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Substantive Changes Made to
Rules Governing Texas Utility Run Energy Efficiency Programs

The energy efficiency rule, **Substantive Rule § 25.181, Energy Efficiency Goal**, was approved by the Public Utility Commission of Texas in the July 30 Open Hearing. The primary provisions effecting the administration of energy efficiency programs by the state's investor-owned utilities are as follows:

- An increase in the energy efficiency goal from the current 20% of the growth in electric demand each year, to 25% of growth in demand in 2012, and 30% in 2013 and beyond
- Customer cost caps were added to assure rate impact is contained
- Increases in 'avoided costs' (or benefits of saving) were adopted to recognize increased value of savings
- Elimination of the hard-to-reach (low-income) program utility bonus provision
- Modification of the cost allocation language to more closely reflect the statute language
- Requiring utilities to facilitate and encourage participation of Retail Electric Providers in efficiency programs

We expect the results of these changes to effect little or no increase in the level of energy efficiency program spending until 2014, and only then assuming economic recovery leads to additional growth in demand. The rate of growth upon which the goals are based is actually determined, according to the rule, using a five year rolling average methodology, so this also tends to delay the impact of new growth on the goals.

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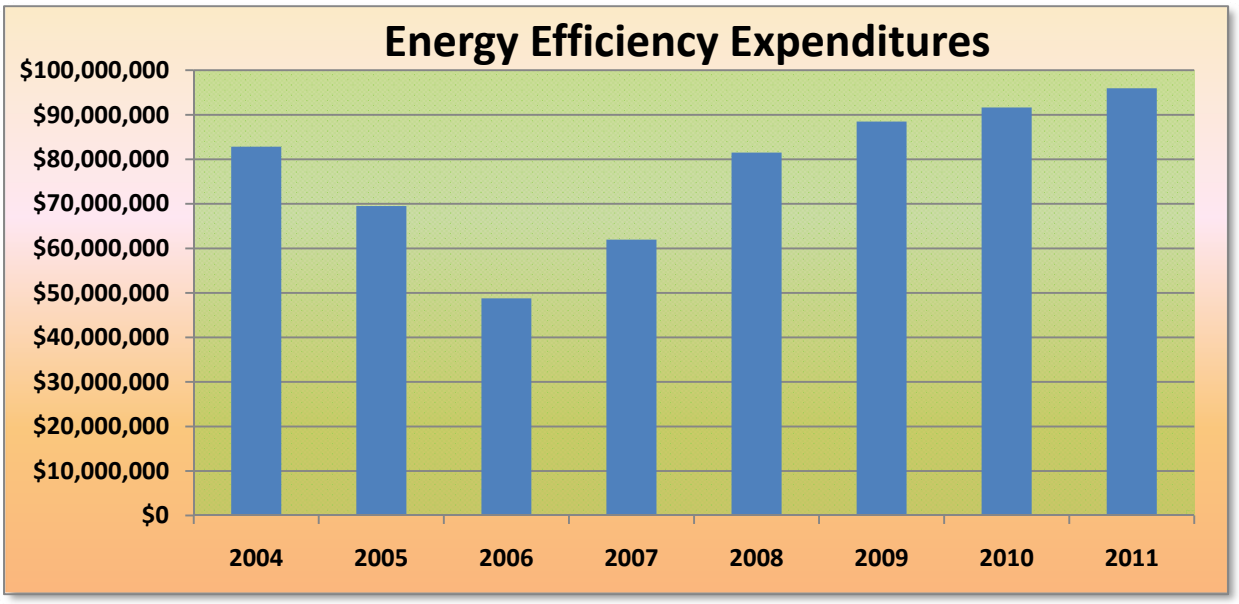
A. Impact of the Change of the Energy Efficiency Goals

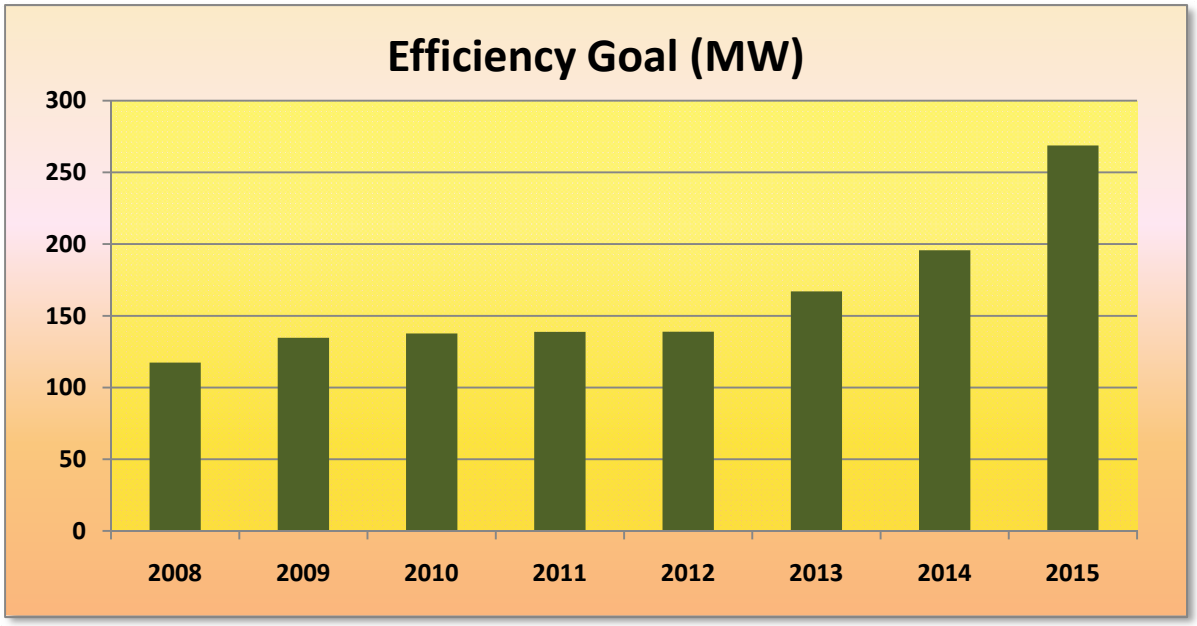
Section (e), *Annual energy efficiency goals*, was changed to increase the current goal of 20% of demand growth (excluding transmission-level industrial facilities) to 25% of demand growth in 2012 and 30% of demand growth in 2013 and subsequent years. Demand growth is the average growth of the five previous weather adjusted peak demands for each utility. (There is a "ratchet" clause which sets a minimum level equal to the previous year's energy efficiency goal, which was unchanged, so goals do not decrease.)

Despite the increase in the goal from 10% of demand growth to 20% in 2010 and 2011, there has been little increase in energy efficiency spending.[1]



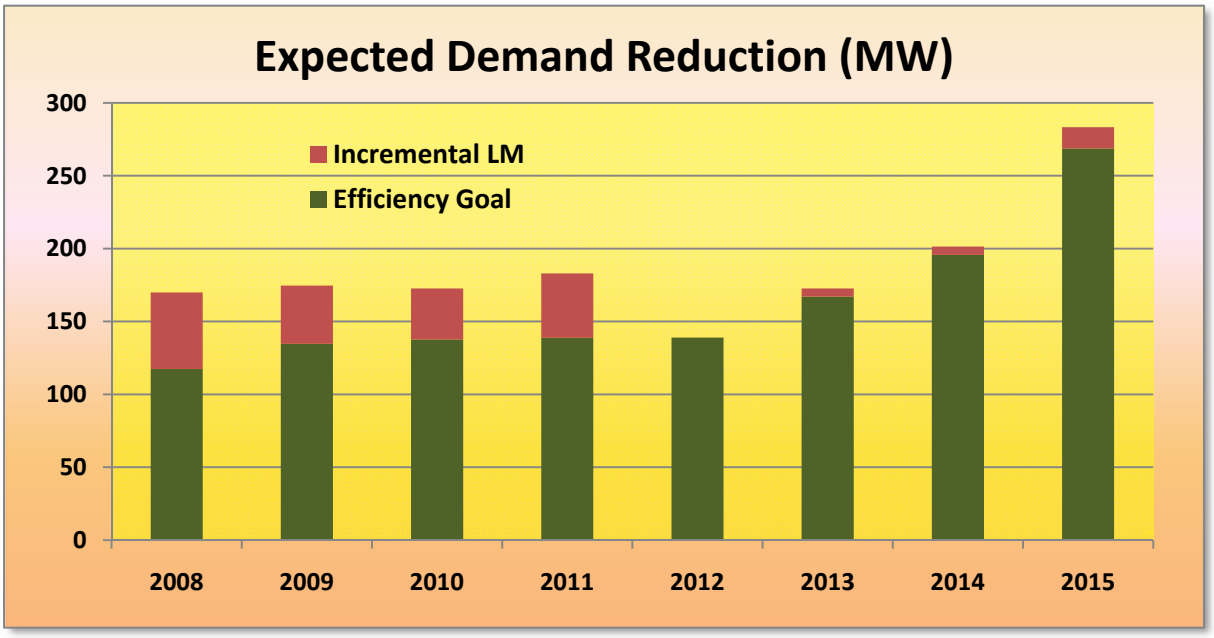
[1] We exclude efficiency spending under the 2006 CenterPoint rate case settlement, since the Commission has repeatedly ruled that these expenditures do not qualify for reimbursement under the energy efficiency programs. Given the current CenterPoint rate case proceeding, it is unclear whether this spending will continue in the future. We also exclude any efficiency and distributed generation included in the EFH settlement.

We expect that the energy efficiency goals, and thus energy efficiency spending, will eventually increase, as shown in the following chart, once the recession years are no longer included in the calculation of the five year average growth in demand.[2] However, for the near term, the new rule will have little impact on program goals.



The amount of **achieved** demand reduction going forward will be slightly more than the efficiency goals, but much less than has been reported. This is due to load management programs having a one year program life, which means that the reduction in demand growth each subsequent year from load management actually only equals the **additional** load management capacity added in that year, or growth in the amount of load management acquired overall. (The utilities tend to meet their mandated goal with efficiency measures, then use load management to reach their maximum bonus, because load management is inexpensive and does not reduce their revenue, and as currently utilized, do not reduce their investments in transmission and distribution infrastructure.) So, as the goal increases, we expect there will be only a small amount of additional load management added each year as shown in the next graph.

[2] We used the forecasts of utility peak demands presented by EUMMOT (the Electric Utility Marketing Managers of Texas) for our calculations with one adjustment. EUMMOT did not account for the impact of energy efficiency on demand growth, and thus future energy efficiency goals. We corrected for that impact, reducing demand growth by any additional efficiency above current levels obtained by increasing the goal. This reduces the goal in future years by about 10 percent below the level projected by EUMMOT.



B. Impact of Cost Caps

Under the new rule, there is now a total cost cap, including the bonus cost, for each utility, based on a cost per kWh or per month for residential customers, and per kWh for commercial customers.

Section f(8):

	Residential (month)	Residential (¢/kWh)	Commercial (¢/kWh)
2011 & 2012	$1.30	0.10	0.050
2013 and forward	$1.60	0.15	0.075

The cap should not be a serious constraint on most utility efficiency programs given the relatively modest goals adopted.[3] We examined the three biggest utilities, to determine when these caps might have an impact on their efficiency programs.[4]

[3] The Rule doesn't actually specify the size of the customer for which this cap would be applied. Most calculations evaluated by the utilities and the Commission were based on 1000 kWh per month as the average customer. Our analysis focused on the per unit cap for residential customers.

[4] For this exercise, we assumed that all low income programs are assigned to residential customers. However, because the bonus for hard-to-reach programs has been eliminated, these programs only have to account for 5% of the efficiency goal as originally required in the rule. We also assumed that weatherization spending will remain at the planned 2010-2011 levels, and that administrative spending, including R&D, will add 15% to costs while incentive payments remain at the 2010-2011 levels for each class of customer. Costs for 2010-2011 are taken from the plans filed by the utilities. We also assumed that each utility earns a bonus equal to 20% of their program costs.

AEP currently exceeds these caps, which may be a tribute to their commitment to energy efficiency in their service area, relative to their peers, but the new cap will require adjustment of their programs. The other two major utilities should have no problem meeting their goals and remaining under the price caps through 2014. In 2015, Oncor may experience difficulty in meeting its goals under the adopted price caps.

¢/kWh	2010	2011	2012	2013	2014	2015
Rate Caps						
Residential		**0.100**	**0.100**	**0.120**	**0.120**	**0.120**
Commercial		**0.050**	**0.050**	**0.075**	**0.075**	**0.075**
Oncor						
Residential	0.079	0.083	0.061	0.084	0.083	0.124
Commercial	0.038	0.039	0.042	0.061	0.060	0.096
CenterPoint						
Residential	0.046	0.043	0.051	0.065	0.086	0.098
Commercial	0.021	0.021	0.018	0.023	0.031	0.035
AEP Central						
Residential	0.155	0.126	0.078	0.077	0.076	0.107
Commercial	0.054	0.065	0.043	0.042	0.042	0.065

We also ran a more conservative scenario, which assumes that the three utilities continue to reach 10% of their goal with hard-to-reach programs, which cost more per unit savings, and that the cost of commercial and residential programs are 20 percent higher than the 2010-2011 planned costs in subsequent years. In this case, Oncor will not be able to meet its 2015 goal and AEP may have trouble meeting the 2015 goal. CenterPoint may have to shift funding from residential to commercial programs.

¢/kWh	2010	2011	2012	2013	2014	2015
Rate Caps						
Residential		**0.100**	**0.100**	**0.120**	**0.120**	**0.120**
Commercial		**0.050**	**0.050**	**0.075**	**0.075**	**0.075**
Oncor						
Residential	0.079	0.083	0.075	0.104	0.103	0.156
Commercial	0.038	0.039	0.047	0.069	0.068	0.107
CenterPoint						
Residential	0.046	0.043	0.064	0.083	0.110	0.124
Commercial	0.021	0.021	0.020	0.026	0.034	0.039
AEP Central						
Residential	0.155	0.126	0.093	0.091	0.090	0.129
Commercial	0.054	0.065	0.048	0.047	0.046	0.073

C. Changes in Avoided Costs

There were some minor changes in avoided costs, as the avoided cost of energy was raised from 5.5¢/kWh to 6.4¢/kWh {section (d)(2)}, and will be set as the average price in ERCOT during peak hours over the previous two years in 2012.

The avoided capacity cost of $80/kW remains in effect for 2011, but will be adjusted upward in 2012 to $100/kW if the base overnight cost of a new conventional combustion turbine as reported by the EIA exceeds $650/kW (it was $638/kW in EIA, Assumptions to the Annual Energy Outlook 2009, p. 88).

Because most of the major utilities have been able to reach their full bonus under the current avoided costs and bonus caps, the adjustment in the Commission's avoided cost calculations will have little impact on program expenditures or bonuses earned by the utilities.

D. Allocating Costs Among Classes

Section F(3) contained a subtle change in language, reverting to the original legislative language, which could provide the Commission with the discretion to spread the costs of low income (hard-to-reach and weatherization) programs, or all programs, among all customers, though currently the Commission has not committed to any change. If the spending on hard-to-reach is reduced to the minimum required to meet the 5% of the total savings goal, the cost caps may not force the Commission to consider this option.

> The EECRF shall be calculated to recover the costs associated with ~~each program~~ programs under this section from the customer classes that receive services under ~~each program~~ the programs.

E. Participation of Retail Electric Providers and Energy Service Providers

A section was added, (i)(5)(C), requiring utilities to encourage the development of programs and program options which would be implemented by Retail Electric Providers (REPs) and Energy Service Providers (ESPs). The utilities in areas where there is customer choice shall conduct programs to encourage and facilitate the participation of REPs and ESPs in energy efficiency and demand response programs. This can be done by coordinating program rules, contracts, and incentives to facilitate the statewide marketing and delivery of programs by REPs or setting aside amounts for programs to be delivered to customers by REPs. The utilities are also instructed to work with REPs and ESPs to evaluate the demand reductions and energy savings resulting from time-of-use prices, home-area network devices, such as in home displays, and other programs facilitated by advanced meters.