DECOUPLING

AND

DECOUPLING PILOT PROGRAMS

Report to the Legislature

August, 2013

As required by

Minnesota Statutes §216B.2412

Submitted by the Minnesota Public Utilities Commission

INTRODUCTION

Statutory Reporting Requirement

Minnesota Statutes (2012), Section 216B.2412, subdivision 3 requires the Minnesota Public Utilities Commission to report annually to the Legislature on decoupling and decoupling pilot programs.

This report is intended to fulfill the reporting requirement of this section.

Costs of Preparing Report

Pursuant to Minnesota Statutes (2012), Section 3.197, it is estimated that the costs incurred by the Minnesota Public Utilities Commission in preparing this report is less than $1,000. Special funding was not appropriated for the costs of preparing this report.

BACKGROUND

Minnesota Statutes (2012), Section 216B.2412 is a provision of law regarding the decoupling of energy sales from revenues.

Definition of Decoupling

Subdivision 1 of that section defines decoupling as:

> a regulatory tool designed to separate a utility's revenue from changes in energy sales. The purpose of decoupling is to reduce a utility's disincentive to promote energy efficiency.

In other words, decoupling is intended to minimize or remove financial inhibitions utilities claim limit their investment in cost effective energy efficiency and other clean energy resources located "behind the customer's meter."

Decoupling Programs

Subdivisions 2 and 3 of that section go on to provide the following:

> Subd. 2. Decoupling criteria. The commission shall, by order, establish criteria and standards for decoupling. The commission may establish these criteria and standards in a separate proceeding or in a general rate case or other proceeding in which it approves a pilot program, and shall design the criteria and standards to mitigate the impact on public utilities of the energy savings goals under section 216B.241 without adversely affecting utility ratepayers. In designing the criteria, the commission shall consider energy efficiency, weather, and cost of capital, among other factors.

Subd. 3. Pilot programs. The commission shall allow one or more rate-regulated utilities to participate in a pilot program to assess the merits of a rate-decoupling strategy to promote energy efficiency and conservation. Each pilot program must utilize the criteria and standards established in subdivision 2 and be designed to determine whether a rate-decoupling strategy achieves energy savings. On or before a date established by the commission, the commission shall require electric and gas utilities that intend to implement a decoupling program to file a decoupling pilot plan, which shall be approved or approved as modified by the commission. A pilot program may not exceed three years in length. Any extension beyond three years can only be approved in a general rate case, unless that decoupling program was previously approved as part of a general rate case. The commission shall report on the programs annually to the chairs of the house of representatives and senate committees with primary jurisdiction over energy policy.

COMMISSION ACTIONS

Establishment of Revenue Decoupling Criteria and Standards

As noted, subdivision 2 of Section 216B.2412 requires the Commission to establish criteria and standards for decoupling. In order to reach an informed decision on how best to establish these standards, the Commission contracted with the Regulatory Assistance Project (RAP) to coordinate a stakeholder input process and to prepare a written report detailing decoupling program options. RAP facilitated several meetings with Commissioners, Commission staff, and stakeholders, and issued its final report on June 30, 2008.

Following receipt of the RAP Report, the Commission solicited comments from interested parties on the findings and recommended decoupling criteria and standards in the Report. Ten parties filed comments and reply comments. Parties discussed objectives of decoupling, pilot program implementation and timing, ratepayer impact, customer class inclusion, pilot evaluation criteria, as well as several other issues raised by the RAP Report and the Commission's Notice Seeking Comments.[1]

The Commission met on May 28, 2009 and ordered the establishment of criteria and standards for pilot decoupling programs. The Commission detailed what information should be provided in the initial proposal of a decoupling pilot, how the proposal would be reviewed, and what information, at a minimum, should be provided for the annual evaluation of approved pilots. The Commission also ordered CenterPoint Energy to file additional information explaining how their proposed decoupling pilot satisfied the requirements of the Commission's Criteria and Standards Order.

[1] The Public Utilities Commission provided a copy of the Regulatory Assistance Project Report with its 2009 legislative report. The Report, comments and related documents can be found via eDockets at www.edockets.state.mn.us under "08" – "132".

The Commission's *Order Establishing Criteria and Standards to be Utilized in Pilot Proposals for Revenue Decoupling,* In the Matter of a Commission Investigation Into the Establishment of Criteria and Standards for the Decoupling of Energy Sales from Revenue (June 19, 2009) can be found via eDockets under Docket No. E,G-999/CI-08-132.

CenterPoint Energy's Conservation Enabling Rider, Pilot Decoupling Program

CenterPoint Energy's initial proposal was filed within their 2008 rate case, Docket No. G-008/GR-08-1075, and included a *full* decoupling mechanism.[2] On June 26, 2009 CenterPoint Energy, Energy Cents Coalition, and the Minnesota Center for Environmental Advocacy/Izaak Walton League of America (Stipulating Parties) filed a Stipulation that proposed a *limited* pilot decoupling program (applicable to all small volume firm customers) and an inverted block rate (IBR) structure for gas costs of the Residential and Commercial/Industrial A and B classes.

The Stipulated Agreement modified the initial decoupling proposal by excluding adjustments based on impacts of weather on revenue, instituting a 'cap' on the amount of both upward and downward adjustments, and proposing an inverted block rate for the collection of gas costs for certain classes.

The Commission modified the agreement of the Stipulating Parties to:

1. eliminate the cap on over-collection and require the annual calculation of over-collection and subsequent refund to ratepayers;
2. reduce the cap on under-earning from four to three percent;
3. require the annual decoupling adjustment be displayed as a separate line item on customers' bills;
4. require CenterPoint Energy to provide an evaluation plan in addition to the reporting requirements established in the Criteria and Standards Order;
5. require the joint effort of the Stipulating Parties to provide, within 90 days of the Order, proposals for new/enhanced conservation projects.

Additional issues raised in the proceeding, such as the decoupling pilot's impact on cost of capital and the simultaneous implementation of the pilot and the IBR structure, are discussed in the body of the Commission's January 11, 2010 *Findings of Fact, Conclusions of Law, and Order* In the Matter of an Application by CenterPoint Energy for Authority to Increase Natural Gas Rates in Minnesota (Docket No. G-008/GR-08-1075).[3]

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[2] *Full* decoupling insulates a utility's revenue from deviation of actual sales from expected sales, regardless of the cause of that deviation. *Partial* decoupling operates similarly to full decoupling, except only a portion of the deviation from actual sales is trued up. *Limited* decoupling limits adjustments for sales losses to specific causes of deviation, such as weather or conservation.

[3] The Commission's January 11, 2010 Order and all related documents can be found via eDockets at www.edockets.state.mn.us under "08" – "1075".

The new rates, including the IBR structure, went into effect on July 1, 2010. The first annual decoupling rate appeared on customer bills on March 1, 2011.

The Commission's January 11, 2010 Order, while authorizing CenterPoint Energy to conduct this pilot program, also required the company to file a proposal for evaluating the program. Consideration of this proposed evaluation plan came before the Commission on December 9, 2010.

In the Commission's December 16, 2010 *Order Approving Decoupling Evaluation Plan As Modified* in this matter, the Commission agreed that CenterPoint Energy's evaluation plan offered a workable framework for addressing the questions posed by subdivision 3 of Minn. Stat. § 216B.2412, namely: assessing the merits of the program in promoting energy efficiency and conservation and determining whether the program is achieving energy savings. Consequently, the Commission approved the evaluation plan with several modifications.

On March 1, 2011, CenterPoint Energy submitted its first annual report on its revenue decoupling pilot program. CenterPoint Energy's first annual report covered the first six months of the pilot program (July 1 through December 31, 2010) and is entitled Revenue Decoupling and Inverted Block Rate Evaluation (Evaluation Report). On May 2, 2011, CenterPoint Energy supplemented its Evaluation Report with a filing entitled Inverted Block Rate-Related Gas Price Elasticity Analysis (IBR Analysis).

The Commission solicited comments on CenterPoint Energy's Evaluation Report and IBR Analysis. None of the parties objected to allowing the decoupling pilot to continue. However, the Minnesota Office of the Attorney General – Antitrust and Utilities Division (OAG-AUD) asked the Commission to suspend or terminate CenterPoint Energy's inverted block rate structure and order refunds. The Minnesota Department of Commerce (the Department), the Suburban Rate Authority (SRA), and Community Action Minneapolis (CAM) supported the OAG-AUD's request.

The Izaak Walton League of America (IWLA), the Minnesota Center for Energy Advocacy (MCEA), and the Energy Cents Coalition (ECC) recommended that the inverted block rates should continue , however, these parties acknowledged it might be reasonable to allow certain customers to opt-out from the inverted block rates under certain circumstances (e.g., medical necessity, etc.). (The Department had also recommended certain opt-out provisions if the inverted block rates were allowed to continue.)

CenterPoint Energy argued that the inverted block rates should continue, but asked the Commission to allow a stakeholder group to develop recommendations for modifications and implementation of those modifications.

During the 2011 Legislative Session, Minn. Stat. § 216B.16, subd. 15 was amended[4], effective May 28, 2011, by deleting the following sentence from this subdivision which requires the Commission to consider ability to pay as a factor in setting utility rates and provides the Commission with authority, if it so chooses, to establish affordability programs for low-income

[4] Laws of Minnesota 2011, Chapter 97, Section 11

residential ratepayers in order to ensure affordable and reliable service to low-income residential utility customers:

> Affordability programs may include inverted block rates in which energy prices are made available to lower usage customers.

On September 16, 2011, subsequent to making their initial recommendations, CenterPoint Energy, ECC, IWLA, and MCEA submitted a joint proposal asking permission for CenterPoint Energy to suspend the inverted block rate structure. CenterPoint Energy, ECC, IWLA, and MCEA proposed forming a workgroup that would make recommendations to the Commission no later than March 1, 2012 for modifying the inverted block rate structure. The Department supported the proposal to suspend CenterPoint Energy's inverted block rates. The OAG-AUD, SRA, and CAM also recommended the Commission suspend the inverted block rates.

The Commission met on September 28, 2011 and ordered CenterPoint Energy to:

- suspend its inverted block rate structure;
- file a proposal for making refunds to compensate consumers for the cost of elongated, inverted block rate billing periods; and
- revise the decoupling rate adjustments implemented on customer bills on March 1, 2011.

The Commission also authorized CenterPoint Energy to lead a stakeholder workgroup to explore the feasibility of revising and reinstating the inverted block rate structure.

The Commission's *Order Suspending Inverted Block Rate Structure, Authorizing Workgroup, And Requiring Revised Decoupling Rate Adjustment* was issued on October 4, 2011 and the Commission's *Order Requiring Bill Adjustment Proposal* was issued on November 8, 2011.

On December 7, 2011, CenterPoint Energy submitted its Proposal for Bill Adjustments to Address Impact of Inverted Block Gas Cost Recovery in 2010 and 2011 (Bill Adjustment Proposal). The Commission solicited comments on CenterPoint Energy's Bill Adjustment Proposal. The Department and the OAG-AUD agreed in many respects with CenterPoint Energy's proposal for determining eligibility for the proposed adjustments, calculating the adjustments, and accounting for the adjustments. However, there were two issues in dispute: (1) the OAG-AUD's objection to CenterPoint Energy's request that ratepayers pay for the bill adjustments, and (2) the number of days that would define an overly long billing period (CenterPoint Energy recommended a billing period longer than 35 days, the OAG-AUD recommended a billing period longer than 32 days, and the Department recommended a billing period longer than 30 days).

The Commission met on February 23, 2012 and ordered CenterPoint Energy to implement its bill adjustment proposal with ratepayers being held responsible for paying for the adjustments. The Commission also:

- directed CenterPoint Energy to reimburse customers who paid more than they otherwise would have due to CenterPoint Energy's use of elongated billing periods while implementing its inverted block rate structure;
- authorized CenterPoint Energy to recover the cost of these reimbursements in generally the same manner as it recovers other gas costs, and specifically, in the same manner as it handles the annual inverted block gas cost true-up adjustment, i.e., on a class-by-class basis; and
- established criteria for identifying customers who qualify for reimbursement and for calculating the amount of the reimbursement.[5]

The Commission's *Order Approving Bill Adjustment Plan For Inverted Block Rate Pilot Program* was issued on April 3, 2012.

On March 1, 2012, CenterPoint Energy submitted its second annual report on its revenue decoupling pilot program. CenterPoint Energy's second annual report covers twelve months of the pilot program (January 1 through December 31, 2011) and is entitled Revenue Decoupling and Inverted Block Rate Evaluation. CenterPoint Energy also submitted its IBR Modification Workgroup Report.

The Commission met on July 19, 2012 and accepted CenterPoint Energy's second annual revenue decoupling report and the IBR Modification Workgroup's report. Because there was no consensus on how to address the unintended consequences of the IBR structure, the Commission ordered CenterPoint Energy to terminate the IBR structure. The Commission explained its decision to terminate CenterPoint Energy's IBR structure in its August 10, 2012 *Order Terminating Inverted Block Rate Structure, Accepting Evaluation And Workgroup Reports, And Requiring Compliance Filings* as follows:

> CenterPoint's inverted block rate design unexpectedly resulted in significantly increased bills for certain customers. Among the customers adversely effected (sic) were low-income customers in poorly-insulated homes, and renters in multi-unit buildings with only one gas meter. Other customers received higher than expected bills because their meters were not read punctually and their natural gas use during the extended billing period lifted them in to a higher gas-price block.
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> The unintended effects of the inverted block rate design on certain customers and the larger bills that were the result of elongated and uneven billing periods were contrary to the public interest. There does not appear to be a way to modify the inverted block rate

[5] For example: (1) Bill adjustments and refunds to former customers shall only be made for customers who received one or more bills for a billing period longer than 32 days, and shall be calculated for each eligible bill based, in part, on an estimate of the amount of gas used during the "elongated" part of the billing period by multiplying the estimate of the customer's average daily gas consumption by the number of days in the billing period in excess of 32 days; (2) Bills eligible for adjustment are those elongated bills received by customers in any month during which the IBR pilot was in effect (i.e., the billing date occurred and the bill was rendered between July 1, 2010 and October 12, 2011); and (3) Refunds to former customers are required but only if the customer is owed more than $2.00.

structure that would be worth the cost to administer, would not result in even greater customer confusion, and would still deliver the intended benefits in a measurable way. Accordingly, this inverted block rate implementation cannot be reinstated.

CenterPoint Energy's third revenue decoupling rate adjustment appeared on customer bills on March 1, 2013. On the same date, CenterPoint Energy filed its third annual revenue decoupling evaluation report.

CenterPoint Energy's revenue decoupling pilot program ended on June 30, 2013. CenterPoint Energy has stated that it anticipates filing a new decoupling program as part of its rate case to be filed in August of 2013.

The Commission met on June 6, 2013 to consider CenterPoint Energy's annual revenue decoupling evaluation report for 2012 and the company's March 1, 2013 revenue decoupling rate adjustments. At that meeting, the Commission, as set forth in its July 26, 2013 correspondence to the company, accepted the company's revenue decoupling evaluation report for 2012 and approved the company's March 1, 2013 revenue decoupling rate adjustments. In addition, the Commission directed CenterPoint Energy to continue efforts to target communication expenditures to optimize the potential for low-income customers to maximize their conservation savings and participation in conservation and other programs specifically designed for low-income customers.

Minnesota Energy Resources Corporation Decoupling Proposal

On November 30, 2010, Minnesota Energy Resources Corporation (MERC) on behalf of its two operating divisions MERC-PNG and MERC-NMU, filed a request for a general increase in its natural gas rates.[6]

A revenue decoupling proposal was included in MERC's filing that, if approved, would separate the amount of distribution revenue MERC collects from its customers from the volume of gas MERC sells to its customers. The intent is to remove the financial disincentive to promote energy efficiency and to allow MERC to recover its approved revenue requirement.

MERC's proposal is for a full decoupling pilot program, as opposed to the limited decoupling mechanism approved in the CenterPoint Energy's pilot program.

Because MERC's request for a decoupling mechanism was filed within its 2010 rate case, MERC's proposal with its request for a rate increase was referred to the Minnesota Office of Administrative Hearings (OAH) for a contested case hearing. The Minnesota Department of Commerce-Division of Energy Resources (the Department); the Minnesota Office of the Attorney General-Antitrust and Utilities Division (OAG-AUD); Super Large Gas Intervenors

[6] In the Matter of the Application of Minnesota Energy Resources Corporation for Authority to Increase Rates for Natural Gas Service in Minnesota, Docket Number G-007,011/GR-10-977.

(SLGI)[7]; and the Izaak Walton League of America-Midwest Office and the Minnesota Center for Energy Advocacy (IWLA/MCEA) intervened in this matter. All of the parties except SLGI submitted testimony on MERC's revenue decoupling proposal.

In the parties post-hearing filings, the status of MERC's revenue decoupling request was described as follows:

> MERC proposed a full decoupling mechanism. The revenue decoupling mechanism (RDM) adjustments would be determined separately for two different rate groups and would be applicable to all customers served under these rate classes: [a] General Service-Residential, and [b] General Service-Small Commercial and Industrial. MERC proposed to submit an evaluation plan to the Commission annually. MERC proposed to calculate the RDM adjustments for three calendar years plus any partial calendar year that the RDM becomes effective. MERC proposed to exclude the CCRC [conservation cost recovery charge] and CCRA [conservation cost recovery adjustment] revenues from the RDM calculations. MERC did not propose a cap for its primary decoupling proposal.
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> The Department recommended that MERC commit to an evaluation plan similar to the one approved for CenterPoint Energy, and that MERC impose a 10% cap on the amount of revenues MERC collects through its RDM[8]. The Department also recommended monthly, not annual, RDM adjustments, and that MERC should calculate the RDM adjustment factors based on actual 2011 customer counts and distribution revenues. The Department also recommended clarification that the Commission may modify the rates in the pilot if warranted by unexpected circumstances. MERC agreed with the Department's recommendations, with the exception of using monthly RDM adjustments. In Surrebuttal testimony, the Department agreed that annual computation of the RDM adjustments was also appropriate.[9]

In its filings in this matter, the OAG-AUD opposed all decoupling rate designs. The OAG-AUD was particularly opposed to MERC's requests for full revenue decoupling, which would compensate MERC for variations in sales due to weather and other extraneous factors unrelated to energy efficiency.

However, the OAG-AUD recommended that if the Commission were to approve MERC's request, that MERC's proposal be modified to:

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[7] The Super Large Gas Intervenors (SLGI) consist of the following members: (1) Hibbing Taconite Company located in Hibbing, Minnesota; (2) ArcelorMittal USA's Minorca Mine located near Virginia, Minnesota; (3) Northshore Mining Company located in Silver Bay, Minnesota; (4) United Taconite, LLC located in Eveleth and Forbes, Minnesota; (5) the Minntac and Keewatin Mines of United States Steel Corporation located in Mountain Iron and Keewatin, Minnesota, respectively; and (6) USG Interiors, Inc.

[8] The 10% revenue adjustment cap would be based on the non-gas margin after removing the CCRC.

[9] MERC, Description and Summary of Issues and Positions, November 23, 2011, Docket No. G-007,011/GR-10-977, pg. 18.

- require measurable, incremental energy savings or decreased energy beyond that which is already required and in addition to that which is already expected;
- reduce MERC's authorized rate of return on common equity capital by at least 16.73 basis points;
- apply to all customer classes; and
- include an evaluation and reporting plan similar to the evaluation plan required of CenterPoint Energy.

IWLA and MCEA supported MERC's request for a full revenue decoupling pilot program but only if the Commission also required MERC to demonstrate annual incremental progress toward achieving the annual 1.5 percent energy savings goal established by Minnesota law.

The Super Large Gas Intervenors (SLGI) opposed the OAG-AUD's suggestion that all customers, and in particular, large industrial customers that are members of the SLGI group, participate in MERC's RDM.

In his report and recommendation, the ALJ found that MERC's revenue decoupling mechanism and proposed pilot program met the requirements of Minnesota law and previous Commission orders on decoupling, and was based on sound ratemaking principles. The ALJ concluded that the RDM should be computed annually, applied to the Residential and Small C&I rate groups, contain a symmetrical ten percent cap on RDM revenues, and run for three full calendar years. The ALJ also recommended that the Commission require MERC to submit an annual evaluation plan similar to the one used in CenterPoint Energy's decoupling pilot, and to file annual reports to the Commission that specify the RDM adjustment to be applied to each rate class for the billing period demonstrating annual progress toward achieving the 1.5% energy efficiency goal set in Minn. Stat. § 216B.241.

On May 24, 2012, the Commission met and authorized MERC to implement its proposal for a full revenue decoupling pilot program, as recommended by the ALJ, with certain modifications and conditions. In its decision, the Commission required MERC to: (1) use the same billing determinants (customer counts, etc.) used to set final rates to determine the RDM baseline; (2) use its initial sales forecast, corrected only as needed to resolve any errors discovered in the Vertex billing audit in favor of ratepayers, for decoupling purposes; and (3) explain its revenue decoupling program in its notice to customers about final rates at the end of this case and in another notice when the first annual revenue decoupling rate adjustment is implemented on customer bills. The Commission provided a detailed explanation of its decision on pages 7-15 of its *Findings of Fact, Conclusions, And Order* (July 13, 2012) in this docket.

MERC's revenue decoupling pilot program began January 1, 2013 with the implementation of final rates in the 2010 rate case. MERC's first revenue decoupling rate adjustment will appear on customer bills on March 1, 2014 at the same time MERC files its first annual revenue decoupling evaluation report.

Other Commission Actions on Energy Conservation

Minnesota Statutes (2012), Section 216B.241, subdivision 2c states:

> Performance incentives. By December 31, 2008, the commission shall review any incentive plan for energy conservation improvement it has approved under section 216B.16, subdivision 6c, and adjust the utility performance incentives to recognize making progress toward and meeting the energy savings goals established in subdivision 1c.

The Commission's December 29, 2008 *Order Establishing Procedural Framework for Consideration of Utility Performance Incentives for Energy Conservation*[10], established procedures for the evaluation of whether and, if so, what changes to the current incentive were needed. The Commission also asked for a workgroup to define incentive models and implementation options.

Following a year of collaboration between utilities, the Minnesota Department of Commerce (the Department), and other interested stakeholders, the Commission issued its January 27, 2010 *Order Establishing Utility Performance Incentives for Energy Conservation*[11]. In this Order, the Commission approved a new shared savings demand-side management (DSM) financial incentive for all investor-owned utilities in Minnesota effective with energy savings achievements in 2010. The new incentive was approved for the period of the utility's triennial CIP filing. The January 27, 2010 Order incorporated several elements detailing the mechanics of the new Shared Savings Model including a cap on the potential incentive award and the calibration of the incentive for specific utilities. (This Order also addressed how the incentive should be adjusted for a utility with an approved decoupling pilot.)

On December 30, 2011, the Department filed an interim report on the impact of the new shared savings incentive in the new Shared Savings Model on both utility achievements and incentive rewards for 2010. On July 9, 2012, the Department issued its final report for 2011.

In addition to the Department, Interstate Power and Light, Minnesota Power, Otter Tail Power, Xcel Energy, CenterPoint Energy, Great Plains Natural Gas Company, Minnesota Energy Resources Corporation, the Minnesota Chamber of Commerce, and the Office of the Attorney General-Antitrust and Utilities Division all filed comments and participated in this proceeding.

The Commission met on February 2 and November 8, 2012, and ordered all natural gas and electric utilities to remove the non-linear adjustment from the shared savings DSM financial incentive effective with the energy savings achievements in 2012.

The Commission's March 30, 2012 *Order Removing Non-Linear Adjustment From the Shared Savings DSM Financial Incentive* and the December 20, 2012 *Order Adopting Modifications to Shared Savings Demand Side Management Financial Incentive* and all related documents can be found via eDockets under "08" – "133".

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[10] In the Matter of Commission Review of Utility Performance Incentives for Energy Conservation Pursuant to Minn. Stat. § 216B.241, Subd. 2; Docket No. E,G-999/CI-08-133.
[11] Ibid.