Legislative Analysis

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ENERGY EFFICIENT MICHIGAN ACT

House Bill 5525
Sponsor: Rep. Kathy Angerer
Committee: Energy and Technology

Complete to 2-5-08

A REVISED SUMMARY OF HOUSE BILL 5525 AS INTRODUCED 12-4-07

The bill would create the "Energy Efficient Michigan Act" to do the following:

- Define key terms. (See detailed summary below).
- Require a natural gas or electric utility, as defined in the bill, to submit an "energy efficiency programs plan" with the Public Service Commission (PSC) for its approval within 90 days of the bill's effective date and every two years thereafter.
- The bill would establish deadlines for the PSC's initial review of a plan and for the resubmission and subsequent review of a rejected plan. A utility would have to revise and resubmit its plan until it was approved, and meet performance standards even if its plan is rejected.
- Set forth requirements for each plan. (Plans would have to include: 1) programs for each customer class (but efforts for each class would not have to be proportionate); (2) a specification of necessary funding; (3) adequate programs and funding levels; (4) cost-effectiveness; (5) a designation of each program's administrator (which could be a utility, one or more utilities acting jointly, a state agency, or a nonprofit organization); and (6) independent expert verification of the expected energy savings from each program.)
- Establish separate performance standards for electric and gas utilities beginning with a two-year initial period (2008-2009) and increasing annually thereafter. (A performance standard would be the expected energy efficiency savings from programs expressed as a percentage reduction of the utility's total sales in the preceding year. The required savings would be somewhat higher for electric utilities than for natural gas utilities. Efficiency savings exceeding the applicable performance standard could be carried forward and used to satisfy up to one third of the next year's standard, but a utility electing the carry forward credit could not also apply for the financial incentive described below.)
- Allow a utility to recover the cost of its efficiency programs in its rates, to adopt a rate decoupling mechanism, and to recover an additional financial incentive of up to 15 percent of the cost of its programs if it met or exceeded the applicable performance standard.
- Allow a utility to opt out of Sections 5, 7, and 9 of the act by making specified payments to an independent program administrator selected by the PSC, and allow the utility to pass along the costs of these payments in its rates. (The

independent administrator would implement efficiency programs for a utility making this choice.)

- Allow the PSC to investigate violations of the act and sanction a utility that does not make a good faith effort to comply with the act.
- Require a utility that falls short of its performance standard to make up the shortfall in the subsequent two years in addition to the savings otherwise required during those years.
- Require municipally-owned utilities to submit plans to the PSC for its review and recommendations (but not approval).
- Require municipally-owned utilities to comply with performance standards.
- Authorize suits against a municipally-owned utility by persons adversely affected by the utility's failure to meet performance standards.
- Authorize awards of attorney fees and expert witness fees to the substantially prevailing party in such a suit--whether it is the plaintiff or the utility.
- Require municipally-owned utilities to report to its customers, the governing body of the municipality and the PSC on its efficiency efforts.
- Allow large customers (those with electricity demand of more than one megawatt) to submit efficiency projects to the PSC and the relevant utility (the one that who would lose sales as a result of the project). The PSC would approve the project if it provided new electricity or natural gas savings and had a payback period between one and eight years. Expected savings from an approved large customer project could be used to satisfy the utility's performance standard and the large customer could apply its expenditures to satisfy up to 90 percent of the surcharges on its bills relating to the utility's efficiency programs.
- Require the PSC to promote load management.
- Require the PSC to report to the Legislature on implementation of the act.

<u>Tie bars</u>. House Bill 5525 is tie-barred to the following bills, meaning that unless all are enacted, the bill will not take effect:

House Bill 5520 (Miller) (Limited or no PSC review of utility generation asset sales)
House Bill 5521 (Gaffney) (PSC certifications, including certificates of need)
House Bill 5522 (LaJoy) ("rate deskewing")
House Bill 5523 (Clemente) (rate increases effective unless PSC approves in 90 days)
House Bill 5524 (Accavitti) (modify choice program)
House Bill 5548 (Mayes) (renewable portfolio standards)
House Bill 5549 (Palsrok) (renewable portfolio standards)
House Bill 5383 (Brown) (allow electricity co-ops to set rates without PSC approval)
House Bill 5384 (Nofs) (loosen restrictions on municipal utility joint action agencies)

DETAILED SUMMARY [Note: Because the bill would create a new act, it contains only odd-numbered sections to leave room for new sections to be added in the future.]

Section 1

<u>Title</u>. The bill would create the "Energy Efficient Michigan Act."

Section 3

Definitions. Terms defined in the bill include:

"Cost-effective" would mean that the program being evaluated meets the "utility system resource cost test."

"Electric utility" would mean a person or entity whose transmission or distribution of electricity is regulated by the PSC. The term would *not* include a municipally-owned utility, an affiliated transmission company, or an independent transmission company.

"Energy efficiency" would mean "a decrease in the consumption of electricity or natural gas achieved through measures or programs that target customer behavior, equipment, or devices without reducing the amount or quality of energy services." Energy efficiency would *not* include "load management."

"Large customer" would mean "a utility customer at a single, contiguous field, location, or facility, regardless of the number of meters at that field, location, or facility, with an electric billing demand greater than 1-megawatt."

"Load management" would mean "measures or programs that decrease peak electricity demand or shift demand from peak to off-peak periods."

"Natural gas utility" would mean "an investor-owned business engaged in the sale and distribution of natural gas within [Michigan] whose rates are regulated by the [PSC]."

"Utility" would mean an electric utility or natural gas utility, except as used in Section 15 [concerning municipal utilities].

"Utility system resource cost test" would mean "a standard that is met if, for an investment in energy efficiency, on a life-cycle basis the total avoided supply-side costs, including representative values for electricity and/or natural gas supply, transmission, distribution, and other associated costs, are greater than the total costs to the utility of administering and delivering the energy efficiency programs, including any costs for incentives paid to customers."

Section 5

Submission of energy efficiency programs plans. Natural gas and electric utilities would have to file an "energy efficiency programs plan" with the PSC within 60 days after the bill's effective date, and every two years thereafter.

Plan requirements. Each plan would have to:

- Offer programs for all customer classes, although the utility would not be required to devote equal effort to each customer class.

- Specify necessary funding levels.
- Demonstrate that the proposed energy efficiency programs and funding are sufficient to achieve the performance standards under Section 7.
- Demonstrate that the programs, viewed collectively, will be cost-effective.
- Include a plan for the "practical and effective" administration of the programs. A program could be administered by the utility (alone or jointly with other utilities), by a state agency, or by an "appropriate experienced nonprofit organization" selected through competitive bidding.
- Provide for independent expert evaluation of the actual energy efficiency programs to verify the incremental energy savings from each program, subject to public review and commission oversight.

PSC review of plans. Within 120 days of receiving a plan, the Commission would have to approve or reject it. If it rejects a plan, the PSC would have to explain why it did so. The utility would have 30 days to revise and resubmit its plan, and the Commission would have to review a revised plan within 30 days. A utility would have to keep revising and resubmitting its plan until it was approved. Performance standards, described below, would still apply to a utility even if its plan is rejected.

Section 7

Electric utility performance standards. An electric utility's energy efficiency programs would have to collectively meet the following minimum performance standards:

- Biennial incremental savings in 2008-2009 equal to 0.3 percent of 2007's total annual electricity sales in kilowatt hours.
- Annual incremental savings in 2010 equal to 0.5 percent of 2009's total.
- Annual incremental savings in 2011 equal to 0.75 percent of 2010's total.
- Annual incremental savings in 2012 (and each year thereafter) equal to 1.0 percent of the preceding year's total.

Gas utility performance standards. A natural gas utility's energy efficiency programs would have to meet the following minimum performance standards [the term "collectively" is not used here]:

- Biennial incremental savings in 2008-2009 equal to 0.1 percent of 2007's total annual gas sales in therms.
- Annual incremental savings in 2010 equal to 0.25 percent of 2009's total.
- Annual incremental savings in 2011 equal to 0.5 percent of 2010's total.
- Annual incremental savings in 2012 (and each year thereafter) equal to .75 percent of the preceding year's total.

Carry forward credits. An electric or gas utility could carry forward incremental savings that exceed the applicable standard to satisfy up to one third of the next year's standard. If the utility accepts the financial incentive described below, it could not also take a carry forward credit from the same period.

Determination of incremental savings. Incremental savings for an electric or a natural gas utility would be the energy savings expected to be achieved during a one-year period by the efficiency measures installed under any of the programs in the utility's plan. An independent expert evaluator would determine the amount of the amount of energy savings achieved or expected to be achieved in a program.

Section 9

Efficiency program cost recovery. A utility would be able to recover the actual, reasonable costs of implementing a PSC-approved program through a tariff rider or other appropriate volumetric charge applied to distribution company rates. To the extent feasible, charges collected from each customer sector would be devoted to energy efficiency programs and services for that sector. All distribution customers would pay the cost recovery charge regardless of the source of their electricity or gas.

Revenue decoupling true-up mechanism. [Note: In general, for-profit utilities maximize revenues by selling as much energy as possible. Revenue decoupling, generally speaking, is a ratemaking approach that decouples revenues from sales to some degree so that a utility is more likely to cooperate with efficiency or conservation programs designed to reduce consumption.]

The bill would allow a utility that annually spends at least 0.5 percent of its total revenues--including electricity or natural gas commodity costs--on approved efficiency programs per year could adopt a "symmetrical revenue decoupling true-up mechanism that adjusts for sales volumes that are above or below forecasted levels." Expenditures exceeding two percent of total revenues would require PSC approval.

Financial incentive for meeting or exceeding standards. If utility meets or exceeds its performance standard--and this has been documented through a commission-approved program evaluation--the PSC could allow a "financial incentive" of up to 15 percent of the utility's actual energy efficiency expenditures for that year to the costs it recovers, upon application and after a hearing.

Section 11

Independent administration option. A utility company could opt out of complying with the previously-described sections of the bill (Sections 5, 7, and 9) by paying a specified percentage of its revenues to an independent energy efficiency program administrator selected by the PSC:

- In 2009, 0.75 percent of total utility sales revenues for 2007.
- In 2010, 1.0 percent of total utility sales revenues for 2008.
- In 2011, 1.5 percent of total utility sales revenues for 2009.
- In 2012 and each year thereafter, 2 percent of total utility sales revenues for the preceding year.

Use of funds and carry forward of unspent funds. The energy efficiency program administrator would use the funds it receives to administer energy efficiency programs for the utility. Funds unspent in any given year would be carried forward to be spent in the subsequent year. [It is unclear whether utility could subtract funds carried forward from the amount otherwise required to be paid to the administrator the following year.]

Cost recovery of payments to an independent administrator. A utility would be able to recover the amount of money transferred to an independent administrator through a tariff rider or other appropriate volumetric charge applied to distribution company rates. All distribution customers would pay the cost recovery charge regardless of the source of their electricity or natural gas.

Selection of administrator. The PSC would select a qualified nonprofit organization through competitive bidding to administer energy efficiency programs for utilities that choose to make payments to an independent administrator rather than comply with Sections 5, 7, and 9.

Section 13

Compliance. The PSC would monitor utility performance to ensure compliance with the requirements of the act. If a utility violated the act, the PSC would investigate the reasons for the violation. If due to a lack of good faith effort, the PSC would have to implement regulatory sanctions, such as a reduction in the utility's authorized rate of return.

If a utility failed to meet a performance standard in any particular year, the utility would have to make up the shortfall over the next two years (in addition to the required efficiency performance standards during those years).

Section 15

Municipal utilities. A municipally-owned utility would have to comply with Section 5(1) which requires the submission of an energy efficiency programs plan meeting specified requirements. The Commission could recommend changes to the municipal utility's plan. [Unlike other utilities, however, it would appear that a municipally-owned utility would not need PSC approval for its plan, nor would it necessarily have to adopt PSC-recommended changes to its plan.] The performance standards set forth in Section 7 are applicable to municipal utilities and, if not met, the municipal utility would have to make up the shortfall over the next two years under Section 13(3), as would be required of other utilities.

Compliance. Any person adversely affected by a municipally-owned utility's failure to meet its performance standards under Section 7 or to make up a shortfall under Section 13(3) could bring an action in a state circuit court for injunctive relief after providing at least 60 days' notice to the municipal utility and the PSC of intent to sue, the basis for the suit, and the relief sought. A court could award a substantially prevailing party its costs of litigation, including reasonable attorney and expert witness fees. In other words, an individual bringing an unsuccessful suit against a municipal utility could be ordered to pay a municipally-owned utility's attorney and expert witness fees.

Reporting. Within one year after the bill's effective date, and every two years thereafter, a municipally-owned utility would have to report to its customers, the PSC, and the governing body of the municipality (1) its expenditures on energy efficiency programs during the previous calendar year, (2) details of each program, and (3) the overall effectiveness of each program. [Although after the first year of the act, these reports would cover two-year periods, the bill would technically only require a report on the utility's expenditures in the previous year, not the previous two years.]

Section 17

Large customer efficiency projects. A large customer--one with an electric billing demand greater than one megawatt--could propose an energy efficiency project to the PSC and the relevant utility, along with supporting documentation, describing expenditures and expected energy savings (in megawatts, megawatt hours, or decatherms). The PSC would have to approve the project if it would provide new electricity or natural gas savings with a simple payback period between one and eight years (calculated as project costs divided by annual energy cost savings). When the project was complete, the large customer would submit verification of the installation, its expenditures, and expected energy savings to the PSC and the relevant utility.

A utility could count the large utility's expected savings toward its performance standards. A large customer could use its verified project expenditures to offset up to 90 percent of the charges that it would otherwise incur under the utility's efficiency programs under Section 9 or 11 in the year the project was completed.

Section 19

Load management. The Commission would have to promote load management in appropriate circumstances, including allowing rate recovery for prudent load management expenditures. "Load management" would mean "measures or programs that decrease peak electricity demand or shift demand from peak to off-peak periods."

Section 21

PSC report. Within one year after the bill's effective date, and every two years thereafter, the PSC would have to report to the Legislature about the implementation of efficiency programs under the bill. The PSC would make copies of the report available to the public and the Department of Labor and Economic Growth would have to post the report on its website.

FISCAL IMPACT:

House Bills 5520-5525 are expected to be tie-barred to other pending bills in both Chambers, so this analysis is preliminary. This group of six bills is expected to require the addition of 25 to 30 staff to the Michigan Public Service Commission to administer the new programs and standards and the resulting caseload. The cost of this additional staff is estimated to be $1.5 million to $1.8 million, assuming that this many staff can be added to the existing MPSC office space.

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