

STATE OF CALIFORNIA

Public Utilities Commission  
San Francisco

**M e m o r a n d u m**

**Date:** May 28, 2009

**To:** The Commission  
(Meeting of June 4, 2009)

**From:** Pamela Loomis, Director  
Office of Governmental Affairs (OGA) — Sacramento

**Subject:** **SB 806 (Wiggins) – Electrical corporation energy efficiency programs.  
Amended April 29, 2009**

**LEGISLATIVE SUBCOMMITTEE RECOMMENDATION:** OPPOSE UNLESS AMENDED

**SUMMARY OF BILL:**

This bill would require the California Public Utilities Commission (CPUC) to limit the investor-owned utilities' (IOUs) administrative costs for energy efficiency programs to five percent. This bill would also make it clear that "administrative costs" would apply to personnel and overhead, but not to marketing, outreach, and program evaluation. In addition, this bill would require the CPUC to ensure that no incentive payments are made to the IOUs unless the energy efficiency savings meet certain conditions.

**SUMMARY OF SUPPORTING ARGUMENTS FOR RECOMMENDATION:**

The CPUC supports containing administrative costs for energy efficiency at reasonable levels to maximize the benefits of the programs to consumers. However, this bill is problematic and could be counterproductive toward well-designed and delivered energy efficiency programs. The CPUC is currently examining the full spectrum of issues associated with the appropriate level of administrative costs in two open proceedings (A. 08-07-021, et.al. and R. 09-01-019). This bill would directly interfere with open contract negotiations being conducted between the IOUs and over 250 third parties and government partnerships for energy efficiency programs proposed under A. 08-07-021, et al.

Further, different types of program delivery mechanisms require different levels of personnel and administrative overhead support in order to be effective. More innovative and experimental programs may have higher administrative costs in the short-run, but

have higher potential energy savings in the long-run. Reserving more program costs for direct payments to customers may not always be the best approach to encouraging consumer investment in efficiency. Capping the IOUs' administrative costs at five percent would have serious ramifications for all of the CPUC's successful energy efficiency programs.

### **SUMMARY OF SUGGESTED AMENDMENTS:**

- Remove proposed Public Utilities Code Section 710 relating to incentive payments.
- Remove the 5% cap and direct the CPUC to investigate the appropriate administrative cost control for each of the IOUs' energy efficiency programs.

### **DIVISION ANALYSIS (Energy Division):**

#### **Administrative Costs**

- The CPUC oversees the IOUs' portfolios of energy efficiency programs funded by the public goods charge (electric and natural gas) and procurement funds.<sup>1</sup> The portfolios must be cost-effective, and the utilities must meet aggressive energy savings goals<sup>2</sup> in order to earn shareholder incentives.
- The CPUC is currently addressing the issue of administrative and all other costs of energy efficiency program implementation in proceeding (A.) 08-07-021, et al., for Pacific Gas and Electric Company, Southern California Edison Company, San Diego Gas & Electric Company, and Southern California Gas Company.
- The CPUC has developed complex and rigorous methods for verifying energy savings and determining the cost-effectiveness of the utilities' energy efficiency programs. The utilities stand to receive substantial incentive payments for achieving the energy efficiency goals set by the CPUC.<sup>3</sup> Therefore, their savings achievements must be real and verifiable.

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<sup>1</sup> The public goods charge is a surcharge imposed on the consumption of natural gas and electricity that is used in part to fund cost-effective energy efficiency and conservation programs implemented by the IOUs. Cal. Public Utilities Code sections 381, 890.

<sup>2</sup> See D. 04-09-060, D. 05-01-055, and D. 05-04-051 (establishing the goals, policies and administrative framework to guide the energy efficiency programs funded by the ratepayers for the 2006-2008 program cycle).

<sup>3</sup> See Decision 07-09-043, establishing a shareholder risk/reward incentive mechanism for energy efficiency programs, available at [http://docs.cpuc.ca.gov/word\\_pdf/FINAL\\_DECISION/73172.PDF](http://docs.cpuc.ca.gov/word_pdf/FINAL_DECISION/73172.PDF) and Rulemaking 09-01-019, addressing the shareholder risk/.reward incentive mechanism, available at [http://docs.cpuc.ca.gov/PUBLISHED/FINAL\\_DECISION/97023.htm](http://docs.cpuc.ca.gov/PUBLISHED/FINAL_DECISION/97023.htm) and D.08-07-047, updating the goals for 2009-2011, available at [http://docs.cpuc.ca.gov/WORD\\_PDF/FINAL\\_DECISION/85995.DOC](http://docs.cpuc.ca.gov/WORD_PDF/FINAL_DECISION/85995.DOC)

- This bill would directly affect or may even pre-empt the outcomes of the open CPUC proceedings A. 08-07-021 and R. 09-01-019, which are examining the full spectrum of issues associated with the appropriate level of administrative costs. Specifically, the open rulemaking (R. 09-01-019) is addressing the shareholder incentive mechanism and a second open set of four energy efficiency portfolio applications by the IOUs (A. 08-07-021, et al) is addressing the 2009-2011 portfolio procurement application process. Thus, it is inappropriate and premature for the CPUC to support a preemptory five percent cap on administrative costs without having the CPUC complete its own assessment and examination of what the appropriate cost levels should be.

For example, in the 2006-2008 program cycle, the IOUs' overall administrative costs for programs ranged from 10% to 16% of total portfolio costs (exclusive of Evaluation, Measurement and Verification costs, which if included would otherwise reduce these percentages). At this time, it is not immediately clear how utilities could reduce these costs to only five percent and still administer effective efficiency programs. This bill offers no comparative basis for determining what level of administrative costs might be appropriate for individual programs or an entire portfolio of efficiency expenditures.

- Different types of program delivery mechanisms require different levels of administrative and marketing support in order to be effective. It is arbitrary to establish a specific percentage limit on these costs without regard to the types of programs being delivered. In addition, it is likely that as the IOUs reach higher levels of energy efficiency requirements in their portfolios (which the CPUC is encouraging them to do), the personnel and administrative overhead costs of reaching those higher level goals will increase. The CPUC should have the discretion to assign and approve appropriate categorical costs based on the benefits being delivered and based on individual program design needs, as long as the overall portfolio of programs is cost-effective.
- This bill would directly interfere with open contract negotiations being conducted between the IOUs and over 250 third parties and government partnerships for programs proposed under A. 08-07-021, et al. All of these partnership and third-party program delivery entities have their own personnel and administrative overhead cost structure, separate from the administrative costs of the IOUs as overall administrators.

### **Incentive Payments**

- This bill would lock the CPUC into a process that is not only deeply flawed, but also inapplicable to the spectrum of programs contemplated for the 2009-2011 program period. In September 2008, the CPUC adopted a Strategic Plan to develop the "next

generation” of energy efficiency programs for 2009 and beyond.<sup>4</sup> This approach recognizes that market transformation is one of the ultimate goals of the IOUs’ energy efficiency programs. The IOUs’ efforts toward market transformation will not always result in quantifiable energy savings in the short term. Therefore, under R .09-01-019, the CPUC may be considering means and standards for calculating shareholder incentive payments for programs where policy achievements have no direct, quantifiable energy savings.

- By requiring savings and incentives to be calculated solely using the steps set forth in D. 07-09-043, this bill would limit incentives to energy savings achievement measured against pre-established goals and preclude incentives for achievement of market transformation goals. Thus, preventing implementation of the overarching, unifying aspect of the Strategic Plan itself. In addition, the bill would preclude the CPUC’s ability to consider other methodologies for measuring energy impacts of the programs (e.g., energy intensity indicators, energy consumption, etc.).

#### **PROGRAM BACKGROUND:**

- The reported administrative costs to the CPUC are comprised of various categories of expenditures (personnel labor and overhead), and combine IOU-specific costs and sub-contractor costs for programs, including both resource and non-resource programs. The non-resource programs, such as education and training and government partnership programs designed to influence ratepayer actions, are particularly labor-intensive, and incur comparatively higher personnel and administrative overhead costs. However, they are extremely valuable in moving consumers toward more energy efficient behavior and investments.
- One overarching requirement for energy efficiency programs is cost effectiveness. Some energy efficiency programs may be very cost effective, but have relatively high administrative costs. In other cases, there are some efficiency programs that may not be cost effective at all, but have low administrative costs. In all, an IOU’s total portfolio must be cost effective to be adopted. For the 2006-2008 program cycle, the CPUC did not impose a cap on the IOUs’ administrative costs, or marketing and outreach costs. CPUC Decision 05-09-043, which approved the IOUs’ programs and portfolio budgets for 2006-2008 states:

*Although we will continue to monitor administrative costs through our reporting requirements, and audit those costs as necessary to verify them, **we believe that program administrators should have discretion to move funds between training, marketing, overhead and other budget categories to achieve the Commission’s goals.** This is consistent with the shift in our oversight paradigm from one that focuses on “cost control” to one that encourages the achievement of a maximum level of net*

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<sup>4</sup> Available at [http://docs.cpuc.ca.gov/word\\_pdf/FINAL\\_DECISION/91068.pdf](http://docs.cpuc.ca.gov/word_pdf/FINAL_DECISION/91068.pdf).

*resource benefits to ratepayers and verifies portfolio performance on an ex post basis. (emphasis added)*

- Looking forward, the CPUC's adopted California Long-Term Energy Efficiency Strategic Plan (D. 08-09-040) calls upon utilities to undertake better leveraged and "market transformation" or "strategic" activities that may cause higher penetrations of energy efficiency measures without paying incentives to each individual customer adopting those measures. In such cases, utility expenditures on marketing and overhead may actually *increase* as a percentage of total spending, since incentive outlays would be expected to decrease. Thus, personnel and overhead will become a *larger portion* of total EE expenditures. If this approach achieves high levels of energy efficiency savings, the results can have *even greater cost-effectiveness, albeit with higher administrative outlays*. This would be a positive outcome for ratepayers.
- Independent verification of energy savings is already performed by the CPUC Energy Division (a financially disinterested entity), pursuant to the framework established in D. 05-01-055 and D. 05-04-051. Under this bill, the CPUC may approve shareholder incentive payments for achieving energy efficiency savings pursuant to CPUC-supervised energy efficiency programs, so long as an independent verification of energy savings is obtained through an audit conducted by a party that is not financially interested in the results of the audit. For the 2006-2008 programs, CPUC Energy Division staff is directing consultants who are performing comprehensive evaluations to provide the data for determining the amount of energy savings achieved through each utility's portfolio.<sup>5</sup> Under the current proceedings addressing the IOU applications and the shareholder incentive mechanism, the CPUC will retain this authority.
- Decisions are pending in both R.09-01-019 and A.08-07-021 et al. Administrative and marketing costs are being addressed along-side overall program costs in A.08-07-021 et al. Passage of this bill prior to a decision in these open proceedings may affect contract negotiations pending with third parties (both IOU sub-contractors and local government partnerships). It is unclear what the impact of SB 806 will be on these negotiations. If this bill becomes effective after decisions in either proceeding have been rendered, and if those decisions do not adopt the cap as proposed by this bill, a second set of proceedings would have to be scheduled.
- The amount of shareholder incentives that the utilities may receive for the 2006-2008 program period is currently the subject of settlement discussions as directed in R 09-01-019. Passage of this bill prior to a decision in R.09-01-019, could bias

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<sup>5</sup> The CPUC's Utility Audit, Finance and Compliance Branch conducts audits of the utilities' claimed costs of the energy efficiency programs, not audits of energy savings. It is therefore a misnomer to refer to these as "audits" of energy savings. The commonly used term is "evaluations" of energy savings.

settlement negotiations and evidentiary hearings scheduled in late June 2009, should no settlement be reached. Thus, if this bill becomes effective after decisions in either proceeding have been rendered and if those decisions do not adopt the provisions currently in this bill, a second set of proceedings might have to be scheduled.

**LEGISLATIVE HISTORY:**

AB 51 (Blakeslee, 2009) would require the CPUC to limit the IOUs' administrative costs for energy efficiency programs to 10%.

**STATUS:**

SB 806 is currently pending on the Senate Appropriations Suspense File.

**SUPPORT/OPPOSITION:**

Support: The Utility Reform Network (TURN)  
Division of Ratepayer Advocates

Opposition: None on file.

**STAFF CONTACTS:**

Michael Poe, Legislative Liaison      [mdp@cpuc.ca.gov](mailto:mdp@cpuc.ca.gov)      (916) 327-7788

**Date:** May 28, 2009

BILL NUMBER: SB 806 AMENDED  
BILL TEXT

AMENDED IN SENATE APRIL 29, 2009  
AMENDED IN SENATE APRIL 13, 2009

INTRODUCED BY Senator Wiggins  
( Coauthor: Senator Padilla  
)

FEBRUARY 27, 2009

An act to amend Section 399.4 of, and to add Section 710 to, the Public Utilities Code, relating to energy.

LEGISLATIVE COUNSEL'S DIGEST

SB 806, as amended, Wiggins. Electrical corporation energy efficiency programs.

Under existing law, the Public Utilities Commission has regulatory authority over public utilities, including electrical corporations, as defined. Existing law restructuring the electrical service industry states that it is the policy of the state and the intent of the Legislature that the commission continue to administer cost-effective energy efficiency programs. Pursuant to decisions and orders of the commission, the commission supervises energy efficiency programs administered by electrical corporations.

This bill would require the commission to limit the administrative costs, as defined, of energy efficiency programs to not more than 5% of the funds expended. The bill would, if the commission determines that incentive payments should be made to electrical corporations and gas corporations for achieving energy efficiency savings pursuant to commission-supervised energy efficiency programs, require that the commission ensure that (1) no incentive payments are awarded to an electrical corporation or gas corporation unless an independent verification of energy savings is obtained through an audit conducted by a party that is not financially interested in the results of the audit, and (2) incentive payments are only awarded based upon actual achievement of energy efficiency goals ~~—(3) incentive payments are only awarded based on long term cumulative energy efficiency goals, and (4) any overpayment of incentives to an electrical corporation or gas corporation be returned to ratepayers~~

Under existing law, a violation of the Public Utilities Act or any order, decision, rule, direction, demand, or requirement of the commission is a crime.

Because the provisions of this bill would be a part of the act and because a violation of an order or decision of the commission implementing its requirements would be a crime, the bill would impose a state-mandated local program by creating a new crime.

The California Constitution requires the state to reimburse local

agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

Vote: majority. Appropriation: no. Fiscal committee: yes.  
State-mandated local program: yes.

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. Section 399.4 of the Public Utilities Code is amended to read:

399.4. (a) (1) In order to ensure that prudent investments in energy efficiency continue to be made that produce cost-effective energy savings, reduce customer demand, and contribute to the safe and reliable operation of the electric distribution grid, it is the policy of this state and the intent of the Legislature that the commission shall continue to administer cost-effective energy efficiency programs authorized pursuant to existing statutory authority.

(2) As used in this section, the term "energy efficiency" includes, but is not limited to, cost-effective activities to achieve peak load reduction that improve end-use efficiency, lower customers' bills, and reduce system needs.

(b) The commission, in evaluating energy efficiency investments under its existing statutory authority, shall also ensure that local and regional interests, multifamily dwellings, and energy service industry capabilities are incorporated into program portfolio design and that local governments, community-based organizations, and energy efficiency service providers are encouraged to participate in program implementation where appropriate.

(c) In order to ensure that energy efficiency programs achieve the maximum benefits for each dollar of ratepayer funding collected to support those programs, the commission shall limit the administrative costs to not more than 5 percent of the funds expended. For the purposes of this subdivision, "administrative costs" means personnel and overhead costs associated with the implementation of each measure and program, but does not include costs associated with the marketing or evaluation of a measure or a program.

SEC. 2. Section 710 is added to the Public Utilities Code, to read:

710. If the commission determines that incentive payments should be made to electrical corporations and gas corporations for achieving energy efficiency savings pursuant to commission-supervised energy efficiency programs, the commission shall ensure ~~all~~

*both* of the following:

(a) No incentive payments are awarded to an electrical corporation or gas corporation unless an independent verification of energy savings is obtained through an audit conducted by a party that is not financially interested in the results of the audit. The results of the audit shall be approved by the commission in a public proceeding. The results of the audit shall be made available to the public at least 30 days prior to any public proceeding in which the commission will determine whether to accept the results.

(b) That incentive payments are only awarded based upon actual achievement of energy efficiency goals  ~~, not as a means of providing earnings to an electrical corporation or gas corporation~~ . It is the intent of the Legislature that the steps outlined in Decision 07-09-043 be used to determine actual achievement of energy efficiency goals by electrical corporations and gas corporations.

~~—(c) That incentive payments are only awarded based on long term cumulative energy efficiency goals. It is the intent of the Legislature that the steps outlined in Decision 07-09-043 be used to determine actual achievement of long term cumulative energy efficiency goals by electrical corporations and gas corporations.~~

~~—(d) That any overpayment of incentives to an electrical corporation or gas corporation be returned to ratepayers.~~

SEC. 3. No reimbursement is required by this act pursuant to Section 6 of Article XIII B of the California Constitution because the only costs that may be incurred by a local agency or school district will be incurred because this act creates a new crime or infraction, eliminates a crime or infraction, or changes the penalty for a crime or infraction, within the meaning of Section 17556 of the Government Code, or changes the definition of a crime within the meaning of Section 6 of Article XIII B of the California Constitution.