

**STATE OF CONNECTICUT**  
**DEPARTMENT OF PUBLIC UTILITY CONTROL**

RE: APPLICATION OF THE : DOCKET NO. 07-07-01  
CONNECTICUT LIGHT AND :  
POWER COMPANY TO AMEND :  
RATE SCHEDULES : DECEMBER 12, 2007

**BRIEF OF**  
**ENVIRONMENT NORTHEAST**

**I. INTRODUCTION**

Environment Northeast (ENE) appreciates the opportunity to present its views on the decoupling mechanism proposed by The Connecticut Light and Power Company (CL&P or the Company) in compliance with Public Act No. 07-242. This mechanism is an important component of the policy objectives in the Public Act which include increasing the use of energy efficiency and demand side management resources to capture all that are cost-effective. The proposed adjustment mechanism would true up distribution revenues to the allowed revenue requirement on a revenue per customer basis and would include a “weather normalization” component. ENE believes that the revenue per customer adjustment complies with the statutory mandate, will effectively decouple revenues from sales volumes, and recommends its approval by the Department. However, the proposed weather normalization component would increase the variability of distribution charges for consumers, create charges which significantly exceed allowed revenues during extreme weather conditions, is entirely unnecessary, and should be eliminated.

CL&P’s decoupling proposal also includes substantial increases to fixed rate components, particularly the customer charges for residential and small business customers. This would necessarily mean that volumetric kWh charges would be lower than they otherwise would be, depending on the overall level of the approved revenue requirement, with a corresponding reduction

in a customer's ability to control his bill, and the price signal to encourage conservation would be reduced. Increased customer charges could disproportionately impact low income customers, many of whom have lower usage. Since one purpose of decoupling is to support reductions in customer usage, it is inconsistent to implement decoupling through substantial increases in customer charges. ENE urges the Department to reject this proposal.

The Office of Consumer Counsel (OCC) and the Connecticut Industrial Energy Consumers (CIEC) have proposed that the Department adopt a Conservation Adjustment Mechanism which would recover "lost revenues" instead of CL&P's decoupling proposal. This proposal would not decouple distribution revenues from sales volumes and thus would not meet the statutory requirements. Moreover, this mechanism has been utilized in Connecticut and other states in the past and has been found to be ineffective and counter-productive. ENE urges the Department to reject this proposal.

## **II. CL&P's Proposed Decoupling Adjustment Mechanism should be Modified and Approved.**

### **A. The Form of the Proposed Adjustment Mechanism Meets the Statutory Requirements.**

Sec. 107 of Public Act No. 07-242 (Sec. 107) requires the Department to "order the state's gas and electric distribution companies to decouple distribution revenues from the volume of natural gas or electricity sales" through one or more of the following strategies: (i) adjusting actual distribution revenues to allowed levels, (ii) rate design changes that increase the amount of revenue recovered through fixed distribution charges, or (iii) a sales adjustment clause. Thus, any proposed mechanism must both decouple revenues from sales volumes and be one of the strategies described in the Act.

CL&P has proposed an adjustment mechanism which would decouple distribution revenues from sales volumes on a revenue per customer (RPC) basis. In general, the proposal would compare the actual revenues per customer with the allowed revenues per customer, based on the most recent rate decision, and would credit or charge customers for any difference over the ensuing year on a uniform per kilowatt hour basis. Goodwin Testimony at 24, 25. Except for the proposed weather

normalization component, discussed below, this mechanism is a variation of the first strategy set out in Sec. 107 which calls for adjusting actual revenues to allowed levels. Similar revenue per customer decoupling mechanisms have been approved in other states.<sup>1</sup> The mechanism would effectively decouple revenues from sales volumes because any changes in revenues per customer would be adjusted to the allowed levels. This general approach meets the statutory requirements.<sup>2</sup>

The revenue per customer mechanism provides a desirable incentive for the Company to add and retain customers because revenues would increase (as they do now) as customer numbers increase. This incentive would not be present if the adjustment simply trued up total revenues to the allowed level. Although the RPC approach provides some opportunities for abuse, the potential for these activities appears to be quite limited and subject to regulatory review, if necessary. Tr. 10-18 at 1640 (Hansen), Tr. 10-18 at 1668-9 (Goodwin). On balance, ENE believes that this adjustment mechanism is reasonable and appropriate and should be approved, except as noted below.

**B. The Proposed Weather Normalization Adjustment Should be Removed from the Decoupling Adjustment Mechanism.**

CL&P's proposed adjustment mechanism includes a "weather normalization" adjustment to actual revenues which CL&P claims will result in its "absorbing the weather risk" and thus protect customers. Goodwin Testimony, p.24. In fact, the actual workings of the proposed mechanism would increase the impact of weather on customers, particularly in extreme weather conditions.

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<sup>1</sup> These include Maryland (Potomac Electric Power Company, Delmarva Power and Light Company) (decisions provided with LF-89) and Utah (Questar Gas Company, Docket No. 05-07-T01, 10/5/06).

<sup>2</sup> The data presented in this docket indicate that the direct financial impact, through charges or credits, of CL&P's proposed mechanism on customers would be quite small. Calculations were presented for three prior years (2004 – 2006). The largest impact would have been in 2006, when the Company experienced the largest annual decline in sales (4.9%) in the last 25 years. The second largest decline during this period was 1.5% in 1982. ENE-02. Excluding the weather normalization component, the adjustment for 2006 would be \$15.6 million or about .07 cts./kWh. OCC-210 at 3. For the more typical years of 2004 and 2005, the projected impact, excluding weather normalization, would be about \$3 million or .01 cts. /kWh. ENE-01, LF- 102. These calculations assume that annual sales would total 24,000 GWh. Tr. 10/18 at 1590 (Goodwin). Mr. Arnett testified that the proposal "should produce very small adjustments." Tr. 10/18 at 1680.

Absent this component, the decoupling adjustment mechanism alone would effectively eliminate the impact of weather on distribution revenue collections for both customers and the Company. Hansen Testimony at 7-8.

As generally applied, weather normalization adjusts actual billings to “normal” weather based on historic averages. The expectation is that, over time, weather fluctuations will average out to this norm, and the method will reduce the variability in billings for distribution costs. Accordingly, customers would expect to see electric distribution charges reduced following hot summer weather conditions and increased following mild summer conditions. The accuracy of the adjustment is dependent on the degree to which actual average temperatures for future periods are the same as the historic averages.

However, in attempting to combine weather normalization with the decoupling adjustment, CL&P has produced a mechanism which actually increases the impact of weather on customer billings. A comparison of ENE-001(p. 3) with LF-102 illustrates the problem. Both exhibits use 2005 data to illustrate the application of CL&P’s decoupling adjustment, but in LF-102, the weather normalization component is eliminated. As shown in ENE-001, the notable weather abnormality in 2005 was a very hot summer. CL&P calculated the weather impact on revenues as \$8.9 million and subtracted this amount from the actual annual revenues of \$646.1 million to derive a “WN Annual Revenue” of \$637.2 million. Tr. 11-8 at 2551-52.

Then CL&P assumed that the latter amount was what was actually paid to complete the calculation and determined that customers owed an additional \$11.7 million. *Ibid.* The difficulty with this approach is that customers had already paid \$8.9 million of this amount, but it was assumed away in the calculation. LF-102 shows the results if weather normalization is eliminated from the calculation and actual RPC revenues are compared to those authorized. The decoupling charge would be reduced to \$2.8 million and the calculation would be greatly simplified and would accurately reflect the difference between allowed and actual revenues.

The effect of CL&P’s weather normalization proposal is to require customers to pay twice for extreme weather conditions—once for the increased consumption and again as a result of the calculation. Presumably, mild conditions would produce the opposite result—the company would undercollect due to reduced consumption and the same amount would be further deducted from

future billings as an adjustment. It is clear that CL&P's approach would increase the variability of weather-related charges and impose higher costs for periods when energy costs are already increased due to extreme conditions.<sup>3</sup> Revenue decoupling eliminates the need for weather normalization and the associated risks to both customers and the Company because it trues up actual revenues to those allowed, irrespective of the cause of the deviation. Hansen Testimony at 7-8.

In addition to these deficiencies, the weather normalization component is not consistent with the statutory conditions. As discussed above, CL&P has proposed a variation on the first strategy listed in the statute, which is "a mechanism that adjusts actual distribution revenues to allowed distribution revenues." By introducing weather normalization, CL&P is no longer adjusting "actual" revenues to "allowed", but is introducing an intermediate adjustment which distorts the actual ratepayer payments and defeats the purpose of ensuring that ratepayers pay no more or less than is authorized. For these reasons, CL&P's decoupling adjustment mechanism should be modified to eliminate the weather normalization component and adopt the straight forward approach embodied in LF-102.

**C. Rate Design Which Proposes to Collect Greater Portions of Distribution Revenues Through Fixed Charges Should Not Be Used to Implement Decoupling or Otherwise Adopted.**

CL&P has proposed to implement decoupling through the adjustment mechanism discussed above and also through substantial increases in fixed distribution charges. For the residential and small business classes, the proposal is to increase the customer charges by 50%, or nearly twice the level of the proposed overall increase. Goodwin Testimony, Ex. CRG-16, 17. While this approach is authorized by Sec. 107, ENE does not believe that the proposed magnitude of the increases is consistent with state policies supporting efforts to reduce the consumption of electricity.

Mr. Goodwin's testimony on this issue relies, in large part, on cost causation arguments such as the following: "It is recognized that distribution cost of service is driven primarily by customer and

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<sup>3</sup> In addition, it is likely that the calculation of "normal weather" would be skewed because it is based on historic averages which don't take into account global warming. See Tr. 11-08 at 2560-61. Under the Company's mechanism, this would result in even larger weather adjustments for hot summers and exacerbate the impact on customers. See Hansen Testimony at 8.

demand related costs, with little, if any, costs driven by kWh consumption.” Goodwin Testimony at 48. This is a static view which does not give due weight to the role that kWh consumption plays in increasing required investments in distribution-related facilities. If energy consumption grows over time, the demands on system facilities will be greater and both maintenance and construction costs will grow correspondingly. It is critically important that customer rates maintain price signals that support customer efforts to reduce loads. Increasing customer charges only reinforces a customer perspective that there is little they can do to control their bills.

Higher customer charges would also adversely affect low-use customers by increasing their distribution costs relative to high-use customers. This would occur because a smaller proportion of the distribution revenues would be collected through volumetric charges. Since many low income customers use less energy than more affluent customers, this policy would likely have a disproportionate impact on them.

State policies unequivocally support encouraging the efficient use of energy and the promotion of energy conservation in designing rates as well as other aspects of utility regulation. Conn. Gen. Stat. Secs. 16-19e (a) and 16a-35k. Public Act No. 07-242 reinforces the importance of restraining energy consumption in a number of ways, particularly in its mandate that “resource needs shall first be met through all available energy efficiency and demand reduction resources that are cost-effective, reliable and feasible.” (Sec. 51 (c)) CL&P’s proposal to substantially increase customer charges is clearly contrary to these strong state policies.

Mr. Goodwin recognized this issue in his testimony and observed that “there remain ample kWh-based charges in other unbundled components to send sufficient price signals to encourage conservation and produce bill savings.” (p. 42) It is clear from studies of the potential for greater energy efficiency and from the experience of the energy conservation programs that many cost-effective opportunities remain which have not been adopted by customers despite these price signals. The bottom line on the proposal to increase customer charges is that it does not change the amount of revenue which will be collected; it merely reallocates a portion of the payments from higher use customers to lower use customers and reduces the proportion of distribution revenues collected through kWh charges. At a time when greater consumption is costly for all, it makes sense to continue strong volumetric price signals to encourage high levels of conservation.

### **III.A Lost Revenue Mechanism Would Not Decouple Revenues from Sales As Required by the Statute and Has Been Demonstrated to be Ineffective.**

OCC and CIEC have proposed the adoption of a Conservation Adjustment Mechanism (CAM) in place of CL&P's proposed decoupling mechanism. The CAM, more generally known as a lost revenue mechanism, has been utilized in Connecticut and other states in the past and has generally been discredited as ineffective, as discussed below. As proposed, it would attempt to compensate the utility for any "lost revenues" arising solely from the implementation of its conservation and load management program, and would not eliminate the impact of sales on revenues. See Briden Testimony at 26, 27. Utilities would retain the throughput incentive to maximize sales in order to maximize revenues and profits. Tr. 10/18 at 1618 (Hansen); Tr. 10/22 at 1786 (Briden). Thus, it would not "decouple distribution revenues from the volume of natural gas or electricity sales" and would not meet the basic requirement of Sec. 107. Moreover, a lost revenue approach is not listed as one of the acceptable strategies for implementing decoupling in Sec. 107. Accordingly, the CAM cannot be considered to be a mechanism which meets the statutory requirements.

A review of the history of legislative action concerning decoupling reinforces the conclusion that a lost revenue mechanism is not consistent with the statutory language. On two prior occasions, in 1991 and in 2005, the General Assembly directed the Department to investigate the decoupling of sales from earnings and prepare a report.<sup>4</sup> On each occasion, the Department's report indicated that it did not support a full decoupling mechanism that breaks the link between sales volumes and revenues and discussed the alternative of instituting a CAM. 1991 Report at Sec. III.A.2, 2006 Report at 16-19. The 2006 Report recommended the continuation of the CAM for gas companies, but not for electric companies. 2006 Report at 16-18.

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<sup>4</sup> The 1991 Report was issued in Docket No. 91-07-20, Report to the General Assembly, DPUC Implementation of Public Act 91-248 (Dec. 24, 1991) and the 2006 Report was issued in Docket No. 05-09-09, DPUC Investigation into Decoupling Energy Distribution Company Earnings from Sales, (Jan. 18, 2006)

In 2007, the legislature enacted Public Act No. 07-242 which adopted an aggressive stance towards promoting energy efficiency and demand reduction through a variety of approaches involving state agencies, the utilities and the private sector. The utilities play a critical role in the process in that they are responsible for developing annual resource procurement plans which include a requirement that “resource needs shall first be met through all available energy efficiency and demand reduction resources that are cost-effective, reliable and feasible” and for implementing C&LM programs approved under the plan. PA No. 07-242, Secs. 51, 52. Fulfilling this obligation will require a full commitment by the utilities to considering the alternatives to achieving these goals, ranging from incentive programs to educational efforts to adopting more stringent codes and standards, and to the development and implementation of the programs and activities approved. Clearly, this level of commitment would be highly unlikely if the utilities retained the throughput incentive to maximize sales in order to maximize revenues.

In light of these requirements, the legislature adopted the mandatory decoupling provision in Sec. 107 which clearly requires breaking the link between utility revenues and the volume of sales. Notably, though the legislature was fully aware of the option of instituting a CAM from the 2006 Report, it is not listed as one of the possible strategies. Equally important, the statute makes no reference to confining the scope of the mechanism to the “lost revenues” of the C&LM program. Instead, it provides for a full severance of the link between sales and revenues and thus excludes the CAM from consideration.

ENE would also like to note that lost revenue mechanisms have been instituted in a number of states and have not been shown to be effective. A recent review by the ACEEE of decoupling and incentive mechanisms concluded that states which utilized this approach in the past have generally abandoned them because the “approach turned out to be problematic, for several reasons.” These included the creation of perverse incentives such as instituting programs that look good but save little energy, contentious reconciliation hearings concerning savings measurement, the failure to change the utility’s disincentive to support broader conservation incentives or its incentive to pursue load building, and the buildup of “lost revenues” over time without reference to actual or allowed

revenue levels.<sup>5</sup> Connecticut is one of the states that dropped this approach for its electric companies in the mid 1990s for similar reasons. 2006 Report at 17-18.

#### IV. CONCLUSION

For the reasons set forth above, ENE urges the Department to approve the Company's proposed revenue per customer decoupling adjustment mechanism except for the weather normalization component, which should be eliminated, limit any increase in customer charges to minimal levels and reject proposals to establish a lost revenue adjustment mechanism.

Respectfully submitted,  
Environment Northeast

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cc. Service List

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<sup>5</sup> LF Ex. 107, Kushler, York and Witte, Aligning Utility Interests with Energy Efficiency Objectives: A Review of Recent Efforts at Decoupling and Performance Incentives, American Council for an Energy-Efficient Economy, Report No. U061, Oct. 2006, at 5, 8.