

DE 10-188
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Panel 1
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STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

DE 10-188
2010 CORE Electric Energy Efficiency Programs
and
Natural Gas Energy Efficiency Programs

REBUTTAL TESTIMONY
OF
JAMES J. CUNNINGHAM, JR. AND AL-AZAD IQBAL

Date: November 15, 2010

1 **Q. Please state your names, current positions and business address.**

2 A. Our names are James J. Cunningham, Jr. and Al-Azad Iqbal and we are employed
3 by the New Hampshire Public Utilities Commission (Commission) as Utility
4 Analysts. Our business address is 21 S. Fruit Street, Suite 10, Concord New
5 Hampshire, 03301.

6 **Q. Please summarize your educational and professional background.**

7 A. Our educational and professional backgrounds are summarized in Appendix A of
8 our direct testimony.

9 **Q. What is the purpose of your rebuttal testimony?**

10 A. Our rebuttal testimony examines OCA's support for the utilities' proposed change
11 to the existing Commission-approved formula for calculating performance
12 incentives (PI).¹

13 **Q. Please summarize the proposed change that OCA supports.**

14 A. OCA supports the proposed change to substitute *actual* utility expenses in lieu of
15 *budgeted* utility expenses in the calculation of PI.

16 **Q. Why does the OCA support the utilities' proposed change in the calculation
17 of PI?**

18 A. The OCA notes that, by substituting actual utility expenses in lieu of budget
19 utility expenses for program years 2007-2009, the six utilities would have earned
20 a smaller PI (p. 9). Further, the OCA supports the change because it removes the

¹ Direct Prefiled Testimony of Mr. Stephen R. Eckberg, dated October 15, 2010, pages 7-11.

1 possibility that a utility could earn an incentive on the same dollar more than
2 once.²

3 **Q. Did you address this issue in your testimony?**

4 A. Yes. We addressed this issue in our direct testimony.³ We recommended no
5 change from the existing formula because the change was premature. We noted
6 that a working group was established earlier in 2010 to review the PI formula and
7 that the group met twice and will continue to meet until all relevant issues are
8 fully explored.⁴ No final recommendation was developed by the working group.
9 Staff believes that the PI amounts are significant⁵ and that the interaction of utility
10 spending and kWh/MMBtu savings needs to be better understood in order to
11 ensure that performance incentives are appropriate and consistent with the
12 Commission's goal of achieving extraordinary savings.⁶
13 Our primary concern is to ensure that the existing budget-based performance
14 metric stays in place – i.e. delivering lifetime kWh and MMBtu savings at or
15 below budget. Elimination of this budget metric could set the stage for increased
16 utility spending. We note that, for the past two years, the electric companies have

² OCA notes that, if unspent budgeted utility expenses are carried forward and included in the subsequent year's budget, the utility could earn a second incentive on those carried forward amounts – i.e. once in the budget for the first year and again in the budget for the second year (ref. testimony of Mr. Eckberg at page 9).

³ Direct Testimony of James J. Cunningham and Al-Azad Iqbal dated October 15, 2010, page 3 and pages 28-31.

⁴ As part of its effort on the PI Working Group, Staff is researching PI practices in other states.

⁵ In 2009, PI amounts were in excess of \$2.0 million (ref. Testimony of Cunningham and Al-Azad Iqbal at page 30).

⁶ Source: Commission Order No. 20,457 which states: "They (incentive payments) are provided only when extraordinary savings are actually achieved."

1 under spent their respective budgets.⁷ We believe this under spending is based, at
2 least in part, on the existing Commission-approved budget performance metric.

3 **Q. Please explain how the elimination of the existing budget-based performance**
4 **metric could set the stage for increased utility spending?**

5 A. Changing the formula from budget-based utility spending to actual-based utility
6 spending could lead to overspending that would be beneficial for the utility since
7 it would earn higher PI amounts.⁸

8 **Q. How could the change to an actual-based PI formula encourage the utilities**
9 **to increase spending, given the relatively fixed level of SBC funding? If the**
10 **SBC doesn't increase, how could the utilities increase spending?**

11 A. Under SB300, the cap on the SBC was removed. Therefore, the utilities could
12 propose that the Commission increase the SBC in year two to recover the over
13 spending incurred in year one.

14 **Q. Please explain more fully how the change to an actual-based PI formula will**
15 **encourage overspending?**

16 A. Below we illustrate how the actual-based PI model could encourage
17 overspending. Under this scenario, we begin by noting that the PI calculation has
18 two components – Savings, and the benefit/cost (B/C) component. Both parts
19 compare budgeted to actual values and determine the performance percentage
20 based on a sliding scale. Each component has a weight of 4 percent. So, under

⁷ Direct Testimony of James J. Cunningham and Al-Azad Iqbal, page 8. In 2008, the electric companies' actual utility expenditures were \$17.7 million, as compared to the budgeted amount of \$18.9 million, a 6 percent reduction from budget. In 2009, the electric companies' actual utility expenditures were \$17.3 million, as compared to the budgeted amount of \$18.2 million, a 5 percent reduction from budget.

⁸ Although there is still a 12 percent cap in place, but the absolute dollar amount of PI could increase if spending increased.

1 the existing budget-based PI formula, if utilities achieve baseline performance
2 (*i.e.* proposed or budgeted) performance on both components (*i.e.* savings
3 component and B/C component), they will calculate an 8 percent PI. If the
4 utilities out-perform their baseline budgeted goal, they could earn up to 12 percent
5 PI. There is no cap on either component of the PI as long as the combined
6 incentive for any sector (*i.e.* Residential or C&I) does not exceed 12 percent of
7 that sector's planned budget. Since each component has no cap, if a utility is
8 getting 12 percent for PI, the contribution of each component could vary. For
9 example, let's assume:

10	Budget	\$100
11	Savings	1,000
12	B/C ratio	1

13 If actual savings is 1,000kWh and B/C ratio is 1, under the existing budget-based
14 PI, the utilities will calculate 8 percent (*i.e.* 4 percent for savings component and 4
15 percent for B/C component). With respect to achieving a higher PI, there are
16 three ways the utilities can get a possible 12 percent PI:

- 17 • Achieve double performance for the savings component and nominal
18 performance for the B/C component (*i.e.* 4% x 2 for the savings
19 component, or 8%; plus, 4% percent for the B/C, or 4%; for a total of
20 12%).
- 21 • Achieve nominal performance for the savings component and double
22 performance for the B/C component (*i.e.* 4% for the savings component,

1 or 4%; plus 4% x 2 for the B/C component, or 8%; for a total of 12%
2 percent).

- 3 • Achieve some combination of higher savings and B/C ratio.

4 Under the proposed actual-based PI formula, the simplest way to get higher
5 savings is to increase spending with the same B/C ratio. For instance, if the
6 utilities spend \$200, and save 2,000 kWh, and B/C ratio is 1, the PI would be 12
7 percent (i.e. double performance for the savings component and nominal
8 performance for the B/C component). The 12 percent is applied to the actual
9 amount of \$200 and the PI amount is \$24 (i.e. \$200 x 12%). By comparison, if
10 the existing budget formula is retained, the PI would only be \$12 (i.e. budget
11 amount of \$100 x 12%) and the utilities would earn only \$12 (i.e. \$100 x 12%).
12 Based on this illustration, the actual-based PI formula would encourage
13 overspending which in turn will give rise to an increase in PI.

14 **Q. In your scenario, if utilities overspend, doesn't the excess spending come out
15 of next year's budget? How does that encourage overspending?**

16 A. It does come out of next year's budget, but it still encourages over spending. As
17 illustrated in the above example, it is beneficial to earn 12 percent on the higher
18 amount just by increasing the spending instead of facing the challenge of trying to
19 achieve better performance. If we assume that the yearly budget is \$100, then the
20 budget for two years would be \$200. If the utility does not overspend as shown in
21 the example, and does not achieve higher performance, then it will get 8% each
22 year (i.e. 4% for the savings component and 4% for the B/C component). Thus
23 their total PI would be \$16 in two years (i.e. \$200 x 8%). It is much lower than

1 the \$24 the utility could earn without any performance gain just by spending \$200
2 in year one. If budget based PI is changed to actual-based PI, we will be
3 encouraging higher spending not higher performance.

4 **Q. What is your conclusion about the OCA's recommendation to support the**
5 **change in the calculation methodology of the PI?**

6 A. As noted in our direct testimony, we believe that it is premature to make any
7 changes to the existing budget-based PI formula until all relevant issues are fully
8 explored. In OCA's testimony, it assumes that changing the circumstances (in
9 this case PI formula) would not change the behavior of a profit maximizing
10 regulated entity. As shown above, changing the PI calculation from a budget-
11 based formula to an actual-based model may encourage overspending, a point that
12 OCA did not recognize (ref. OCA response to Staff 1-1, attached).
13 Therefore, we think that it is premature to change the PI formula at this time
14 without conducting an in-depth analysis of such a change. Given the magnitude of
15 the PI amounts, Staff believes that the PI working group needs to finish its task
16 and conduct a comprehensive review of the issues before any steps are taken to
17 change the PI formula.

18 **Q. Please comment on the OCA's suggestion that the actual-based PI formula**
19 **avoids the double counting of unspent budget dollars that are carried**
20 **forward.**

21 A. OCA suggests that if the budget-based PI formula were changed to an actual-
22 based PI formula, the potential double counting of budget dollars would be
23 avoided. Specifically, OCA notes that if program dollars in one year are unspent

1 and carried forward and included in the budget for the subsequent program year,
2 the utility could also earn an incentive on those carried forward amounts.

3 This issue is simply resolved without changing the PI formula. Specifically, as
4 noted in our testimony, the utilities can notify the Commission of under spending
5 in any year so that it can be identified and excluded from the calculation of PI in
6 the subsequent year.⁹

7 **Q. Do you have any other comments?**

8 A. Yes. OCA recommends that the PI working group lacks specific direction or
9 resources to undertake a thorough review of options to the incentive
10 methodology.¹⁰ We believe that the PI working group includes experts from the
11 industry, OCA and Staff and that the group has sufficient resources to conduct a
12 comprehensive review. Further, the recommendations of the working group will
13 be shared with the Core Team for their input. Finally, any recommendation
14 adopted by the Core Team and reflected in any future Core or natural gas energy
15 efficiency filings will be subject to review and approval by the Commission.
16 Based on the above, we believe that the PI working group does not lack specific
17 direction or resources to undertake a thorough review of options to the incentive
18 methodology.

19 **Q. Does that complete your testimony?**

20 A. Yes, it does. Thank you.

21

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⁹ Docket DG 09-049, letter from Sarah Knowlton, August 10, 2010.

¹⁰ Source: OCA Testimony at page 10.

DE 10-188 Core Efficiency Programs
OCA's Responses to Staff's Data Requests – Set #1

Date Received: October 21, 2010

Date of Response: November 1, 2010

Request No.: Staff 1-1

Witness: Stephen R. Eckberg

Request: Reference page 9-10. With respect to the proposed change in the performance incentive (PI) calculation from 'budget' to 'actual' expenses, please respond to the following questions:

- a. Does OCA believe the proposed change creates a possibility of over spending? Please explain.
- b. If the OCA believes there is a possibility of overspending, how does the OCA suggest that such potential overspending should be dealt with? Please explain.
- c. If the OCA believes there is a possibility of overspending, does OCA believe that a limit on over spending above budgeted expenses should be set? Please explain.

Response: Objection. The request seeks additional testimony.

Subject to and without waiving the objection, Mr. Eckberg states as follows:

[Note: For the purposes of responding to all sections of this question, the OCA interprets "overspending" as referred to in this data request to mean spending by any of the six utilities that is greater than Commission-approved budget levels.]

- a. No. The OCA does not believe that the proposed change to the PI calculation *creates* the possibility of overspending the planned budget for a given program year. It is the OCA's understanding that the possibility to overspend already exists whenever additional funds beyond the amounts planned become available during a program year. Such additional funds could become available from sources such as: additional FCM payments beyond planned amounts; increased kWh or therm sales due to various factors which could increase SBC and/or EE charge collections for programs; legislative or commission action which

increases SBC (electric) or EE charge (natural gas) funding to programs; or other reasons.

b. The OCA believes that the current 2011-2012 program proposals have neither more nor less potential for over-spending than programs in previous years.

c. The OCA has not contemplated a limit on "over budget expenditures" for the utility-administered energy efficiency programs. }