

DECOUPLING

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This has been an extraordinarily wide-ranging, useful and interesting tour through the principles of ratemaking – sort of a Bonbright for the 21st Century. After more than 100 years of regulation, the questions raised in this docket are *core* questions – to what extent should we re-write the regulatory compact to cope with the need to drastically reduce load and load growth, drastically reduce greenhouse gas emissions, and decentralize key functions, while managing essential utility distribution investment.

Central regulatory assumptions are up for grabs – regulatory lag works differently when load is not growing, utility oversight works differently when much of the investment desired is on the customer side of the meter, achieving affordability is a different challenge if we are no longer dealing with a decreasing-cost industry.

But we have learned *something* worth retaining over 100 years. For example, perhaps front-end loading of investments in rates may not be the best way to match the timing of the benefits of investment. A future test year, with reconciliation, will still require prudence review, periodic full-blown rate cases, and something to replace the efficiency incentive provided by the historic test year. [Considerable argument will be necessary on this, given NGrid's aggressive push for it.] Pre-approval of efficiency investments, along with shareholder incentives or lost base revenues (LBR), has led to extremely effective, award-winning programs, not to mention significant savings of energy and capacity.

[Earlier hearings detailed responses to each other proposal, e.g., full decoupling is not tied to efficiency performance; partial decoupling is too complicated, opaque, and imprecise to administer; raising fixed charges will hurt low-income customers by raising small-customer bills and hurt the environment by diluting the variable price signal to conserve. As a practical matter, I think partial decoupling and higher fixed charges are pretty low on the Commission's list.]

Four basic principles of regulation remain valid and important:

1. Just and reasonable prices, related to costs.
2. Set in a transparent forum with due process. [Partial decoupling flunks this test.]
3. Balancing conflicting interests in a reasonable way.
4. While not arbitrarily taking utility property.

In this context, those principles suggest these three corollaries:

1. Decouple only to reduce cost (DOER's principle).
2. Consider *coupling*, tying desired performance to incentives. Put another way, make sure there is a relationship between the means you choose and the ends you desire. [We have considerable experience in Massachusetts showing that utility regulation (performance incentives, LBR) can have a positive impact on utility investment in efficiency.] It is not clear that utility regulation has much impact on ESCo investment, or code adoption and enforcement. Nor is it clear that the decoupling strategies we have been discussing –

which are *revenue* strategies -- will have an impact on demand response or smart grid investment.

3. Do no harm – to customers, to the environment, to the economy.

To expand on the last principle a bit:

First, do no harm to customers.

- Low-income electricity customers tend to be small consumers, so their bills will tend to rise if revenue responsibility is shifted to fixed charges.
- Low-income customers already use 15% less electricity than average – their ability to shift in response to critical peak pricing is relatively slight.
- Demand response and distributed generation are good ideas, but care must be taken not to raise total costs by adopting strategies that cost more than they save.
- Without careful ratemaking, even *economic* distributed generation could raise rates and bills.
- Short-term investments with long-term benefits can be justified as cost-effective in the long-run – but care should be taken that customers can afford these good things in the *short* run.

Second, do no harm to the environment:

- Those high fixed charges that hurt low-income customers also have the effect of lowering variable energy rates, sending *exactly* the *wrong* price signal.
- By contrast, an inverted rate structure – higher per unit prices for higher consumption – may be the most appropriate right now.

Third, do no harm to the economy:

- Decoupling will have the effect of raising rates in a recession, when consumption often decreases, exactly the opposite of the financial stimulus that is usually called for in a recession.
- To add to the perversity, utility costs (such as cost of capital) are often decreasing in a recession.

So where does this leave us?

First- Rate cases keep revenues in line with reasonable costs. Decoupling looks only at revenues. [Reduced ROE, a capital structure adjustment to reduce reliance on expensive equity, a limit on annual rate increases (say, 3%), periodic rate cases.]

Second - Existing decoupling mechanisms have worked very well, so move carefully in establishing mechanisms for the (hopefully) expanding investments in efficiency.

Finally - Please pay particular attention to the ability of low-income customers to pay their bills. Customers cannot afford investments in everything desirable all at once (even if cost-effective) . As the arrearage data show, and as I know you know and are sensitive to, low-income customers are already struggling – with declining success – to pay their bills AND feed their families. Please recognize that adverse bill impacts on low-income customers will require compensating mitigation strategies such as expanded efficiency programs to lower bills, as well as increased low-income discounts. (Which, by the way, are not that expensive since they are spread over all other consumption.)