Utah DSM Rate Design Working Group

Rate Designs that Promote Energy Efficiency and Conservation

Report to the

Utah Public Service Commission

May 11, 2009

Submitted by
Utah DSM Rate Design Working Group

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EXECUTIVE SUMMARY

As a result of the Cost of Service, Rate Spread, and Rate Design Stipulation ("Stipulation") filed on September 29, 2008 by the parties in the Rocky Mountain Power's (RMP) general rate case (Docket No. 07-035-93) and the subsequent Commission Order issued on October 10, 2008, a DSM Rate Design Working Group has been convened to discuss and investigate rate design proposals to promote conservation and energy efficiency. This Working Group consisted of approximately 30 participants representing 19 parties.

The Working Group met five times over a period of five months. During these meetings, individual members of the Working Group made presentations and led the discussions on specific issues identified by the Working Group. These presentations and discussions provided a forum to educate the Working Group members on alternative rate designs for the different customer classes and alternative methods to remove the Company's disincentives towards investing in energy efficiency programs. However, because of time constraints, most of these issues were not fully studied. Consequently, the Work group was not able to reach consensus over the issues that were discussed. Although resolution of issues did not occur, the Work Group believes the time spent was worthwhile in helping parties gain a better understanding of the issues. This report is the Working Group's report to the Commission regarding the Working Group's activities and recommendations, as was required by the Stipulation.

INTRODUCTION

On September 29, 2008, the parties in Rocky Mountain Power's general rate case (Docket No. 07-0355-93) filed a Stipulation on Cost of Service, Rate Spread, and Rate Design – Phase II ("Stipulation") which was approved by the Commission in its Report and Order on Cost of Service and Rate Design issued on November 6, 2008. That stipulation required

> "The DSM advisory group, or another group to be established by the Division with similar representation by stakeholders ("DSM Group"), will convene to discuss and investigate rate design proposals to promote conservation and energy efficiency. The first meeting of the DSM group must be convened within 30 days of the Commission's approval of this Stipulation. The DSM Group shall submit a report regarding the DSM Group's activities and recommendations to the Commission within six months of the DSM Group's first meeting. The Parties agree that this report to the Commission will not report on pricing based on customer vintage. Following the filing of said report, the DSM Group will continue to meet quarterly thereafter."

As was required by the Stipulation, the DSM Group convened for its first meeting on November 10, 2008. This report is the DSM Group's report to the Commission regarding the Group's activities and recommendation's as was required by the Stipulation.

MEETINGS

The DSM Rate Design Group met five times. Each meeting focused on a pre-assigned subset of the issues with individual participants making presentations and leading the discussion on the various issues. Most of the presentations were distributed in advance of

the meeting where that issue would be discussed. The specific dates that the meetings took place were as follows:

1. November 10, 2008
2. January 8, 2009
3. February 5, 2009
4. February 26, 2009
5. March 12, 2009

ISSUES

At the first meeting of the DSM Rate Design Group, participants reviewed the Taskforce's assignment and agreed upon a list of sixteen issues to be discussed in preparation for a report to the Utah Commission on May 11, 2009. It was agreed that each meeting would focus on a pre-assigned subset of the issues with individual participants making presentations and leading the discussion on the various issues and proposals. It was further agreed that those making proposals would circulate a discussion paper on their proposal in advance of the meeting where that issue or proposal would be discussed. Below is the list of the sixteen issues discussed by the group.

1. Lorenze curve of peak and average usage.
2. Elasticity of usage.
3. Marginal cost of production.
4. Reasonable opportunity for the company to recover its allowed rate of return.
5. Decoupling the Company's revenue requirement.
6. Fixed cost recovery through fixed charge.
7. Inclining rates for both the summer and winter.
8. Time of use pricing (real time pricing, Scheduled time pricing, and critical peak pricing)
9. Proper differential between block prices.
10. Demand and energy charge balance for commercial class.
11. Considerations to split some of the Schedules (e.g., Schedules 6 and 9).
12. Rate Impact of the rate design for the customers in the same schedule.

13. Off ramps for commercial customers impacted unfavorably and on ramps to more favorable rates for those commercial customers who demonstrated efficient use of energy over time.
14. The 15 minute timetable for determining the highest demand peak for the month.
15. Inability to switch between utility companies. This comes into play when Rocky Mountain is accepting bids in the summer time to buy power.
16. Should Co-generation tariff be established?

Besides these issues, the group indicated a desire for RAP (Regulatory Assistance Project) to give a presentation regarding innovative rate designs that promote energy efficiency to inform the group about similar policies in other states. On January 8, 2009, Jim Lazar of RAP gave a presentation on rate design options and revenue decoupling.

SPECIFIC PRESENTATIONS

Five rate design presentations were made during the task force, four by interested parties and one by RAP. The following pages contain a write up of each presentation followed by comments from the participating parties.

PRESENTATION BY RAP (Jim Lazar)

Jim Lazar of the Regulatory Assistance Project (RAP) gave a thorough overview of rate designs for various classes of customers. These rate designs were cost-based and promote energy efficiency. The complexity of the rate designs varied across customer class. More complex rate designs were deemed appropriate for larger customers who had the sophistication to understand the designs and usage levels to spread the costs of more advanced meters. For smaller usage customers i.e., the residential class, he recommended inverted block rates which he explained are common and cost-based (either load-factor based, resource cost based, or environmental cost based) and provide incentives for conservation and adoption of energy efficiency measures by customers. The inverted block rate is preferable to Time Of Use (TOU) rates or critical peak pricing rates, both of which require more expensive meters that do not appear to be cost effective at this point. He explained that over 70% of low income customers use less than the average kWh and thus would not be harmed with steeply inverted rates, the

other 30% of low income customers could be eligible for demand side programs (DSM) to help lower energy usage and thus mitigate bill impact.

For small commercial customers, RAP recommends against inverted block rates as usage per customer varies greatly depending on type and size of business. RAP recommends either TOU rates or critical peak pricing if savings can justify the cost of advanced meters, if not, then an inverted block rate based on historical usage (rolling baseline rates) may prove useful in encouraging the adoption of energy efficiency measures. For large commercial or industrial customers, RAP recommends the adoption of TOU rates in addition to critical peak pricing. RAP points out that the most common mistake in designing rates for large commercial and industrial customers is placing too much emphasis on demand charges and assuming that energy usage is more volatile than demand.

RAP also gave an overview of decoupling mechanisms. RAP indicated that decoupling is a mechanism to ensure that utilities have a reasonable opportunity to earn the same revenues that they would under conventional regulation, independent of changes in sales volume for which the regulator wants to hold them harmless. It differs from conventional regulation in that it sets revenues based on cost, and lets the rates float as sales volumes change between rate cases whereas the conventional regulation sets rates based on cost, and lets the revenues float as sales volumes change between rate cases.

RAP advanced the following six-point plan for effective and fair decoupling:

1. The mechanism should provide about the same revenues as conventional regulation, save for the elements you want to decouple.
2. Effective conservation programs should be provided.
3. Progressive rate design must be in place.
4. Cost of Capital adjustments should be made.
5. There should be a rate collar.
6. Periodic rate proceedings to “re-link” to costs should be held.

RAP warned that a decoupling mechanism should not be confused with an attrition adjustment.

Comments on RAP's Presentation

CCS's Comments

Approximately six years ago Rocky Mountain Power (RMP) implemented an inverted energy rate structure during the summer peak period for the Utah residential class. At that time, parties considered many of the issues raised in RAP's presentation in developing the current residential rate design; a rate structure that is basically unchanged except for an increase in the monthly customer charge in 2006. Looking forward, the key issue is whether the existing residential rate design requires certain modifications so that it better reflects cost causation, ensures intra-class fairness and sends a stronger price signal to high use customers to reduce usage in summer peak months.

While the Committee has not been a proponent for revenue decoupling, we believe that the six elements proposed by RAP is an analytically sound starting point for evaluating alternative decoupling mechanisms. We specifically note RAP's acknowledgement that having decoupling reduces risk and should be reflected in the allowed ROE. We also agree with RAP's observation that "a decoupling mechanism should not be confused with an attrition adjustment."

SWEEP'S Comments

SWEEP thinks that Jim Lazar of RAP gave a balanced overview of rate design alternative. Sweep urges the Division to recommend that the Commission take administrative note of the matrix presented in Jim Lazar's presentation which shows the preferred rate design options by class. In Docket No. 081-420EG "IN THE MATTER OF THE INVESTIGATION OF REGULATORY AND RATE INCENTIVES FOR CUSTOMERS OF GAS AND ELECTRIC UTILITIES", the Colorado Public Utilities Commission took administrative note of Lazar's matrix and indicated that it would attempt to implement its recommendations for its utilities in

future rate proceedings. The Utah Commission should take administrative note of the Colorado Commission's findings as described in its Final Order in this docket.

SWEEP strongly urges the Utah Commission to begin implementation of new rate designs that will encourage conservation and energy efficiency. SWEEP presented a proposal for residential customers which encourages the efficient use of electricity and which places the costs of new resources on the group of customers that make the largest proportional demands on the system. This calls for an inverted block rate which divides usage into four separate blocks with the last block paying substantially more than the first block.

SLCAP & AARP's Comments

New rate designs and cost recovery mechanisms should be considered both carefully and comprehensively, and must not be pancaked one on top of another or imposed in isolation without recognition of how they impact consumer bills. Incentives and consideration of lost revenues should be directly tied to the utility's measurable and verifiable performance in achieving energy efficiency goals established by the Commission. The utility should not be rewarded for exogenous factors such as weather, economic conditions, high energy prices and other factors that reduce energy usage separate and apart from utility sponsored energy efficiency programs. If consumers use less energy, they should not see their bills increase due to numerous added surcharges.

DPU's Comments

The Division, on behalf of itself and the members of the DSM Rate Design Working Group, would like to extend its appreciation Jim Lazar of RAP who, in a relatively short notice, prepared and delivered an excellent presentation on rate designs for various rate classes and alternative decoupling mechanisms to the DSM Rate Design Working Group.

Regarding the rate designs for various customer classes, RAP provided a table that summarizes different rate designs and their suitability and availability to different customer classes. For the residential rate class, he considered the inverted block rate as the recommended rate design. While the Division agrees with RAP that inverted block

rate design is appropriate rate design for Utah's residential customers, the Division believes that the current inverted block rate design needs to adjusted in such a way that it reflects cost causation while at the time encouraging energy efficiency. One way to achieve that is to keep the current three block design, increase the differential between the first and last block, and increase the customer charge (gradually) to a level that is consistent with the Commission approved methodology.

Regarding the commercial class, RAP recommended time of use (TOU) rates with fixed time periods if interval metering is not in place and TOU plus critical peak pricing if interval metering is in place. However, in Utah we have both demand and energy charges. Customers in this class vary widely in their load factors. This creates problems in balancing the demand and energy charges. A higher demand charge or energy charge would negatively affect the low or high load factor customers, respectively. The Division thinks that further study is needed in understanding the characteristics of the customers in this class so that a rate design that treats the customers in this class more fairly and promotes energy efficiency can be determined. The basis for this that based on the 08 rate case, more of the rate increase will be collected with a demand charge. This leaves the low load factor customers subsidizing the high load factor customers. This problem was there for the last few rate cases.

With respect to decoupling, RAP's presentation on this topic was balanced. Mr. Lazar provided a six point guide for decoupling and warned against confusing a decoupling mechanism with an attrition adjustment. One needs to be careful about the source of the reduced revenue before making adjustments to the decoupling mechanism. The Division thinks that this six point guide is good starting point in evaluating possible decoupling mechanisms.

Rocky Mountain Power's Comments

RMP thanks Mr. Lazar for his presentation summarizing a number of rate design structures throughout the country. RMP agrees with Mr. Lazar's contention that inverted

rates are not appropriate for commercial and industrial customers. It also agrees with his notion that rates must be cost based.

RMP also commented on Mr. Lazar's statement that "70% of low income customers use less than the average kWh". It noted that nearly the same percentage of non-low income customers use less than the average kWh and that income was not a good predictor of usage.

PRESENTATION BY WRA (Steve Michel)

Issues Addressed:

1. Reasonable opportunity for the company to recover its allowed rate of return.
2. Decoupling the Company's revenue requirement.
3. Fixed cost recovery through fixed charge. (Steve Michel, RMP)

On February 5, 2009 Steven Michel with Western Resource Advocates (WRA) led a discussion of various techniques to remove utility disincentives for providing energy efficiency as a resource for customers. The discussion began with an explanation of how and why utilities lose money by deploying energy efficiency. This occurs because utility rate structures are such that the savings to participant customers are often greater than the avoidable costs of the utility. This disincentive for utilities, WRA believes, prevents energy efficiency from being developed to its full economic potential.

The discussion then proceeded to various mechanisms to eliminate this disincentive. Among these mechanisms were:

1) Establishing a company separate from the utility to implement efficiency programs. "Efficiency Vermont" and the "Oregon Energy Trust" are two examples. These companies do not eliminate utility losses from efficiency, but allow efficiency to go forward by entities unaffected by these losses.

2) Rate designs which allow the utility to partially or fully recover its fixed costs through fixed charges. This modification could be limited to high usage customers, to avoid a

situation where low use residential customers see an increased bill. This mechanism, however, works against providing rate design incentives such as increasing block rates, for customer efficiency.

3) Decoupling mechanisms that provide periodic revenue adjustments to allow the utility to recover a constant level of fixed costs per customer. This assures the utility that its revenue requirements are achieved regardless of customer efficiency levels. There are many adjustments to this type of mechanism (weather, growth, ROE, etc.) that can be made, depending upon a commission's appetite for complexity and precision, or simplicity. This mechanism generally eliminates both the disincentive for efficiency, and the incentive for the utility to increase throughput (selling customers both CFLs and plasma TVs), and can be combined with a fixed cost recovery mechanism (2, above) to limit the magnitude of the adjustments.

WRA also suggested that, in addition to removing disincentives, Commissions may want to provide affirmative incentives for utilities to undertake DSM – because of the non-monetary benefits energy efficiency provides over supply-side resources.

WRA believes this discussion of incentives and disincentives for DSM should continue with further stakeholder workshops – so that a mechanism, or combination of mechanisms, can be developed that best meets the needs of Utah customers and citizens.

Comments on WRA's Presentation

CCS's Comments

WRA presented, and led a discussion on, three general alternatives to eliminate utility disincentives to pursue energy efficiency. The discussion centered on three approaches: (1) A separate entity to administer energy efficiency programs such as the Oregon Energy Trust; (2) straight-fixed variable rate design where utility costs categorized as fixed are recovered through a fixed distribution charge; (3) revenue decoupling mechanisms.

RMP has acquired a cost-effective portfolio of energy efficiency and demand-side management programs in Utah absent any of the mechanisms addressed by WRA. Additionally, the Company

has been able to recover prudently-incurred DSM expenditures in a separate tariff rider adjusted periodically to track the level of DSM investment. DSM is a cost-effective resource that helps the Company meet a portion of its rapidly growing resource deficit position and RMP has recently either altered or expanded existing Utah programs to target greater participation levels and energy savings. RMP's history and present circumstances calls into question the underlying premise of whether RMP has disincentives in the area of DSM. The Committee believes that any of the mechanisms addressed by WRA would have to be shown to provide more benefits than costs before implementation in Utah could be considered.

DPU's Comments

Currently the Company acquires and implements many cost-effective DSM programs. The company recovers the costs of implementing DMS programs through a tariff rider. However, the costs recovered through the tariff rider do not include the revenue lost due to the reduced sales. This gives the Company reason for concern. The Division agrees that the three approaches presented by WRA are potential means of removing the Company's disincentives towards DSM. Therefore, the Division supports further analysis and consideration of methods to eliminate or reduce the utility's financial disincentives associated with investment in energy efficiency measures.

UCE's Comments

UCE is supportive of the concept proposed by Steve Michel, of Western Resource Advocates (WRA), to study providing "affirmative incentives" in addition to removing disincentives. However, UCE has some concern about the concept of "Rate designs which allow the utility to partially or fully recover its fixed costs through fixed charges" included in this write-up. UCE is concerned that this type of rate design modification is counter to the intent of the stipulation and the intent of the PURPA standard relating to rate design, which states "rates …shall promote energy efficiency investments". While we recognize that utilities need assurance that they will be able to recover fixed costs, we strongly agree with the WRA comment that this mechanism "works against providing rate design incentives such as increasing block rates, for customer efficiency". To address the valid concern of recovery of fixed costs, rate design mechanisms should be reviewed in concert with other regulatory mechanisms, such as decoupling.

SLCAP and AARP's Comments

Several advisory group participants proposed the decoupling of revenue from usage. However, decoupling itself does not encourage energy efficiency by consumers. It is a revenue collection mechanism that would guarantee utilities the recovery of a predetermined level of revenue between rate cases, without regard to the volume of energy sold. In some forms of decoupling there is no consideration of the cause of lost revenue (i.e., the loss of revenue could be completely unrelated to utility sponsored energy efficiency programs). RAP noted that decoupling proposals from around the country range from "awful to excellent." We agree that if pursued, decoupling can be done in ways that are better or worse for ratepayers. The National Association of State Utility Consumer Advocates recently adopted a resolution listing the essential consumer protections for decoupling: "NASUCA recommends that the mechanism be structured to (1) prevent over-earning and provide a significant downward adjustment to the utilities' ROE in recognition of the significant reduction in risk associated with the use of a decoupling mechanism, (2) ensure the utility engages in incremental conservation efforts, such as including conservation targets and reduced or withheld recovery should the utility fail to meet those targets, and (3) require utilities to demonstrate that the reduced usage reflected in monthly revenue decoupling adjustments are specifically linked to the utility's promotion of energy efficiency programs."[1]

According to Dr. David Dismukes, Professor and Executive Director of the Center for Energy Studies at Louisiana State University, the majority of states with energy efficiency programs have not adopted decoupling/lost revenue adjustments.[2] Such proposals have also been rejected by regulatory agencies in other states. For example, although the law in New Mexico permits decoupling, the New Mexico Public Regulatory Commission found that Public Service New Mexico's (PNM) proposed lost revenue adjustment too far reaching:

[1] NASUCA Resolution 2007-01 (June 2007). www.nasuca.org

[2] David E. Dismukes, Ph.D., Professor and Associate Executive Director, Center of Energy Studies, Louisiana State University. "Regulatory Issues for Consumer Advocates in Rate Design, Incentives and Energy Efficiency", Presentation to the National Association of State Utility Consumer Advocates Mid-Year Meeting, June 11, 2007. Available at www.nasuca.org

"If implemented, it would, in effect, make PNM whole for past conservation efforts of consumers that have absolutely nothing to do with the enactment of the Efficient Use of Energy Act on which PNM relies for recovery for lost volumes. Moreover, PNM's proposal fails to take any account of customer growth that has occurred during the time that consumption per customer may have declined. Therefore, the Commission finds that the decoupling proposal advanced by PNM in this case is fatally flawed, and that the Commission will not consider it again in any case." (PNM, Case No. 06-00210-UT, 6/29/07)

SWEEP's Comments

Steve Michael presented a clear example of why a utility would hesitate and be disinclined to invest in demand-side resources. To mitigate these disincentives, Michael suggests three possible solutions; first, to move some or all fixed charges into a customer charge, second, to create or promote a demand-side trust like Oregon has done and third, to consider some decoupling measure that would collect revenues for fixed charges independent of actual usage. A decoupling mechanism if successfully implemented would eliminate disincentives inherent in utility investment in energy efficiency but Michael suggests it would not create incentives for investment in such efficiency. Michael argues that rate design could motivate customers to pursue DSM on their own or in conjunction with utility DSM programs while some other incentive such as a reward for every kWh saved might motivate the utility to pursue DSM. SWEEP opposes the first option of collecting all fixed charges in a customer charge, this will create a rate structure that will encourage additional consumption of electricity and add to the future costs of the system. The second solution of a state-sponsored energy trust that would administer DSM investments would require state legislation and political support for such an agency is unlikely. SWEEP recommends consideration of the third option, decoupling and urges the opening of a docket that would investigate this option. Given the tremendous success of Questar's decoupling mechanism with respect to the change in management's attitude towards DSM, a decoupling mechanism for PacifiCorp might see even better results. PacifiCorp's IRP identifies DSM as one of the most cost effective resources thus increased investment in these resources will benefit ratepayers in the long run. SWEEP supports further analysis and consideration of methods to mitigate the utility's financial disincentives associated with investment in energy efficiency measures.

RMP's Comments

RMP supports Mr. Michel's argument that rate designs that allow the utility to partially or fully recover its fixed costs through fixed charges are necessary.

PRESENTATION BY CENTRAL VALLEY WATER (Ron Day)

Issues Addressed:

1. The 15 minute timetable for determining the highest demand peak for the month.
2. Inability to switch between utility companies. This comes into play when Rocky Mountain is accepting bids in the summer time to buy power.
3. Should Co-generation tariff be established?

Central Valley Water Reclamation Facility is the largest wastewater treatment facility in the state of Utah. It services five special districts and two cities treating approximately 50 million gallons of water a day. As part of the treatment process, the facility captures methane gas which it uses to run generators, thereby producing approximately 1400 kWh of electricity as well as providing heat and cooling to the plant operations. Because of EPA regulations, Central Valley is required to have back up engines in order to meet stand alone requirements (4,000 kWh). These resources, along with serving the seven entities, in effect makes Central Valley a micro utility. Based on 25 years of experience, Central Valley offers the following advice on utility rate design within a demand side management environment.

Regarding residential rates, Central Valley recognizes that Rocky Mountain Power needs a fair way to recover its fixed costs and the only current mechanism for doing so is on a kWh usage. Central Valley is not opposed to a higher customer charge much like is presently done with the Questar tariff. However, recognizing that the two biggest factors affecting both peaks and usage are central air conditioners and size of homes, there must be blocks with price differentials significantly large enough to affect consumer attitudes to conserve power consumption even if it means that the high end users may be over paying for their services. One questions whether the

highest blocks are subsidizing other blocks when the price of additional new or purchased generation is factored in. Central Valley strongly recommends, as was suggested by Jim Lazar, that a three-year rolling baseline rate be established for new and increased customer usage to cover said generation growth.

Commercial and industrial customers have demand/facility charges that serve somewhat as fixed costs. They are determined by the highest consecutive 15-minute usage during the month. Schedule 6 has a flat charge for its operations, while schedules 8 and 9 are on time of usage from May through September.

As with the residential customers, Central Valley is not opposed to a flat fixed cost so long as it is not based on a 15-minute interval and the energy costs are adjusted to reflect the proportional costs. We believe this sends the right price signal for companies to reduce energy consumption where possible. Schedule 6 should be included in this process as well. Central Valley reiterates, as we did with the residential, that a three-year rolling baseline rate be established for new and increased customer usage to cover generation growth.

Questar's biggest challenge has been determining when to buy natural gas. They have had much more success implementing DSM as customers can apply alternative resources easier than are available with energy. As a result, Questar has been able to collect more revenue for fixed costs by receiving a higher customer charge. Because natural gas is a non-regulated commodity, customers have the right to either buy it from Questar or some other source. However, Questar must deliver it. The tariffs, as they now stand, are not user friendly as it relates to switching between tariffs offered by Questar, thus reducing the ability to implement DSM to its fullest.

A classic example where this could work better is during the summer months of May through September. Rocky Mountain Power is in need of more power which it buys through its demand exchange program. Questar has excess capacity on its line during this period. If tariffs permitted co-gen facilities such as ours to burn more gas during the summer and reduce Rocky Mountain Power peak time usage, and reverse the process in the winter by taking more power and using less natural gas this would help the DSM program for all three entities. This is why Central

Valley Water proposes a co-generation tariff for consideration as well as asking that co-generation qualify for DSM funding.

The final area to be addressed is decoupling. Central Valley is not opposed to this concept. However, since this reduces the earnings risk, there should be a corresponding reduction to the rate of return.

Comments on Central Valley Water's Presentation

DPU's Comments

The Division agrees with the Central Valley Water's assessment that the size of Utah's new homes and central air conditioning are major contributors to increases in both peak demand and overall usage. The Division also agrees that there should be three blocks with price differentials large enough to affect consumer attitudes to conserve power consumption.

Regarding the inability to switch between utility companies and the establishment of Co-generation tariff proposed by Central Valley Water, the Division would support any further study that would serve to further clarify the issues involved.

SWEEP's Comments

SWEEP agrees with the assessment of Central Valley Water Reclamation Facility that peak demand and energy usage in the residential sector is driven by central air conditioners and the large size of new homes. We agree that inverted block rates must have blocks with price differentials significantly large to affect consumers' attitudes to conserve power and invest in energy efficiency measures. Pricing of the higher blocks should reflect the cost of new generation or purchased power during peak.

PRESENTATION BY SWEEP (Dr. Richard Collins)

Issues Addressed:

1. Lorenze curve of peak and average usage.
2. Elasticity of usage.

3. Marginal cost of production.
4. Proper differential between block prices.

Rich Collins representing SWEEP provided the case for an inverted block rate design that would encourage residential ratepayers to more efficiently use electricity. The inverted block rate design is intended to meet the various goals of rate design considered by the Commission. These goals include: setting rates to reflect cost causation, the promotion of conservation and energy efficiency, administrative ease, public understanding and equity. As explained by Jim Lazar, rates should be designed according to particular rate classes. It is generally accepted that time of use rates based on real time costs are theoretically the best for meeting cost causation and sending the most appropriate pricing signals to customers to promote efficiency. However, given the costs of real time meters and the signaling equipment necessary to send real time pricing signals to customers, this option is neither available nor cost effective for residential customers. The next best option is inverted block rates. Mr. Lazar maintains that inverted block rates are cost based and function as a demand/energy rate and as an appropriate seasonal rate.

An analysis of usage rates by residential customers was presented by SWEEP. Usage data of Utah residential customers provided by Rocky Mountain Power shows that use per household varies dramatically. After careful examination, usage levels were divided into four different blocks. The first block contains usage from 0 to 400 kWh, the second block, 401-1000 kWh, the third block, 1001-2000 kWh and the fourth block contains usage greater than 2000 kWh.

The following table shows the usage levels in terms of percentage of customers in each block and the percentage of total summer time use per block

2007-2008	% of customers	% of usage
Block 1	24%	6%
Block2	45%	34%
Block 3	24%	38%
Block 4	7%	21%

Thus, approximately 70% of customers who used less than 1000 kWh per month account for just 40% of the residential electricity use during the summer months while the top 30% of residential customers who use more than 1000 kWh account for 60% of residential summer time usage. The concentration of usage is even higher in the fourth block where the top 7% of the customers use 21% of the power in the summer months. Further analysis of summer residential usage growth by block between 2006-2007 and 2007-2008 reveals that growth is substantially larger in the higher blocks. The top two usage blocks account for 82% of the summer residential usage growth while the fourth block contributed over 48% of the total increase in residential usage between the two years. It is uncertain whether the increase in residential use between the two years is due to growth in customers, weather or some other reason, but clearly the growth in electricity usage is concentrated in the top two blocks as shown by the table below

Summer Growth (% of Total for each Block) 2006-2007 & 2007-2008

Total Increase in Customers	**40,728**	**Total Increase in kWh**	**282,973,672**
% of Total Increase Attributable to Block 1	11.8%	% of Total Increase Attributable to Block 1	2.9%
% of Total Increase Attributable to Block 2	34.0%	% of Total Increase Attributable to Block 2	15.1%
% of Total Increase Attributable to Block 3	29.9%	% of Total Increase Attributable to Block 3	33.6%
% of Total Increase Attributable to Block 4	24.3%	% of Total Increase Attributable to Block 4	48.4%

In recent rate proceedings, the Company argues that the primary cause for higher rates is the growth in demand for electricity. The Company provides evidence that new generation resources are more expensive than existing resources. Thus growth in demand for electricity is driving cost increases for all customers. The principle of cost causality dictates that the customers who are responsible for the growth in demand should pay their fair proportion.

The rationale for the number of blocks and pricing of blocks is provided. The number of blocks should reflect usage patterns and be priced to send a clear price signal that will get a demand response and is reflective of costs placed on the system. Evidence is presented by both SWEEP and RAP which shows that generation costs range from $.02 to $.04 per kWh for embedded cost resources such as hydro and older base-load resources while newer base-load resources are more expensive and are in the range of $.08 per kWh. Intermediate gas resources are in the $.12 range depending on the forecast of natural gas prices, while, resources needed to meet critical peak can cost $.50 or more per kWh. Given that air conditioning load is a major contributor to peak load, the higher use blocks should reflect these higher generation costs. SWEEP recommends that the

pricing of residential blocks should be logical and easily understood and reflect the costs placed on the system. Thus price differentials of 25% increase for the second block, 50% increase for the third block and a 100% increase for the fourth block are recommended. These price differentials place most of the price increase on the latter two blocks to reflect the increased growth in these blocks and the resultant costs placed on the system.

During the meeting, Rocky Mountain Power representatives expressed concerns about revenue stability with the inverted block rates. The Company worries about its ability to collect its authorized revenue requirement when most of the rate increases for residential customers are concentrated at the higher blocks which will experience largest increases in their rates. To address revenue stability concerns, SWEEP recommends that either an explicit recognition of elasticity impacts be incorporated into revenue requirement determinations or the adoption of a decoupling mechanism to address the recovery of fixed costs.

Sweep reminds the Commission of the recently passed H.R.9, the Joint Resolution on Cost-Effective Energy Efficiency and Utility Demand–Side Management. This resolution urges state and local governments, electrical corporations, natural gas utility corporations… to work together to recognize energy efficiency as a priority resource. The resolution states that the Legislature expresses support for regulatory mechanisms that could include performance-based incentives, decoupling fixed cost recovery from sales volume, and other innovative rate deigns intended to help remove utility disincentives and create incentives to efficiency and conservation so long as these mechanisms are found to be in the public interest. SWEEP recommends that the PSC move forward with adoption of a fixed cost recovery decoupling mechanism in conjunction with adopting our tiered rates proposal. We believe that the adoption of both a decoupling mechanism and innovative rate designs such as the inverted block rate for residential customers and time of use rates for commercial and industrial customers is in the public interest and will meet both the Commission's goals and the Legislature's resolutions.

Comments on SWEEP's Presentation

CCS's Comments

In its presentation, SWEEP relied on a combination of 1) "Lorentz Curve" type analysis of

residential summer usage, 2) various sources for estimating residential price elasticity and 3) resource cost information from an early draft section of PacifiCorp's 2008 IRP as a proxy for marginal generation costs to construct a four-part summer energy rate design. According to this rate design, the rates for the two lower blocks are based on average embedded costs and the rates for the two higher blocks are based on long run marginal costs of providing service. Additionally, the tail block (4^{th} block) rate is about double the first block rate. According to SWEEP, the tail-blocks are priced in a way to stimulate a strong demand response from the residential segment where summer energy usage has substantially increased over the past few years.

The Committee commends SWEEP for attempting to critically analyze changes/trends in summer usage patterns, residential price elasticity and available marginal cost information to formulate an alternative energy rate structure. The Committee used similar information in the last rate case to address the summer and winter energy rate structure; in particular, the appropriate level of the summer tail block rate. While the Committee shares SWEEP's view of sending a stronger conservation message via the energy rate structure, we also believe that other objectives such as cost causation, fairness, and rate continuity or stability need to be weighed in designing rates. We also question the validity of SWEEP's proposal that the Commission adopt a revenue decoupling mechanism (raised in its summary versus presentation) given that SWEEP has not presented a thorough analysis of how such a mechanism provides additional benefits, how it would operate in conjunction with the tiered rate proposal, or policy implications of such a proposal.

Lastly, SWEEP's presentation highlights current limitations in available information in the cost-of-service and rate design area. For example, parties' analytical efforts in the area of residential rate design have been plagued by a lack of 1) a Utah Marginal Cost Study, 2) weather normalized load data for the existing three residential summer blocks and 3) information on shared services that should be applied in determining appropriate customer charge levels (single vs. multi-family dwellings) within the residential class. These deficiencies need to be swiftly remedied by the Company to enable parties to develop better informed rate design proposals.

DPU's Comments

Though the SWEEP provided an analytical basis for its recommended three block rates, the Division believes that it was preliminary and needs further refinements in terms of the variables that should be considered in such analysis. For example, the revenues from the different consumption levels were not considered in the analysis. The Division agrees with SWEEP that blocks with significant price differential are needed to send the customers the appropriate price signal. However, the Division disagrees with SWEEP that the number of blocks should be four. Instead the Division believes that the current three blocks are appropriate.

UCE's Comments

UCE supports the comments made by Dr. Rich Collins, representing the Southwest Energy Efficiency Project (SWEEP), and recommends that an inverted block design be adopted that is inline with the design in Dr. Collins' proposal. We support further analysis with respect to weather normalization and price elasticity during the rate design process.

RMP's Comments

RMP believes that Mr. Collins' table above showing that small usage customers, comprising 24 percent of the customers, use six percent of the energy highlights a significant problem and subsidy in current residential rate design. RMP notes that 24 percent of the customers also pay only about six percent of total residential revenues, due in part to the low residential customer charge. However, 42 percent of the cost of serving them relates to distribution and retail costs which do not vary with usage. This means that these low usage customers are not providing revenues that adequately recover the cost of serving them.

RMP also does not support Mr. Collins' residential rate design proposals but will save those comments for other dockets.

SLCAP and AARP's Comments

Tiered or Inclining Block Rates

AARP and SLCAP recommend tiered or inclining block rates as the rate design proposal which both encourages energy efficiency and does not unnecessarily increase monthly fixed charges on low-use customers. As shown by both Rich Collins, and AARP/SLCAP witness Dr. Johnson, low-use and low income customers are not driving peak demand or demand for new investments.

Energy efficiency can be achieved without drastic changes to rate design or decoupling:

There are options to encourage conservation and energy efficiency at minimal cost to consumers. There are numerous examples of residential applications of demand response that do not require large investments in technology or drastic changes in rate design, but which can be highly effective in reducing peak demand, especially during critical periods. In a recent report the U.S. Department of Energy estimated that residential load control saved 0.4-1.5 kWh per customer per event (load control in this report included programmable thermostats, and direct load control of appliances and A/C, water heaters and pool pumps). Rich Collins showed that a small percentage of customers accounts for a disproportionately large amount of usage. Providing an incentive to only this small group of customers to reduce usage can have tremendous benefits to the system without imposing additional costs on other customers.

PRESENTATION BY RMP (Bill Griffith)

Issues Addressed:

1. Fixed cost recovery through fixed charge.

Rocky Mountain Power prepared an analysis of fixed costs that would appropriately be recovered through a fixed charge for residential customers. Based on the cost of service results filed in Docket 08-035-38, RMP's calculation showed that a monthly residential fixed charge of approximately $24.00 per month would be appropriate if the Company's fixed costs of serving residential customers were recovered through a fixed monthly charge.

Attached are two Exhibits that show how RMP calculated the monthly residential fixed charge.

Comments on RMP's Presentation

DPU's Comments

Based on the cost of service results filed by the Company in Docket No. 08-035-38, RMP calculated a fixed cost of $24.00. A small portion of this fixed cost ($2.00) is collected on customer charge. The rest is collected on a volumetric charge. The Division believes that only a customer charge calculated based on the method adopted by the Commission should be collected as fixed charge; the rest should be collected as a volumetric charge. This along with three block energy charge with a price differential large enough to influence customer behavior would encourage energy efficiency.

UCE's Comments

Bill Griffith, of Rocky Mountain Power/PacifiCorp noted that fixed cost recovery through fixed charges for residential customers would result in a charge of approximately $24.00 per month. This is of significant concern to UCE. We worry that a large fixed charge would blunt the price signal being sent to customers.

SLCAP and AARP's Comments

The advisory group discussed fixed cost recovery mechanisms, such as removing some or all fixed cost recovery from variable rates and increasing the customer charge. RMP prepared an analysis of fixed cost recovery through the customer charge. RMP's proposal would set the customer charge at $24 per month and volumetric rates would be reduced a commensurate amount. AARP and SLCAP oppose this type of rate design, sometimes called "straight fixed variable."

Increasing the customer charge, while reducing volumetric rates, is contrary to the goal of this advisory group. Indeed, such a rate design discourages conservation, as usage becomes less expensive. Shifting costs currently recovered on a usage basis to the fixed charge is especially harmful to low usage customers, who are often older households and low income households. Increasing fixed charges, whether through increased customer charges or new adjustment

surcharge mechanisms, disproportionately increase the bills of low usage customers. Cost recovery through volumetric rates, including tiered rates, ensures that those high usage customers, who are also most likely to take advantage of energy efficiency programs, also pay a fair share of the program costs. Information provided by Rich Collins indicates that high use customers drive the majority of the growth in revenue requirement. As AARP/SLCAP witness Dr. Charles Johnson showed in testimony in Docket No. 07-035-93, low income (Schedule 3) customers on average use less than Schedule 1 customers and contribute far less to peak demand.

SWEEP's Comments

The Company did provide input on the role of the customer charge in recovering fixed costs and the need to provide revenue stability for the Company. Revenue stability is a goal of rate design but it might conflict with other goals. Bill Griffith suggested that the ideal rate design would include a high customer charge and Time of Use (TOU) rates. SWEEP tried to address the revenue stability concern by recognizing the elasticity of demand effects and incorporating such effects in revenue requirement determination. Given the current rapid-fire rate requests of the Company, elasticity effects could be determined by the actual reactions by consumers and then explicitly incorporated into future revenue requirement projections.

CCS Comments

As part of a general discussion of fixed cost recovery mechanisms, RMP presented an analysis of the customer charge level necessary to recovery all fixed cost elements charged to residential customers. The Company's analysis indicated that a customer charge level of $24/month would be required to recover fixed cost elements charged to the residential class and that the energy rates would be correspondingly reduced.

Recovering all fixed cost elements through a customer charge has typically been referred to as a "straight fixed variable" or "SFV" rate design. A SFV rate design primarily accomplishes revenue stability for the utility. From a consumer perspective, the SFV rate design is problematic. For example, it would diminish the price signal sent via the energy rates to conserve energy. It would also have potential equity implications due to a disproportionate impact on low users.

The Committee does not support the SFV rate design concept. We generally support the current residential rate structure, which includes a formula determined by the Commission for calculating the customer charge and a three-tiered summer energy rate structure and a single (flat) winter energy rate. We believe the present customer charge needs to be divided into different customer charges for single family and multi-family residences. In addition, the present energy rate block structure may require changes going forward to send price signals that better reflect cost causation and promote energy conservation.

PRESENTATION BY ENERGY STRATEGIES (Kevin Higgins and Neal Townsend)

Issues Addressed:

1. Demand and energy charge balance for commercial class.
2. Considerations to split some of the Schedules (e.g., Schedules 6 and 9).
3. Off ramps for commercial customers impacted unfavorably and on ramps to more favorable rates for those commercial customers who demonstrated efficient use of energy.

Kevin Higgins and Neal Townsend of Energy Strategies made a presentation on the above listed issues. With respect to demand and energy charge alignment for commercial customers, they recommended that rate designs need to reflect cost causation. This could be accomplished by aligning demand-related charges with demand-related costs, energy-related charges with energy-related costs, and customer-related charges with customer-related costs. Recovering costs based on cost causation will minimize subsidies within a rate schedule and will send better price signals for energy and demand. Understating the customer, demand, and energy charge will shift cost to larger, higher load factors, and lower load factor customers within a rate schedule, respectively. They used Schedule 6 to illustrate their point.

With respect to the consideration of splitting some of the schedules, Energy Strategy brought forward the following suggested criteria that should be used in determining whether or not a new rate schedule should be created from an existing schedule.

- Is there a difference in the nature of the service provided to the customers on the proposed new schedule?
- Is there a difference in the utility facilities utilized by the customers on the proposed new rate schedule?
- Is there a charge/cost misalignment in the current rate schedule that is causing inequities for the customers on the proposed new rate schedule?
- Does the current rate schedule mix customers with fundamentally different rate design goals (e.g. residential and commercial/industrial)?

However, regardless of what criteria are used in splitting a rate schedule, Energy Strategies urged that caution should be exercised when considering splitting a rate schedule. One has to remember that creating a new rate schedule will dilute load diversity and increase the likelihood of irrational or problematic rate transitions (particularly if based on customer size). I addition, rate schedules populated with relatively few customers can produce anomalous cost of service results that are volatile from rate case to rate case. This is because class characteristics may change as new customers sign into the rate schedule.

In concluding, Energy Strategy indicated that as rate components become more granular (e.g., TOU energy charge), differences among customers with respect to cost to serve are increasingly captured by rate design rather than through different rate schedules.

Comments on Energy Strategies' Presentation

DPU's Comments

The Division agrees with Energy Strategies that charges need to be aligned with their respective costs. This would minimize interclass subsidization. The Division also agrees that when considering splitting a schedule, caution should be exercised. However, the load factors of the customers in Schedule 6 vary considerably such that an increase in the

demand charge would hurt the low load factor customers and increasing the energy charge would hurt the high load customers. Therefore, in order to promote energy efficiency, further study is needed to determine the pros and cons of splitting Schedule 6 and how it could be done.

UCE's Comments

Utah Clean Energy supports further analysis of rate design options for the commercial sector to advance energy efficiency while balancing the needs of diverse commercial energy customers.

SWEEP's Comments

Kevin Higgins and Neal Townsend of Energy Strategies made a presentation on demand and energy charge alignment for commercial customers. They make a cogent case for meeting one of the goals of rate design which is to design rates to reflect cost causation and minimize subsidies among and within classes. They recommend aligning demand charges with demand-related costs, energy-related charges with energy–related costs and customer-related charges with customer-related costs. Using Schedule 6 as an illustrative example, they show the benefits of meeting the goal of cost causation and minimizing subsidies. SWEEP agrees that their analysis is solid for meeting their stated goal. However, this task force was assigned to study rate designs that would encourage conservation and promote energy efficiency. On that account, the proposal failed to show how the proposed rate design would meet these objectives. SWEEP agrees that the design of rates to reflect cost causation and mitigate subsidies is an important rate design objective but it should not trump the objective of promoting conservation and energy efficiency. This is particularly true in today's environment. Given the Company's need to acquire resources to meet future load and given that future resource acquisition is substantially more expensive than existing resources, the Commission should design rates that will promote conservation and energy efficiency. Given that DSM is one of the Company's cheapest resources especially if it is acquired by the consumer, the Commission should make conservation and energy efficiency its primary rate design goal.

RMP's Comments

RMP thanks Mr. Higgins and Mr. Townsend for their thoughtful presentations and agrees that differences among customers with respect to cost to serve are increasingly captured by rate design rather than through different rate schedules.

GENERAL COMMENTS AND RECOMMENDATIONS

Several parties made a general comments and made general recommendation.

CCS

General Comment

The Committee appreciates the work of the Division in coordinating the presentations and topics addressed by the Working Group. In total, the presentations were informative and provided interesting information to contribute to the ongoing examination of rate design topics. However, we note that each topic was addressed in isolation, rather than examining the pros and cons of various proposals and analyzing the details of how these proposals might affect other regulatory issues and policies. In actuality, rate design can only be accomplished in the context of a rate case considering the specific facts and circumstances of the individual utility at that point in time. Rate design involves both art and science and consideration should be given to balancing multiple policy objectives. Because these broader questions were not the scope of this Working Group, the Committee believes that there should be no Commission action as an outcome of this process. In order to be considered for implementation, any of the rate design proposals or mechanisms addressed in these discussions would need to be raised, and supported by testimony and evidence, in a future rate proceeding before the Commission.

General Recommendation

The Committee's recommendations are as follows:

(1) There should be no Commission action related to any of the proposals contained in the presentations or summaries relating to the Working Group. Testimony and evidence needs to be presented to the Commission in a rate proceeding so it can appropriately examine proposals, and

associated technical and policy issues, and determine what, if any, changes in the area of rate design are in the public interest.

(2) Informational deficiencies currently exist in the area of cost of service and rate design that would benefit from a commitment by the Company to file certain studies as part of its next general rate case. Two studies conspicuously lacking at this time are a Utah Marginal Cost Study and a Shared Services Study. The Commission could advance the discussion and quality of analysis by ordering that these studies be conducted by the Company and filed with the Commission.

UCE

General Comments on Residential Rate Design

According to several presentations made to the Rate Design Group about residential rate design modifications, residential rate design that promotes efficient use of energy should include the following elements[3]:

- Simple, easy to understand design
- Large/steep differential between tiers
- Appropriate number of tiers to reflect customer usage patterns
- Keeping the majority of the price signal in the volumetric sales

These elements are necessary to send price signals to promote conservation and efficiency and to enable customers to understand rate structures and respond positively to the price signal being sent by the Company. Effective rate design is a 'no cost' mechanism to deliver additional energy savings and leverage existing DSM programs. Education and marketing is central to successful energy efficiency programs and rate design. We recommend that rate design be clearly included in customer education and marketing of DSM programs.

During the Rate Design Group meetings, a valid concern for the Company regarding the proposed residential rate design was the likelihood that, by placing more of the price signal in volumetric charges, this structure could jeopardize the Company's ability to recover fixed costs.

[3] Personal communication with Jim Lazar, RAP, January 8, 2009; Dr. Rich Collins, SWEEP, February 26, 2009.

This concern was acknowledged by the Division staff, as well as Dr. Collins and others. One mechanism to address this concern is to "decouple" the utilities revenues from its electricity sales, and allow periodic revenue adjustments to assure recovery of fixed costs.

To investigate and address barriers to more aggressive utility deployment of DSM, including the concern noted above, Utah Clean Energy recommends that a docket be opened to investigate decoupling, performance based incentives, rate design, energy savings goals, etc., within 60 days of the date that the rate design report is filed. This is consistent with the American Recovery and Reinvestment Act of 2009 (HR1), which requires that:

> *The applicable State regulatory authority will seek to implement, in appropriate proceedings for each electric and gas utility, with respect to which the State regulatory authority has ratemaking authority, a general policy that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently and that provide timely cost recovery and a timely earnings opportunity for utilities associated with cost-effective measurable and verifiable efficiency savings, in a way that sustains or enhances utility customers' incentives to use energy more efficiently.*[4]

General Recommendations

UCE's recommendations for the rate design report are below:

1. Implement a residential tiered block structure in line with that proposed by Dr. Rich Collins in his presentation and comments on February 26, 2009,
2. Within 60 days of the filing of the rate design report, open an exploratory docket to investigate and address barriers to more aggressive utility deployment of DSM, including decoupling, affirmative incentives, rate design, energy savings goals, etc.,
3. Aggressive and effective education and marketing regarding the selected rate design should be carried out in concert with Rocky Mountain Power's planned DSM marketing and communication strategy,

[4] American Recovery and Reinvestment Act of 2009 (HR 1), Section 410, pg 32, http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h1enr.pdf

4. Further analysis of rate design options for the commercial sector is needed to advance energy efficiency while balancing the needs of diverse commercial energy customers.

SLCAP and AARP

General Comment

The stated purpose of the advisory group is to "discuss and investigate rate design proposals to promote conservation and energy efficiency." However, the advisory group also heard numerous proposals designed to achieve revenue stability for utilities. AARP and SLCAP submit that such measures, which include shifting significant fixed costs on to the customer charge, are both counter to encouraging energy efficiency and inconsistent with the purpose of the advisory group.

SWEEP

General Comments

SWEEP appreciates the efforts on the part of the Division to organize and lead the Commission-ordered Task Force on innovative rate designs to promote conservation and energy efficiency. Although a consensus on rate design proposals was not reached, the task force did discuss a number of important issues and members of the task force were exposed to cogent rate design proposals that if adopted would encourage the ratemaking goals of conservation and efficient use of electricity.

General Recommendations

SWEEP recommends that the Task Force issue a report to the Commission that outlines the importance of rate designs that will promote conservation and the adoption of energy efficiency measures. The Task Force should recommend to the Commission that it explicitly request that testimony on rate design include the parties' rationale for adoption based on the goal of conservation and adoption of energy efficiency measures. The Task Force should recommend that a docket be opened to investigate the benefits and costs of a decoupling mechanism.