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# Decoupling: Frequently Asked Questions

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## **NARUC & Grants & Research**

- NARUC represents PUCs in the States
- G&R Dept. addresses research and facilitates dialogue on key questions facing Commissions
- 17 current projects covering infrastructure, environment, regulatory design, finance, security and other issues for the gas, water, electric, telecom sectors
- Demand-side & Clean Energy plays some role in about 1/2 of our projects

Federal Funders: EPA, Dept. of Energy, Dept. of Homeland Security

Partnerships with FCC, NCS, FERC, private sector, non-governmentals



## Why efficiency?



ENERGY STAR-labelled heat pumps  
and air conditioners use  
**20% less energy**  
than new standard models.



## Efficiency and rates

- More efficiency means we can do more with less electricity
- There are reasons utilities like efficiency:
  - Resource adequacy
  - Load management
  - Deferring the need to build new infrastructure
- ... Why would a utility want you to use more electricity instead of less?



## Because of how they collect revenue

- Mostly they are in the business of selling kilowatt hours / therms, not energy services.
- Current revenue structures give you more money the more you sell
- Who determines how utilities collect revenue?

### PUCs

- PUCs exist so that public-benefit services (like electricity) can stay in business, without taking consumers to the cleaners to pay for something they need.
- They do this by setting cost-of-service rates



## Setting Rates

- Base costs in rates are determined by figuring out the cost of operations using a "model year", and spreading that cost across classes (commercial, industrial, residential) and across customers within classes
- Revenue Requirement equals:
  - Operating expenses, plus
  - Return on investment, plus
  - Return of investment (Depreciation)
- The basic components of operating expenses are:
  - Base costs (power plants, transmission lines, employees) that stay roughly constant between rate cases
  - Variable costs (fuel, purchased power, storm restoration, etc.) that can change unpredictably between rate cases.
- We set the rates by setting a model price:
  - Allocate revenue requirement to each rate class
  - Allocate class revenue requirement to rate components (customer charge, energy and demand)
  - For each rate component:
    - $\text{Revenue Requirement} \div \text{number of customers} = \text{Price}$



## Rate cases and Sales are Divorced

- Rate cases focus on costs to reach revenue requirement, but once the case ends, prices are all that matter
- Variable components are dealt with in part using fuel adjustments or other surcharges. Base costs (mostly fixed) are largely governed in rate cases.
- Anecdotally, utilities are only motivated to come in for new rates in lean times, and avoid rate cases when profits are good.



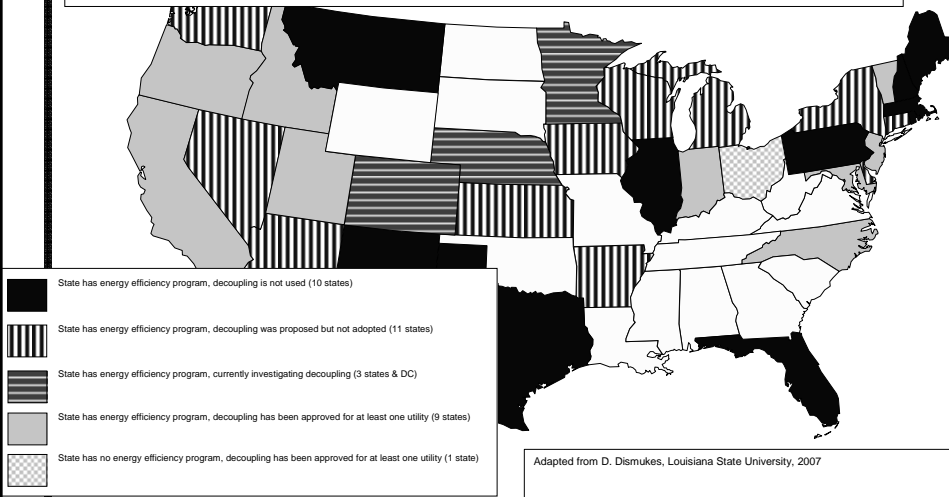
## What is Decoupling?

- Decoupling is an extension of traditional ratemaking
  - It begins with a traditional rate case
  - Sets a target revenue
  - Then periodically adjusts, so...
  - Revenues for each class remain at the target level
- If a company sells more, customers get a rebate
- If they sell less, the rates will be adjusted upwards
- This decreases “regulatory lag”: rates are adjusted annually (or more often)



## Who has tried decoupling?

III. 1: States That Have Considered Electricity or Gas Decoupling



## Decoupling: What It Does and Doesn't Do

### What it does:

- Eliminates incentive to increase profits through increased sales
- Eliminates “losses” from reductions in sales
- Captures effects of all efficiency and DSM activities

### What it doesn't do :

- Create a positive incentive for increased efficiency or demand-side resource
- Address “barriers” to efficiency or DSM
- Change the design of rates



## What It Does and Doesn't Do

- Does it make **bills** go up?
  - Not necessarily. People who use less will see savings, people who use more will see higher bills: just like now.
  - Dilution effect on those who use the same, and potential infrastructure and fuel savings may create reductions.
- Does it make **rates** go up when others save?
  - Not necessarily: small incremental increase
  - For electricity, a growing sector means means more billing units to divide revenue requirement by
- Doesn't the current system work well enough?
  - Some argue no: without changing the way utilities make money, the numbers are just too huge to overcome with incentives alone.



## Approaches to throughput

- Revenue Decoupling
  - Full
  - Per Customer
  - Normalized
- Lost Revenue Recovery or Conservation Adjustments
- Straight-Fixed Variable Rates



## Does decoupling increase efficiency?

- California
- Con Edison
- Idaho
- Versus 3<sup>rd</sup> party provision



## One concern: Risk Transfers

- Between classes
- Business-to-consumer
- Weather
- Fuel-cost
  
- The Maine Example



## Off-ramps and adjustments

- Normalization & “re-coupling”
- Balancing Accounts
- Rate banding
- Shared earnings
- Course corrections



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## Read The FAQ!



[http://www.naruc.org/Publications/NA\\_RUCDecouplingFAQ9\\_07.pdf](http://www.naruc.org/Publications/NA_RUCDecouplingFAQ9_07.pdf)