

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA



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Order Instituting Rulemaking to Examine the
Commission's Energy Efficiency Risk/Reward
Incentive Mechanism.

Rulemaking 09-01-019
(Filed January 29, 2009)

**THE OFFICE OF RATEPAYER ADVOCATES AND
THE UTILITY REFORM NETWORK'S PROPOSAL
TO RESOLVE RISK/REWARD INCENTIVE MECHANISM ISSUES**

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I. INTRODUCTION

Commission Decision (D.) 15-09-026¹ granted rehearing of D.08-12-059,² D.09-12-045³ and D.10-12-049⁴ and ordered the consolidated rehearing of those decisions in this docket. The Assigned Commissioner and Administrative Law Judge's Amended Scoping Memo and Ruling, issued January 22, 2016 (Scoping Memo) directed parties to submit proposals to resolve issues within the scope of this proceeding, focusing on the "the total incentive level for each utility" that will produce incentive awards that reflect energy savings independently verified by the Energy Division and produce rates that are just and reasonable.⁵ The Office of Ratepayer Advocates (ORA)⁶ and The Utility Reform Network (TURN) submit this proposal, which relies on the independently verified energy savings parameters required by D.07-09-043.⁷ Section II of this document explains the proposal. Section III summarizes the procedural history. Section IV summarizes the evaluation, measurement and verification (EM&V) process. Appendices A and B include additional procedural history and details about the EM&V process.

ORA and TURN recommend that the Commission direct refunds to ratepayers in the amounts shown below.

¹ D.15-09-026, *Order Granting Rehearing Of Decisions 10-12-049, 09-12-045 and 08-12-059 and Consolidating Rehearings, Modifying Rulemaking 09-01-019 and Denying Rehearing of Rulemaking, and Denying Request for Official Notice*, September 22, 2015, Ordering Paragraphs 4 and 5 at p. 13.

² D.08-12-059, *Decision Granting in Part and Denying in Part the Petition for Modification*, January 2, 2009.

³ D.09-12-045, *Decision Regarding RRIM Claims for the 2006-2008 Program Cycle*, December 29, 2009.

⁴ D.10-12-049, *Decision Regarding the Risk/Reward Incentive Mechanism Earnings True-Up for 2006-2008*, December 27, 2009. ORA and TURN's proposal refers collectively to D.08-12-059, D.09-12-045 and D.10-12-049 as the RRIM decisions.

⁵ Scoping Memo, p. 3. The assigned Administrative Law Judge (ALJ) subsequently revised the schedule, but otherwise left intact the approach adopted by the Scoping Memo. *Administrative Law Judge's Ruling Revising Schedule*, February 5, 2016.

⁶ ORA was also known as the Division of Ratepayer Advocates (DRA) at some points during the course of the energy efficiency proceedings described in this proposal, but for the sake of simplicity the proposal refers exclusively to ORA.

⁷ D.07-09-043, *Interim Opinion on Phase I Issues: Shareholder Risk/Reward Incentive Mechanism for Energy Efficiency Programs*, September 25, 2007.

Pacific Gas and Electric Company (PG&E)	\$104,045,62
Southern California Edison Company (SCE)	\$39,874,716
San Diego Gas & Electric Company (SDG&E)	\$13,616,957
Southern California Gas Company (SoCal Gas)	\$12,400,135

These refunds are consistent with one of the bedrock principles of the shareholder incentive mechanism for energy efficiency, which requires:

“[a]ll calculations of the net benefits and kW [kiloWatt], kWh[kilowatt hour] and therm achievements are independently verified by the Commission’s Energy Division and its evaluation, measurement and verification (EM&V) contractors, based on adopted EM&V protocols.”⁸

ORA and TURN respectfully request that the Commission adopt this proposal, which utilizes the independent evaluation of energy savings that was an absolute prerequisite to the award of shareholder incentives.

II. THE ORA/TURN PROPOSAL RELIES ON SAVINGS VERIFIED BY THE ENERGY DIVISION’S INDEPENDENT REVIEW AND THEREFORE PRODUCES RATES THAT ARE JUST AND REASONABLE

ORA and TURN’s proposal is based on the Risk/Reward Incentive Mechanism (RRIM) adopted in D.07-09-043 and revised in D.08-01-042. The proposal complies with the RRIM’s requirement that the energy efficiency savings be independently verified by the Energy Division. The appropriate basis for calculating incentives that are just and reasonable is Scenario 7, Tab 1 (S7-T1) from the the *Energy Division’s 2006-2008 Scenario Analysis Report* (Scenario Report)⁹, because that scenario uses evaluated net savings and is the only scenario that conforms to the adopted RRIM. The Energy Division evaluated the Utilities’ 2006-2008 energy efficiency savings, issuing the First Verification Report on February 5, 2009;¹⁰ the Second Verification Report in Resolution E-4272 on October 15, 2009;¹¹ and the *2006-2008 Energy Efficiency*

⁸ D.07-09-043, *Interim Opinion on Phase 1 Issues: Shareholder Risk/Reward Incentive Mechanism for Energy Efficiency Programs*, Conclusion of Law 5(3), p. 216.

⁹ The Scenario Report was appended to *Assigned Commissioner Ruling Providing Energy Report and Soliciting Comments on Scenario Runs*, May 4, 2010.

¹⁰ Appendix B-2.

¹¹ Appendix B-2.

Evaluation Report on July 26, 2010.¹² The *2006-2008 Energy Efficiency Evaluation Report* described the verified energy savings, but did not evaluate the possible award of incentives.

To evaluate possible incentive awards, Scenario Report calculated incentives for a range of scenarios. Most of those scenarios violate the adopted RRIM, including the requirement that the Energy Division independently verify energy efficiency savings.¹³

S7-T1 complies with the RRIM, as modified by D.08-01-042, by presenting the Utilities' achievements "based on net evaluated savings."¹⁴ This is the only scenario in the Scenario Report that comports with the Commission's approved methods and policy. Section 4.5 of the *2006-2008 Energy Efficiency Evaluation Report* presents the final evaluated savings compared to the adopted savings goals. Table 25 on page 101 of Section 4.5, reproduced in Appendix B-3 of this proposal, presents the energy efficiency savings goals for each metric and for each utility, and a full accounting of the components of energy savings that count towards each utility's goal. The components of utility savings include evaluated savings accomplishments between 2004 and 2008, 50% of evaluated codes and standards savings, and adjusted Low Income Energy Efficiency program savings. The results in Table 25 in the *2006-2008 Energy Efficiency Evaluation Report*, which represent the final evaluated statement of energy savings, is identical to the data presented in S7-T1. ORA and TURN's proposal is therefore based on S7-T1, with the following two exceptions:

1. Energy Division calculated the true-up in S7-T1 by determining the total earnings allowed based on the evaluated net savings and subtracting the incentives awarded to each utility in D.08-12-059 and D.09-12-045. S7-T1 did not account for incentives granted by D.10-12-049, because the Scenario Report was completed prior to the Commission's adoption of D.10-12-049. ORA and TURN recalculated the final award of incentives to the Utilities by using the S7-T1 evaluated net savings and subtracting the interim incentives that would have been awarded on the basis of the Energy Division First and Second Verification Reports.
2. S1-T7 did not account for the Commission's order in D.08-01-42, Ordering Paragraph 2(b), which allows the Utilities to retain interim earnings and

¹² Filed in R.09-01-019 by Energy Division on July 26, 2010 pursuant to the ALJ's July 21, 2010 Ruling.

¹³ D.07-09-043, Conclusion of Law 5(e), p. 216; Scenario Report, p. 1 ("The scenarios presented as alternatives to Scenario 7 are provided as information only and are not endorsed by Energy Division as appropriate for determining shareholder earnings.").

¹⁴ Scenario Report, p. 1.

continue to earn incentives on the *ex post* performance earnings basis (PEB)¹⁵ if the utility met the minimum performance standard (MPS)¹⁶ based on its interim earnings claims, but the final true-up calculation results in the utility meeting less than 80% for any individual savings metric or less than 85% for the average savings threshold, but greater than 65% of the Commission's goals for each individual metric. As ORA and TURN describe in more detail below, the proposed refund is net of what the Utilities would have earned in the first and second interim payments had the Commission granted earnings in accordance with the adopted RRIM rules. Thus, ORA and TURN's proposal calculates final awards of incentives for SCE and SoCalGas that are higher than the final award of incentives calculated by the Energy Division. The final award of incentives for SDG&E and PG&E are unchanged. PG&E's incentives remain at zero, because PG&E did not achieve higher than 65% on the Commission adopted MW goal on an *ex-post* basis.

The steps required calculate incentives pursuant to the RRIM¹⁷ as adopted in D.07-09-043 and modified by D.08-01-042 are summarized below.

1. First interim incentives based on *ex ante*¹⁸ or forecasted energy savings and demand reduction, and verified (or *ex post*) measurements of the number of energy efficiency measures installed and their cost, less 35% hold back;
2. Second interim incentives based on *ex ante* or forecasted energy savings and demand reduction, and verified (or *ex post*) measurements of the number of energy efficiency measures installed and their cost, less 35% hold back;
 - a. payment of the first interim incentives is subtracted from the calculation of the second interim incentives;
3. Final true-up payment based on the Energy Division's true up using verified energy savings and demand reductions using *ex post* measurements with the caveat that Utilities were allowed to keep the interim incentives and continue earning at the 9% rate as long as the final verified savings exceeded 65% of the Commission's goals;

¹⁵ As explained in Section III A 1 at page 12, the PEB was dollar value of a utility's energy efficiency portfolio's net benefits. Net benefits were the portfolio resource savings minus costs.

¹⁶ As explained in Section III A 1 at page 12, the RRIM included a an MPS; for each utility's portfolio of energy efficiency activities. SDG&E, PG&E and SCE shareholders would receive incentives for achieving no less than a 85% average of the Commission's kilowatt hour (kWh), kilowatt (kW) and therm goals, and if no individual savings metric achieved less than 80% of those goals. The RRIM required SoCalGasto meet an MPS of 80% of its therm savings goal to be eligible for incentives

¹⁷ Please see Section III A 1, pp. 12-13, for a more detailed description of the RRIM.

¹⁸ The tension between the use of *ex ante* and *ex post* measurements was at the heart of nearly all RRIM disputes. *Ex ante* means parameters (including number of energy efficiency measures installed, amount of energy savings per measure, and the amount of demand reduction per measure) predicted at the outset of the program. *Ex post* applies to those same parameters measured and verified after the completion of the program. Thus, *ex ante* and *ex post* numbers will almost certainly differ, just as any real world forecast is likely to differ from the actual event.

- a. both the first and second interim claim incentive payouts would be subtracted from the final claim calculations incentives calculation to establish the final payout amount,
- A. The first interim incentives should have been \$2,886,293 rather than \$82,200,000.**

To ensure that “all money awarded”¹⁹ by the RRIM decisions was just and reasonable, ORA and TURN calculated the incentives for each of the two interim incentives claims and the final true-up claim using the Energy Division’s EM&V results in accordance with the RRIM adopted in D.07-09-043 and modified in D.08-01-042. The Energy Division’s first verification report calculated incentives based on the verified costs and installations of the energy efficiency program activities and updates to the *ex-ante* parameters for estimating program savings and benefits in accordance with the RRIM adopted in D.07-09-043 and modified by D.08-01-042.²⁰ The Energy Division’s First Verification Report calculated incentives of \$2,886,293 for SoCalGas net of the 35% hold back required by D.08-01-042. SoCalGas was the only utility that qualified for incentives according to the Energy Division’s First Verification Report.

Table 1: Allowable incentives based on the First Verification Report

	1st Interim Incentives	35% Holdback	1st Interim Incentives Net of Holdback
PG&E	\$0	\$0	\$0
SCE	\$0	\$0	\$0
SDG&E	\$0	\$0	\$0
SoCalGas	\$4,440,451	\$1,554,158	\$2,886,293
TOTAL	\$4,440,451	\$1,554,158	\$2,886,293

Decision 08-12-059 granted a total of \$82,200,000 for the first interim claim based on the Utilities’ unverified self-reported savings.²¹

¹⁹ D.15-09-026, Ordering Paragraph 6, p. 13.

²⁰ Energy Division First Verification Report, p. 11.

²¹ D.08-12-059, p. 2.

Table 2: Incentives granted by D.08-12-059

Utility	
PG&E	\$41,500,000
SCE	\$24,700,000
SDG&E	\$10,800,000
SoCalGas	\$5,200,000
TOTAL	\$82,200,000

B. The second interim incentives should have been \$92,674,418 rather than \$61,494,555.

The Energy Division calculated the second interim incentives as shown in the Energy Division's Second Verification Report, which used the verified costs and installations of the energy efficiency program activities and updates to the *ex-ante* parameters in accordance with the RRIM as modified by D.08-01-042. The Commission adopted Resolution E-4272, approving the Energy Division's Second Verification Report in October 2009.²²

The total amount of the second interim incentives as determined by the Energy Division's Second Verification Report was \$147,016,478. Net of the 35% hold-back required by D.08-01-042, the second interim incentives totaled \$95,560,711. Incentives were based on cumulative savings and net benefits, so the amount of SoCalGas's first interim incentives should be subtracted from the calculation of its second interim incentives.²³ SoCalGas should have received \$1,907,179 rather than \$4,793,472. Since the Energy Division's First Verification Report calculated that PG&E, SCE and SDG&E were not entitled to first interim incentives it was not necessary to net their first interim incentives against their second interim incentives.

²² Resolution E-4272, Table ES1c, p. 15.

²³ See Section III A.1, p. 13 for a more detailed description of the interim claims process.

Table 3: Allowable incentives based on the First and Second Verification Reports

	1st Interim Incentives	2nd Interim Incentives	Hold-back	2nd Interim Incentives Net of Holdback and 1st Interim Incentives
PG&E	\$0	\$86,458,401	\$30,260,440	\$56,197,961
SCE	\$0	\$53,183,505	\$18,614,227	\$34,569,278
SDG&E	\$0	\$0	\$0	\$0
SoCalGas	\$2,886,293	\$7,374,572	\$2,581,100	\$1,907,179
TOTAL	\$2,886,293	\$147,016,478	\$51,455,767	\$92,674,418

In comparison to the incentives calculated using the Energy Division Second Verification Report, D.09-12-045 granted a total of \$61,494,555 to the Utilities. The basis for the Commission’s award was the Energy Division Second Verification Report with the following additional adjustments:²⁴

- (1) Exclusion of the cumulative effects of 2004-2005 savings goals.
- (2) Adjustment of the savings goals to recognize interactive effects that were not originally considered in setting 2006-2008 goals.
- (3) Adjustment of the shared savings rate to 12% based on the use of the Utilities’ proposed unmodified *ex ante* assumptions.
- (4) Adjustment of the Net to Gross ratio for SCE’s residential lighting program.
- (5) Adjustment of the realization rate applied to SDG&E’s Energy Savings BID program and SoCal Gas’ Local Business Energy Efficiency program.

The RRIM adopted in D.07-09-043 and modified by D.08-01-042 did not include these adjustments. Therefore, in order to be consistent with the RRIM adopted and modified in those two decisions, ORA and TURN’s proposal excludes these adjustments.

²⁴ D.09-12-045, p. 3.

Table 4: Total incentives granted by D.08-12-059 and D.09-12-045 for the First and Second Interim Claims

Utility	D.08-12-059	D.09-12-045	TOTAL
PG&E	\$41,500,000	\$33,430,614	\$74,930,614
SCE	\$24,700,000	\$25,652,348	\$50,352,348
SD&GE	\$10,800,000	\$300,572	\$11,100,572
SoCalGas	\$5,200,000	\$2,111,021	\$7,311,021
TOTAL	\$82,200,000	\$61,494,555	\$143,694,555

C. The correctly calculated total award of RRIM incentives is \$41,915,644 and not \$211,853,077.

To true-up the total award of incentives for each of the Utilities, the Energy Division used scenario S7-T1 of the Scenario Report, which reflects the RRIM adopted in D.07-09-043 and modified by D.08-01-042. Scenario S7-T1 uses evaluated net savings and is the only scenario that conforms to the adopted RRIM. As shown below in Table 5, under S7-T1, the total award of RRIM incentives for all Utilities combined should be \$41,915,644. This amount is based on the allowable incentives of \$30,247,472 calculated from the evaluated net savings, but includes the first and second interim incentives that the Utilities are entitled to retain pursuant to D.08-01-042, Ordering Paragraph 2b. PG&E, however, failed to exceed the 65% minimum threshold required to retain incentives.²⁵

Table 5: Allowable incentives based on the final true-up scenario S7-T1

RRIM Incentives Based on D.07-09-043 and D.08-01-042

	1st Interim Incentives	2nd Interim Incentives	Scenario S7-T1	ORA/TURN Proposed Incentives
PG&E	\$0	\$56,197,961	\$0	\$0
SCE	\$0	\$34,569,278	\$26,936,490	\$34,569,278
SDG&E	\$0	\$0	\$2,552,894	\$2,552,894
SoCalGas	\$2,886,293	\$1,907,179	\$758,088	\$4,793,472
TOTAL	\$2,886,293	\$92,674,418	\$30,247,472	\$41,915,644

The Commission granted incentives of \$68,158,522 in D.10-12-049, resulting in total incentives of \$211,853,077 for the 2006-2008 energy efficiency program cycle. The total incentives, and the incentives awarded in each of the decisions for which rehearing was granted are shown in Table 6.

²⁵ D.08-01-042, Ordering Paragraph 2(b), p. 24.

Table 6: Total incentives granted by the RRIM decisions

Utility	D.08-12-059	D.09-12-045	D.10-12-049	Total Incentives Granted by Commission
PG&E	\$41,500,000	\$33,430,614	\$29,115,011	\$104,045,625
SCE	\$24,700,000	\$25,652,348	\$24,091,646	\$74,443,994
SDG&E	\$10,800,000	\$300,572	\$5,069,279	\$16,169,851
SoCalGas	\$5,200,000	\$2,111,021	\$9,882,586	\$17,193,607
TOTAL	\$82,200,000	\$61,494,555	\$68,158,522	\$211,853,077

D. The Commission should require refunds totaling \$169,937,433 in order to complete the implementation of the RRIM adopted in D.07-09-043 and modified by D.08-01-042.

As explained above, the RRIM decisions awarded incentives that failed to comply with the RRIM adopted in D.07-09-043 and modified by D.08-01-042. The Commission granted incentives in excess of the amount allowed if the Commission adhered to the rules and policies it had established for the RRIM.

The Commission’s RRIM, which requires utilizing the Energy Division’s EM&V process, results in a total combined incentives of \$41,915,644 for SCE, SDG&E, and SoCalGas based on verified energy savings. Because the Utilities have already received incentives in excess of the amount calculated using the energy savings verified by the Commission’s EM&V process, ORA and TURN recommend that the Commission require refunds as follows.

SCE	\$39,874,716
SDG&E	\$13,616,957
SoCalGas	\$12,400,135
PG&E	\$104,045,625

Because PG&E failed to achieve 65% of the adopted energy savings MW goal, the Commission should require PG&E to refund the entire amount of incentives awarded by the RRIM decisions.²⁶

ORA and TURN present two options for returning the excess incentives to ratepayers: The Commission should require the Utilities to refund the excess incentives, including interest, to their customers as either (1) a revenue credit to customers’ distribution and gas transportation accounts, as described in pages 166 and 167 of D.07-09-043; or (2) as a line item to the

²⁶ D.08-01-042, Ordering Paragraph 2(b), p. 24.

customers' first monthly bill following the issuance of a decision resolving RRIM issues. TURN has issued data requests to the Utilities regarding the potential bill impact of the second option, and ORA and TURN will provide additional information in support of the preferred recommendation in their reply comments.

Table 7: ORA and TURN Recommended Refunds

	Total Incentives Granted by Commission	ORA/TURN Proposed Incentives	Proposed Refunds
PGE	\$104,045,625	\$0	\$104,045,625
SCE	\$74,443,994	\$34,569,278	\$39,874,716
SDGE	\$16,169,851	\$2,552,894	\$13,616,957
SCG	\$17,193,607	\$4,793,472	\$12,400,135
TOTAL	\$211,853,077	\$41,915,644	\$169,937,433

III. PROCEDURAL HISTORY

Decision 08-12-059, D.09-12-045, and D.10-12-049 awarded nearly \$212 million²⁷ to the Utilities for their performance in administering energy efficiency programs from 2006 to 2008, as part of the RRIM adopted in D.07-09-043. The nearly \$212 million in shareholder incentives were in addition to the Utilities' full cost recovery for their energy efficiency programs.²⁸ Decision 15-09-026 recognized that the award of incentives failed to comply with the RRIM, including the key requirement that the ratepayers only pay incentives for independently verified savings.²⁹ Decision 15-09-026 therefore directed the rehearing of the RRIM decisions to ensure that "all money awarded" by the RRIM decisions was "just and reasonable and based on calculations verified by the Commission, via its Energy Division, pursuant to the directives and process adopted in Rulemaking 06-04-010 and Rulemaking 09-01-019, as modified."³⁰

²⁷ The Commission's award of incentives to the Utilities for the 2006-2008 program totaled \$211,853,077. D.10-12-049, p. 2.

²⁸ D.05-09-043, *Interim Opinion: Energy Efficiency Portfolio Plans and Program Funding Levels for 2006-2008 – Phase 1 Issues*, p. 4, Conclusion of Law 6, p. 184 ("The level of program funding proposed by the utilities over the three-year program cycle, as well as their proposed cost allocation and associated ratemaking treatment, is reasonable and supported by the record.")

²⁹ D.07-09-043, Conclusion of Law 5(e), p. 216.

³⁰ D.15-09-026, Ordering Paragraph 6, p. 13.

A. D.07-09-043 adopted the RRIM to encourage superior performance in saving energy and maximizing net resource benefits.³¹

The Commission adopted the RRIM in D.07-09-043, following a series of earlier decisions and policies that:

- (1) recognized the importance of energy efficiency as a resource for combating climate change and meeting California’s energy needs;³²
- (2) established energy savings goals for gigawatt hours (GWh), megawatts (MW) and therms for 2004-2013, subject to update for 2009 and beyond;³³
- (3) concluded that the Utilities, as part of their overall obligation to procure resources, should administer energy efficiency programs;³⁴
- (4) determined that energy efficiency savings must be independently verified in order to produce meaningful results for procurement planning;³⁵
- (5) found that a shareholder incentive mechanism was necessary in order to encourage the Utilities to place energy efficiency on the same footing as supply-side resources;³⁶ and
- (6) adopted the Utilities’ proposed energy efficiency budgets totaling \$1,968,762,439 for the 2006-2008 program cycle.³⁷

The Commission explained in D.07-09-043 that the RRIM included features designed to promote energy efficiency as a resource, while balancing the interests of shareholders and ratepayers. Decision 07-09-043 established the following principles of the RRIM:

“[E]arnings to shareholders accrue only when utility portfolio managers produce positive net benefits (savings minus costs) for ratepayers.”

³¹ D.07-09-043, p. 108.

³² D.04-09-060, *Interim Opinion: Energy Savings Goals for Program Year 2006 and Beyond*, September 29, 2004, p. 22 (discussing the Energy Action Plan and prior Commission decisions).

³³ D.04-09-060, adopting annual and cumulative goals for electric and natural gas savings for the Utilities as shown in Tables 1A to 1E. “The annual numbers represent the annual GWh and megawatt (MW) savings achieved by the set of programs and measures implemented in that specific program year. The cumulative numbers represent the annual savings from energy efficiency program efforts up to and including that program year.” D.04-09-060, p. 10.

³⁴ D.05-01-055, *Interim Opinion on the Administrative Structure for Energy Efficiency: Threshold Issues*, February 3, 2005, Conclusion of Law 1, p. 152; Ordering Paragraph 1, p. 154.

³⁵ D.05-01-055, p. 112. Section III C and Appendices B-1 and B-2 of this proposal describe the Commission’s EM&V process that began even prior to that decision.

³⁶ D.05-01-055, p. 91.

³⁷ D.05-07-093, *Interim Opinion: Energy Efficiency Portfolio Plans and Program Funding Levels For 2006-2008 – Phase 1 Issues*, September 27, 2005, p. 4.

“[E]arnings begin to accrue only as the utilities reach to meet and surpass the Commission’s kWh [kilowatt-hour], kW [kilowatt] and therm savings goals.”

“Earnings are greatest when performance is superior, not just ‘expected.’”

“All calculations of the net benefits and kW, kWh and therm achievements are independently verified by the Commission’s Energy Division and its evaluation, measurement and verification (EM&V) contractors, based on adopted EM&V protocols.”³⁸

1. RRIM

The overarching premise of the RRIM was that the Utilities would design and implement energy efficiency programs to reduce energy demand and consumption, while shareholders and ratepayers would share any benefits that exceeded the Commission’s adopted saving thresholds. The RRIM included an MPS for each utility’s portfolio of energy efficiency activities.³⁹ SDG&E, PG&E and SCE shareholders would receive incentives under the RRIM if the utility’s portfolio achieved no less than an 85% average of the Commission’s kWh, kW and therm goals, and if no individual savings metric achieved less than 80% of those goals.⁴⁰ The RRIM required that SoCalGas meet an MPS of 80% of its therm savings goal to be eligible for incentives. SoCalGas’s lower MPS reflected the higher risk SoCalGas faced in meeting the MPS, since SoCalGas’s portfolio of energy efficiency programs included only gas programs, which saved therms but not kWh or kW.⁴¹

Once a utility’s portfolio met the MPS, the RRIM entitled shareholders to a portion of the portfolio’s net benefits, defined as portfolio resource savings minus costs. The dollar value of the portfolio’s net benefits was the RRIM’s PEB.⁴² If a utility achieved the MPS, its shareholders would receive 9% of the portfolio PEB. If a utility achieved 100% or more of the Commission’s savings goal(s), its shareholders would receive 12% of the net benefits.⁴³ If a

³⁸ D.07-09-043, p. 4. These four aspects of the shareholder incentive mechanism were among nine that the Commission adopted (emphasis in original); see also Conclusion of Law 5 at pp. 215-215.

³⁹ D.07-09-043, p. 22.

⁴⁰ D.07-09-043, pp. 27-28; Ordering Paragraph 2(a), p. 219.

⁴¹ D.07-09-043, p. 28, Ordering Paragraph 2(b), p. 219.

⁴² D.07-09-043, pp. 19-20.

⁴³ D.07-09-043, Ordering Paragraph 2(e), p. 220.

utility achieved more than 65% but less than 85% of the Commission’s savings goals, the utility’s performance would be in the RRIM’s deadband, and shareholders would neither receive incentives nor be subject to penalties.⁴⁴ If a utility achieved 65% or less of the Commission’s savings goals for kWh, kW or therms, the RRIM provided that the utility would be subject to penalties.⁴⁵

To provide timely feedback to the Utilities for their performance in achieving energy efficiency savings, and to “produce a stream of earnings during and at the end of the program to provide ongoing incentives to the [U]tilities,” the RRIM included two interim incentive payouts as well as one final true-up claim.⁴⁶ The earnings payouts were based on cumulative savings⁴⁷ and net benefits, so payment of the first interim claim would be subtracted from the calculation of the second interim claim earnings, and both the first and second interim claim payouts would be subtracted from the final claim calculations to establish the final payout amount.⁴⁸ Decision 07-09-043 included a 30% “hold-back” from the interim payouts of earnings and provided that if the final true-up determined that a utility had been overpaid by the interim claims, the over payment would be treated as a debit to offset future incentive earnings.⁴⁹

2. Independent verification of energy savings and demand reduction was a cornerstone of the RRIM.

Decision 05-01-055, which established the current administrative structure for energy efficiency in which the Utilities select the portfolios and the Energy Division is responsible for EM&V, explained why independent measurement of energy savings is so important:

“EM&V serves both as the quality control mechanism for ratepayer funded energy efficiency programs and as a data input for IRP [Integrated Resource Planning] and the portfolio planning process. Rigorous, reliable EM&V is crucial to California’s ability to attain its energy efficiency goals for three interrelated reasons.

⁴⁴ D.07-09-043, p. 29; Ordering Paragraph 2(e) and (f), p. 220.

⁴⁵ D.07-09-043. Ordering Paragraph 2(f), p. 220. D.07-09-043 capped earnings and penalties at \$450 million over each three-year program cycle for the four Utilities combined. Ordering Paragraph 2(g), p. 221.

⁴⁶ D.07-09-043, p. 124.

⁴⁷ D.07-09-043 provided that incentives would be based on cumulative achievements. D.07-09-043, p. 5 fn 6.

⁴⁸ D.07-09-043, Ordering Paragraph 4, p. 221.

⁴⁹ D.07-09-043, Ordering Paragraph 2(e), p. 220.

“First, IRP requires independent EM&V. EM&V plays a determinative role in the reliability of energy efficiency savings. For energy efficiency to be considered a reliable resource in IRP, such that EE [energy efficiency] is taken seriously along side steel-in-the-ground resource by the IOU resource portfolio planners, California must have an EM&V framework designed to generate accurate and reliable data. Conflicts of interest that encourage compromised EM&V of programs jeopardize the success of IRP.

“Second, Independent EM&V ensures that ratepayers get the energy efficiency for which they pay. California needs an EM&V framework bold enough to prevent wasteful expenditures of ratepayer money on energy efficiency programs. Ratepayers should reap the benefits of the energy efficiency programs they fund. These ratepayer benefits should include well-run, effective energy efficiency programs, resultant lower customer bills, and increasing utility use of energy efficiency as a demand-side resource. Ratepayers deserve an administrative structure that gives them a reasonable assurance that their money is being wisely and efficiently expended.

“Finally, independent EM&V enables the program selector to assemble the strongest portfolio of programs. EM&V must be as transparent and independent as possible to ensure that the best program designs are adopted and that the best program implementers are selected. An EM&V structure that does not completely shield EM&V studies from potential conflicts of interests undercuts California’s ability to reach our energy savings potential.”⁵⁰

To implement the administrative structure of D.05-01-055, D.07-09-043 provided that the Utilities would design energy efficiency programs using forecasted (*ex ante*) data for the number of measures installed, and the expected energy savings and reduced demand, but that the award of incentives would rely on the Energy Division’s independent verification (*ex post*) of actual installations and savings.⁵¹

EM&V of the 2006-2008 energy efficiency portfolios was an enormous undertaking. The portfolios contained hundreds of installed energy efficiency measures. For each measure, there were parameters that were required to be known or estimated in order to calculate the energy savings. For example, the parameters needed to calculate savings from compact florescent lamps (CFLs)⁵² included the wattage of the efficient lamp, the wattage of the lamp being replaced, the hours of operation, the installation rate (to take into account the fact

⁵⁰ D.05-01-055, pp. 112-113, citing comments filed by TURN.

⁵¹ D.07-09-043, p. 114.

⁵² CFLs were the energy efficiency measure that received the lion’s share of ratepayer funding.

customers may buy bulbs that are not immediately installed), and whether customers would have purchased the bulbs in the absence of the energy efficiency programs.⁵³

3. Decision 07-09-043 required verification of the Utilities' energy savings using *ex post* measurements to true-up the interim claims and payments.

Decision 07-09-043 provided that the interim incentives would be calculated with:

1. the *ex ante* parameters used to forecast energy savings and demand reduction, and
2. verified (or *ex post*) measurements of the number of energy efficiency measures installed and their costs.⁵⁴

Following completion of the program cycle, the Energy Division would evaluate each utility's third and final claim, verifying measure installations and program expenditures as it had for the interim claims, but using *ex post* measurements (rather than the *ex ante* estimates used for interim claims) to "true up" the actual energy savings. This final true-up would evaluate whether the Utilities had achieved the MPS for the full three-year program and would calculate the Utilities' PEB net benefits using *ex post* measurements.⁵⁵ The two interim payments would be true-up after the *ex post* evaluation determined actual demand reduction and energy savings consistent with established EM&V protocols.⁵⁶

⁵³ "In the context of energy efficiency, "free riders" are those program participants who would have undertaken the energy efficiency activity in the absence of the program. We adjust program savings to remove the effect of free riders because their participation would have happened anyway, and therefore the savings associated with their actions cannot be considered a benefit of the program." D.07-09-043, p. 13, fn 12.

⁵⁴ D.07-09-043, pp. 114-15; 116 (Energy Division staff verify utility reported information regarding number of installations and their costs as part of the interim verification process, but "per-measure savings for interim claim are still based on expected or estimated (*ex ante*) savings for each of the interim claims.")

⁵⁵ D.07-09-043, p. 115.

⁵⁶ D.07-09-043, p. 116 ("For the final 'true-up' claim, the achievements considered at that time reflect the results of the Final Verification and Performance Basis Report, that is, the *ex post* results of all performance parameters evaluated by Energy Division and its consultants for the program cycle;" p. 119; "it is not until the final true-up claim that we will be able to determine the level of net benefits (PEB) and MW, GWh and MTherm savings produced by the energy efficiency portfolio over the three-year period, based on all the EM&V activities undertaken for that program cycle;" Ordering Paragraph 4, p. 221.

Relying on *ex post* measurements would ensure that ratepayers paid incentives to shareholders for real savings, rather than forecasted savings that did not materialize.⁵⁷ Relying on *ex post* measurements was also intended to decrease the temptation for the Utilities to use inflated savings estimates in order to obtain higher incentives.⁵⁸ Finally, the final true-up process would help ensure that energy efficiency produced “sizable GWh, MW and MMtherm [megatherm] savings that resource planners can depend upon now and in the future.”⁵⁹

B. Decision 08-01-042⁶⁰ modified the final-true-up process, but did not otherwise revise the requirement that incentives be based on independently verified savings using *ex post* measurements.

Shortly after D.07-09-043 adopted the RRIM, the Utilities filed a petition for modification⁶¹ requesting that the Commission revise the final true-up provisions of the RRIM to eliminate the requirement to return interim payments based on the final true-up, as long as the *ex post* results showed that portfolio performance fell within the deadband range or higher.⁶²

ORA and TURN opposed the Utilities’ First PFM. ORA pointed out that the requested relief would significantly modify the RRIM

“in favor of utility shareholders by effectively lowering the threshold at which utility shareholders can earn incentives on energy efficiency savings. Granting the requested relief would allow shareholders to earn 9% of net energy efficiency savings, as long as the Utilities’ energy efficiency savings exceeded 65% of the Commission’s energy efficiency goals rather than 80 to 85% of those goals, as envisioned by D.07-09-043.”⁶³

⁵⁷ D.07-09-043, Conclusion of Law 5(e), p. 216.

⁵⁸ D.07-09-043, Findings of Fact 109 and 111, p. 204.

⁵⁹ D.07-09-043, p. 121.

⁶⁰ D.08-01-042, *Interim Opinion: Joint Petition for Modification of Decision 07-09-043*, February 1, 2008.

⁶¹ *Petition for Modification of Decision 07-09-043 by Pacific Gas and Electric Company (U 39 M), Southern California Edison Company (U 338 E), San Diego Gas & Electric Company (U 902 M), and Southern California Gas Company (U 904 G)*, as amended November 7, 2007 (Utilities’ First PFM).

⁶² First PFM, p. 15.

⁶³ *Response of the Division of Ratepayer Advocates to Amended Petition for Modification of Decision 07-09-043 by Pacific Gas and Electric Company, Southern California Edison Company, San Diego Gas & Electric Company and Southern California Gas Company*, November 30, 2007 (ORA Response to Utilities’ First PFM), p. 2; *see also* Response of The Utility Reform Network to the Amended Petition for Modification of Decision 07-09-043 by Pacific Gas and Electric Company, Southern California Edison Company, San Diego Gas & Electric Company and Southern California Gas Company, November 30,

(continued on next page)

TURN pointed out that the request to revise the RRIM so that MPS achievement would be calculated using *ex ante* estimates that “best reflect the available information at the time of program filing” was impermissibly vague and likely to encourage more gaming and disputes.⁶⁴ ORA noted that granting the Utilities’ requested relief would mean that as long as the Utilities met their MPS using verified installation measures and costs, they would continue to earn incentives at the 9% rate, even if the final EM&V results revealed energy savings as low as 65.1% of the Commission’s adopted goals.⁶⁵

The Commission revised the final true-up provisions of D.07-09-043 as requested in the Utilities’ First PFM, but increased the hold back of interim earnings from 30% to 35%.⁶⁶ In response to TURN’s comments about the Utilities’ impermissibly vague request to use *ex ante* estimates that “best reflect the available information at the time of program filing,” D.08-01-042 specified exactly which *ex ante* estimates would be used to calculate interim claims, including the requirement that:

“For measures contained in the Database for Energy Efficient Resources (DEER),⁶⁷ the 2008 and 2009 DEER updates of *ex ante* measure savings parameters, including net-to-gross ratios and expected useful lives. The 2008 DEER update shall apply to the 1st Claim and the 2009 DEER update shall apply to the 2nd Claim.”⁶⁸

While D.08-01-042 modified the true-up requirements, clarified the *ex ante* parameters used to calculate interim claims, and increased the interim payment hold back from 30% to 35%, it did not eliminate the requirement that the final payment of RRIM incentives required the use of independently verified savings. Decision 15-09-026 did

(continued from previous page)

2007 (TURN Response to Utilities’ First PFM), p. 7 (granting the request relief would “would dismantle the careful balance between ratepayer and shareholder interests the Commission sought to reflect” in the RRIM.)

⁶⁴ TURN Response to Utilities’ First PFM, pp. 10-13, citing Utilities’ First PFM, p. 14.

⁶⁵ ORA Response to Utilities’ First PFM, p. 6.

⁶⁶ D.08-01-042, Ordering Paragraph 2(a), p. 23.

⁶⁷ DEER is a database that contains values for energy savings parameters, including net-to-gross ratios and expected useful lives. “DEER is developed jointly by th[e] Commission and the California Energy Commission and funded by ratepayers.” D.08-01-042, p. 16.

⁶⁸ D.08-01-042, Ordering Paragraph 3(b), p. 29.

not modify D.07-09-043 or D.08-01-042, so taken together, D.07-09-043 and D.08-01-042 provide the basis for determining RRIM payments.

C. The EM&V process for the review of energy savings parameters adhered to the adopted technical protocols and provided numerous opportunities for stakeholders and parties to comment.

As detailed below, the Energy Division followed established protocols for the EM&V process required by D.07-09-043:

“a specific and adequate process by which parties can submit questions, concerns and comments to both Energy Division and evaluation contractors. Conferences and the submission of written comments based on conferences, allow parties to participate in the process by raising and discussing issues. This takes place in formulating the several reports before they are finalized: the draft Verification Report, the draft final evaluation reports, and the draft Final Performance Basis Report.”⁶⁹

1. The Energy Division’s EM&V Process adhered to Commission Directives and established EM&V Protocols.

The foundation of the Energy Division’s impact evaluations was the Evaluator Protocols, adopted by ALJ ruling on April 25, 2006.⁷⁰ The Evaluator Protocols were intended to guide the planning and implementation of energy efficiency program evaluations by specifying the minimum acceptable evaluation approaches to be used for individual program evaluations, while providing flexibility to Energy Division project managers to use additional methods that would provide reliable evaluation results using the most cost-efficient approaches available.⁷¹ The Energy Division’s individual program evaluations were used to develop the *ex post* savings results in the *2006-2008 Energy Efficiency Evaluation Report*. Each of the final evaluation reports, listed on page 11 of the *2006-2008 Energy Efficiency Evaluation Report*, described how the evaluation study design complied with the Evaluator Protocols. The Energy Division followed the established technical protocols in planning and implementing the individual evaluations used to develop *ex post* savings parameter updates. The Evaluator Protocols were

⁶⁹ D.07-09-043, pp. 131-132.

⁷⁰ *Administrative Law Judge’s Ruling Adopting Evaluators’ Protocols for the Evaluation of Energy Efficiency Programs*, issued April 25, 2006 in R.06-04-010.

⁷¹ *Assigned Commissioner’s Ruling Establishing Schedule for Addressing High Priority Issues During 2004, and Notice of Workshop on Administrative Structure*, February 6, 2004, pp. 7-8. Rulemaking 01-08-028.

developed with the full participation of parties, including the Utilities and were ultimately adopted by the assigned ALJ.⁷²

2. The Energy Division followed the Commission's adopted procedures for providing the opportunity to review and comment on the 2006-2008 Energy Efficiency Evaluation Report and its underlying assumptions.

As summarized below and explained in more detail in Appendices B-1 and B-2 of this proposal, there were numerous opportunities for parties to participate in the development of the underlying EM&V protocols, as well as the actual impact studies that measured energy savings from the Utilities' energy efficiency portfolios.

Decision 08-12-059 required a review of the Energy Division Verification Report on 2006 and 2007 energy efficiency activities through a Commission Resolution. An October 20, 2008 ALJ ruling directed the Energy Division to issue the report on January 15, 2009. On January 15, 2009, the Director of the Energy Division requested that the Executive Director of the Commission grant a three week extension for issuance of the report to allow additional review due to the controversial nature of the subject matter.⁷³ On January 29, 2009, the Commission adopted the Order Instituting Rulemaking (OIR) 09-01-019 for the current proceeding. The OIR suspended the schedule for the Energy Division Verification report covering energy efficiency activities from 2006 through 2008, noting that D.08-12-059 had awarded incentives for 2006-2007. The Energy Division finalized the Verification report and notified the R.06-04-010 service list of its availability on February 5, 2009.⁷⁴

On July 30, 2009, the assigned ALJ issued a ruling ordering the issuance of the Second Energy Division Verification Report by Draft Resolution, with a provision for parties to file comments.⁷⁵ The ruling noted that the use of the second Energy Division Verification Report for calculating the Utilities' incentives remained unresolved as a result of ongoing disputes, but that

⁷² *Administrative Law Judge's Ruling Adopting Evaluators' Protocols for the Evaluation of Energy Efficiency Programs*, issued April 25, 2006 in R.06-04-010.

⁷³ Appendix B-2; and ORA TURN workpapers available at <http://ora.ca.gov/RRIMRehearing.aspx>

⁷⁴ Appendix B-2, Email from Tim Drew Mon 12/1/2008 11:05 AM; and ORA TURN workpapers available at <http://ora.ca.gov/RRIMRehearing.aspx>

⁷⁵ *Administrative Law Judge's Ruling Regarding Issuance of the Energy Division Verification Report*, July 30, 2009.

the Commission nevertheless needed the Second Energy Division Verification Report on the record in order to resolve any disputes. On August 6, 2009 the Energy Division distributed the Draft Second Interim Verification Report for comments via Draft Resolution E-4272.⁷⁶ In addition to written comments on Draft Resolution E-4272, a September 3, 2009 ALJ ruling provided notice of an Energy Division facilitated workshop on September 16, 2009, providing all stakeholders with the opportunity to discuss the draft Verification Report in person, pursuant to procedures set forth in Attachment 7 to D. 07-09-043.⁷⁷

As required by Attachment 7 to D.07-09-043, on November 3, 2009, the Energy Division staff notified the R.06-04-010 service list and other interested parties of the public review period for the 2006-2008 evaluation reports.⁷⁸ The notification and the schedule for written comments and workshops covering the Energy Division's technical evaluation reports are explained in Appendices B-1 and B-2 of this proposal.

Energy Division received more than 1,700 comments from the Utilities and other stakeholders on the technical evaluation reports, which the Energy Division and its consultants considered for adjustments to the evaluation reports. Additionally, the Energy Division responded to multiple data requests from the Utilities and stakeholders requesting the underlying data and related information in order to inform comments on the technical evaluation report results.⁷⁹ The Energy Division finalized the technical evaluation reports in February 2010. Pages 11-13 of the Energy Division 2006-2008 Energy Efficiency Evaluation Report provides the internet locations for Energy Division's technical evaluation reports and appendices (48 documents in all).

Assigned Commissioner John Bohn issued an April 8, 2010 ruling that included the opportunity to comment on the Energy Division's "Evaluation Reporting Tools/Database" (ERT) and the RRIM calculator for determining the true-up of incentive earnings.⁸⁰ Assigned Commissioner Bohn issued a subsequent ruling on May 4, 2010 providing the Energy Division's

⁷⁶ Appendix B-2; and ORA TURN workpapers available at <http://ora.ca.gov/RRIMRehearing.aspx>

⁷⁷ *Administrative Law Judge's Ruling Scheduling Technical Workshop on Energy Efficiency Calculations*, September 3, 2009. The Commission's Reporting Section transcribed the September 16, 2009 workshop.

⁷⁸ Appendix B-2; and ORA TURN workpapers available at <http://ora.ca.gov/RRIMRehearing.aspx>.

⁷⁹ *2006-2008 Energy Efficiency Evaluation Report*, p. 5.

⁸⁰ *Assigned Commissioner's Ruling on Process for True-Up of Incentive Earnings*, April 8, 2010. <http://docs.cpuc.ca.gov/SearchRes.aspx?DocFormat=ALL&DocID=30030>.

Scenario Report and soliciting comments on nine scenario runs that calculated incentives using different assumptions.⁸¹ On April 15, 2010, the Energy Division released the *Draft Final Performance Basis Report (2006-2008 Energy Efficiency Evaluation Report)* required by D.07-09-043.⁸² The Energy Division notified parties of workshops on April 23, 2010 and April 30, 2010 to discuss the technical aspects of the 2006-2008 Energy Efficiency Evaluation Report, and provided the opportunity for stakeholders to provide written comments by May 17, 2010. The *2006-2008 Energy Efficiency Evaluation Report* was finalized on July 9, 2010 and the Energy Division notified the service list in this proceeding.⁸³ Appendix O of the *2006-2008 Energy Efficiency Evaluation Report* provides a table of comments and Energy Division's 88 pages of responses to comments.⁸⁴ That report showed that when measured against the goals established for the Utilities' 2006-2008 energy efficiency programs, not a single utility met the MPS.⁸⁵

The Energy Division thus followed the Commission's adopted procedures, providing stakeholders a fair opportunity to review and comment on the *2006-2008 Energy Efficiency Evaluation Report* and its underlying assumptions. D.10-12-049 did not reject the conclusions of the *2006-2008 Energy Efficiency Evaluation Report*, even though it chose to ignore the results of that report in awarding incentives to the Utilities.

IV. CONCLUSION

ORA and TURN respectfully request that the Commission adopt ORA and TURN's proposal. The proposal relies on energy savings verified by "an entity other than the one standing to profit from inflated program achievements"⁸⁶ and explains the steps necessary to

⁸¹ *Assigned Commissioner's Ruling Providing Energy Division Report and Soliciting Comments on Scenario Runs*, R. 09-01-019, May 4, 2010, p. 3.

<http://docs.cpuc.ca.gov/SearchRes.aspx?DocFormat=ALL&DocID=30812>.

⁸² Appendix B-2, Carmen Best email Thu 4/15/2010 4:40 PM, ORA/TURN workpapers available at <http://ora.ca.gov/RRIMRehearing.aspx>.

⁸³ Appendix B-2, Carmen Best Email Fri 7/9/2010 4:09 PM and ORA workpapers available at <http://ora.ca.gov/RRIMRehearing.aspx>

⁸⁴ *2006-2008 Energy Efficiency Evaluation Report*, Appendix O.

⁸⁵ See Appendix B-3: Table 25 "Comparative of Program Cycle 2006-2008 Evaluated Results to Goals" at page 101 of the *2006-2008 Energy Efficiency Evaluation Report* showed that the Utilities performance compared to goals ranged from 63% to 78% of the goals.

⁸⁶ D.05-01-055, Finding of Fact 53, p. 155.

calculate appropriate refunds. Adoption of ORA and TURN’s proposal would meet the requirement that “all money awarded” by the RRIM decisions be based on calculations verified by the Commission, via its Energy Division. Adoption of the proposal would therefore result in just and reasonable rates.⁸⁷

Respectfully submitted,

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⁸⁷ D.15-09-026, Ordering Paragraph 6, p. 13.