

**BEFORE THE
House Consumer Affairs Committee**

**Hearing on Act 129 of 2008 --
Energy Efficiency Mandates Imposed on
Electric Utilities**

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Testimony of

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Good afternoon Chairman Godshall, Chairman Daley and members of the House Consumer Affairs Committee. I am Terry Fitzpatrick, President and CEO of the Energy Association of Pennsylvania (“EAP” or “Association”), a trade association comprised of electric and natural gas utilities operating in Pennsylvania. I am here today on behalf of the Association’s electric utility members, which are also known as electric distribution companies (EDCs).¹ Thank you for this opportunity to appear before you today.

The purpose of this hearing is to review the energy efficiency and peak demand reduction mandates contained in Act 129 of 2008. Among other things, this law required EDCs with more than 100,000 customers to implement programs to reduce energy consumption by 1% by May 2011, and 3% by May 2013. It also required reductions in peak demand of 4.5% in the 100 hours of highest usage by May 2013. In the event EDCs did not persuade enough customers to participate in the programs in order to meet the targets, the law provided that they were strictly liable for penalties ranging from \$1,000,000 to \$20,000,000 regardless of fault. With the exception of one EDC that did not meet the interim 1% consumption reduction target (and paid a \$1,000,000 penalty), EDCs satisfied these requirements.

Following the completion of the “Phase I” requirements described above, Act 129 directed the PUC to evaluate the costs and benefits of the programs, and to direct incremental additional reductions if the programs were cost-effective. The PUC conducted this analysis and ordered additional consumption reduction targets in “Phase II” covering the years 2013 to 2016. The EDCs are on track to meet the mandated

¹ Citizens’ Electric Company; Duquesne Light Company; Metropolitan Edison Company; PECO Energy Company; Pennsylvania Electric Company; Pennsylvania Power Company; Pike County Light & Power Company; PPL Electric Utilities; UGI Utilities, Inc.-Electric Division; Wellsboro Electric Company; and West Penn Power Company.

targets established for Phase II. And, after conducting a second set of market potential studies this past year, the PUC established reduction targets for a “Phase III”, which will commence on June 1, 2016 and run through May 31, 2021. With regard to peak demand reduction requirements, the Commission concluded that the design required in Phase I was not cost-effective, so it did not order additional requirements in Phase II. However, following an independent study conducted in 2014, the PUC proposed additional requirements for Phase III based upon a finding that additional peak demand reductions can be designed to be cost-effective.

Act 129 allows EDCs to recover only the cost of implementing energy efficiency and peak demand reduction requirements and caps the cost of the combined programs at 2% of the EDC’s total annual revenues as of December 31, 2006. The law specifically precludes EDCs from recovering the revenue they lose due to customer usage reductions, except through a base rate case where rates may be set on a going forward basis to reflect the lower usage levels. EDCs spent close to \$250 million last year alone on their Act 129 energy efficiency and conservation programs; an amount that is ultimately borne by all ratepayers and that does not include the cost of paying the statewide evaluator hired by the PUC or the cost of *other* utility-run conservation programs such as the Low-Income Usage Reduction Program (LIURP). This number represents the fifth-largest statewide spending on such programs in the nation.²

To understand Act 129, it is necessary to understand the background against which it was adopted. At the time it was passed, it appeared that the electricity bills of customers might increase significantly – 50% or more – when caps on the supply

² As of 2012; *Edison Foundation, Summary of Electric Utility Customer-Funded Energy Efficiency Savings, Expenditures, and Budgets: Issue Brief, March 2014.*

charges of EDCs expired in most of Pennsylvania in 2010 to 2011. This had already occurred a few years earlier in Maryland, Delaware, and in the service territory of a small Pennsylvania EDC, resulting in rate shock and a vigorous policy debate about the causes of the problem and possible solutions. The General Assembly adopted Act 129 as a response to the expected increase in customers' bills; however, these expected steep increases generally did not occur. In fact, some customers even saw their bills decrease due to a drop in wholesale electricity prices at the beginning of the recession. Since that time, the emergence of natural gas production from the Marcellus Shale has resulted in lower power prices (wholesale electricity prices tend to follow natural gas prices because of the increasing reliance upon gas to generate electricity) than was envisioned when Act 129 was passed.

With this background in mind, EAP suggests three changes to the energy efficiency and peak demand reduction provisions of Act 129. First, we suggest that the statute should be amended to change the punitive, inflexible provisions that require large penalties if targets are not met without regard to consideration of the underlying circumstances and the degree of fault of the utility. This could be accomplished by changing the word "shall" to "may" in section 2806.1 (f). EAP notes that no other state statute establishing standards for energy efficiency relies on mandatory penalties if a target is missed by even one kilowatt hour. In fact, a number of other states provide incentives when an EDC meets or exceeds a reduction goal.

Second, Act 129 should be amended to allow utilities to recover the revenue they lose as a result of their energy efficiency programs through a timely, transparent mechanism that is directly tied to the usage actually reduced through utility energy

efficiency programs. This approach is preferable to attempting to make lost revenue determinations as part of complex, expensive, and time consuming rate cases. The ability of utilities to recover these lost revenues in rate cases under Act 129 demonstrates that the Legislature understood the existence of these revenue losses – and the negative impact the losses would have on utilities’ ability to fund grid operations. Lost revenue recovery mechanisms provide a more timely and transparent way to keep utilities financially whole for executing governmental mandates, and they more effectively ensure that resources are available to maintain and improve the reliability of the grid.

Third, Act 129 should be updated by reconsidering the baseline for funding the program. Currently, the Act bases the 2% cap on implementation costs on each utility’s total revenue for the year 2006, which includes revenue from distribution and generation/supply charges (including charges from competitive suppliers collected from customers through the utility’s bill). Utility revenues were higher in 2006 because caps on the generation charges of utilities were still in place in most of the state, and most of the electric load was still supplied by utilities. In contrast, electric generation suppliers (EGSs) now supply about two-thirds of the electric load in the state. Because of these factors, as stated previously, Pennsylvania has one of the most expensive utility energy efficiency programs in the country. The Act should be amended to establish a more recent year, such as 2013, as the baseline, or to base cost caps on the distribution costs only.

The Clean Power Plan

In August 2015, the U.S. Environmental Protection Agency (EPA) released the “Clean Power Plan” (CPP) – final regulations under the Clean Air Act governing carbon dioxide emissions from existing electric generating plants. The CPP is intended to reduce carbon dioxide emissions in the U.S. by 32% from 2005 levels by 2030, and a specific emission rate reduction target of 33% has been established for Pennsylvania. States will submit plans to EPA as to the strategies they will implement to meet their emission reduction targets or, if they do not submit plans, EPA will implement a federal plan for the state.

The final rule is substantially different from the rule EPA proposed on June 18, 2014. EPA established uniform national emission rates for affected units and applied those rates to state generation mixes to create state goals. These standards are the underpinnings for the state-specific emission rate and mass-based targets. The final regulations contain extensive changes from the proposed regulations that were released in 2014, and over time there will be additional analysis of the cost impact of these changes. Other changes in the final rule include moving the starting point for implementation from 2020 to 2022, establishing a ramp up to the final standards, and providing a provision for a “safety valve” for individual power plants in order to protect reliability of electric service.

The CPP provides states with different options for achieving compliance with the carbon dioxide reduction targets depending on the compliance plan. These may include improving the efficiency of coal generating plants, joining with other states to establish a cap and trade program for carbon dioxide emissions, increasing generation from

renewable sources, increasing energy efficiency among consumers of electricity and encouraging demand reduction programs.

Electric utilities in Pennsylvania are “wires companies” – they own and operate distribution and transmission systems, and do not own generating plants. Accordingly, they are not directly responsible for compliance with the regulations governing emissions from power plants although all segments of the industry are likely to be impacted in some way. Additionally, electric utilities will be affected if Pennsylvania increases mandates for renewable energy and utility energy efficiency or demand reduction programs to meet its targets under the CPP. With regard to renewable energy, electric utilities and electric generation suppliers are already required to purchase 18% of their supply portfolios from alternative energy sources by 2021, including 8% from renewable sources. With regard to energy efficiency or demand reduction, one of the options PA could choose would be to increase the requirements on electric utilities. As described above, regulated electric utilities in Pennsylvania already are subject to significant mandatory requirements under Act 129 which are paid for by customers.

There is significant legal and political uncertainty hanging over the CPP in general, and in the event the CPP might withstand these challenges at the federal level, there is also uncertainty about how Pennsylvania will seek to comply with the regulations. At this point, electric utilities would ask generally that maintaining and improving reliability and affordability of electric service be given the highest importance in developing these policies. In addition, if Pennsylvania relies on increased utility energy efficiency requirements as part of its CPP compliance plan, this further

increases the importance of reforming the Act 129 program so that it remakes these programs in a manner that is aligned with utility business objectives, as are the programs in many other states, and provides incentives to exceed mandated requirements.

Thank you for the opportunity to appear before you today, and I would be happy to answer questions.