory Utility Commissioners (NARUC) Utility Rate School, a mock rate case offering intensive, hands-on learning experience to new regulators. In this format, each participant is assigned a specific role in an energy efficiency regulatory proceeding, such as commissioner, utility, energy efficiency advocate, or consumer advocate. Participants receive confidential instructions and information on their role's perspective, then meet in person to role play and negotiate their interests in a mock regulatory proceeding.

Key Points

- A proposed new resource for utility regulators to plot a course through the array of regulatory options available to surmount barriers to aggressive and sustained utility investment in, and support of, energy efficiency programs.
- Uses an interactive, simulated real-world decision-making process involving stakeholders and their interests.
- There are three options for the format of the *Guide*. Feedback from regulators on the preferred format is requested no later than November 15, 2011 (see contact information on page 2).

About SEE Action

The State and Local Energy Efficiency Action Network (SEE Action) is a state and local effort facilitated by the federal government that helps states, utilities, and other local stakeholders take energy efficiency to scale and achieve all cost-effective energy efficiency by 2020.

About the Working Group

The working group is comprised of representatives from a diverse set of stakeholders; its members are provided at www.seeaction.energy.gov.

Option 2: An online interactive simulation. In this format, the participant engages in an online simulation of decision making in the setting of an energy efficiency regulatory proceeding. Depending on the choices made, real-time feedback is delivered on the resulting impacts of those choices.

Option 3: A written case for independent study or group discussion. In this format, the reader is placed in the shoes of the regulator (the protagonist of the case), who faces difficult decisions in the context of an energy efficiency regulatory proceeding and must understand the perspective of utilities and stakeholders. The reader must evaluate the situation at key points in the story, determine options and the impacts of those options, and make a decision on a course of action.

Topics to Be Covered in the *Guide*⁴

Foundations

- Energy efficiency as a supply and demand resource and integrated resource planning
- Virtues and limitations of traditional regulatory tools in motivating utilities to invest in energy efficiency
- Administrative options for energy efficiency program delivery
- Regulatory choice impacts on the economic efficiency of utilities
- Lessons for regulators on process from state experience to date
- Alternate rate structures

Program Funding

- Expensing, or capitalization and amortization of energy efficiency program costs
- Timing of energy efficiency program cost recovery

The Throughput Incentive

- Frequent rate cases
- Lost revenue adjustment mechanisms
- Straight-fixed variable rate design
- Decoupling

Energy Efficiency as a Utility Business: Aligning Utility and Ratepayer Interests

- Performance target incentives
- Shared savings incentives
- Rate of return adjustment
- Difference between regulatory compliance and all cost-effective energy efficiency

The purpose of this concept paper is to solicit feedback from potential users of the *Guide* on its value, the

proposed format options and curriculum topics. Please provide feedback no later than Nov 15th, 2011 to Johanna Zetterberg at johanna.zetterberg@ee.doe.gov.

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References

¹ See McKinsey & Company, *Unlocking Energy Efficiency in the U.S. Economy*; National Action Plan for Energy Efficiency Report, *Vision for 2025: A Framework for Change*, and *Aligning Utility Incentives with Investment in Energy Efficiency*; Regulatory Assistance Project, *Energy Efficiency Policy Toolkit*; National Economic Research Associates Economic Consulting, *Making a Business of Energy Efficiency: Sustainable Business Models for Utilities*, Prepared for Edison Electric Institute; U.S. Environmental Protection Agency, "Clean Energy Resource Database," <http://cfpub.epa.gov/ceird>.

² By statute or by order of the regulator, another entity may be designated to administer energy efficiency programs. Several states have made this choice. Attention to utility motivation to support energy efficiency remains relevant in the event of non-utility energy efficiency administration.

³ See Harvard Business School, *Developing Negotiation Case Studies*. www.hbs.edu/research/pdf/11-008.pdf.

⁴ These topics are covered in the National Action Plan for Energy Efficiency's *Aligning Utility Incentives with Investment in Energy Efficiency*. www.epa.gov/cleanenergy/documents/suca/incentives.pdf

Disclaimer:

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