Staff Briefing Paper

Meeting Date: October 22, 2020

Company: All Electric and Gas Utilities with Approved DSM Financial Incentives

Docket No.: E,G-999/CI-08-133

Issues:

1. Should the Commission modify the current Demand Side Management Shared-Savings Financial Incentive Mechanism for implementation in the 2021-2023 triennium?

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Relevant Documents:

- Order Extending Existing Incentive Formula and Encouraging Discussions for Future Revisions
  - Proposal: MN Department of Commerce
  - Comments: Xcel Energy
  - Comments: Minnesota Power
  - Comments: CenterPoint Energy
  - Comments: Minnesota Energy Resources Corporation
  - Comments: Otter Tail Power
  - Date: February 20, 2020
  - Date: March 3, 2020
  - Date: May 18, 2020

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The attached materials are work papers of the Commission Staff. They are intended for use by the Public Utilities Commission and are based upon information already in the record unless noted otherwise.
## Relevant Documents

| Comments: American Council for an Energy-Efficient Economy | May 18, 2020 |
| Comments: Center for Energy and the Environment | May 18, 2020 |
| Comments: Fresh Energy, et al | May 18, 2020 |
| Comments: MN Office of the Attorney General | May 18, 2020 |
| Replies: Xcel Energy | June 11, 2020 |
| Replies: Minnesota Power | June 11, 2020 |
| Replies: CenterPoint Energy | June 11, 2020 |
| Replies: Minnesota Energy Resources Corporation | June 11, 2020 |
| Replies: Otter Tail Power | June 11, 2020 |
| Replies: Center for Energy and the Environment | June 11, 2020 |
| Replies: MN Office of the Attorney General | June 11, 2020 |
| Replies: MN Department of Commerce | June 11, 2020 |
I. **Statement of the Issues**

Should the Commission modify the current Demand Side Management Shared-Savings Financial Incentive Mechanism for implementation in the 2021-2023 triennium?

II. **Background**


Subd. 2c. Performance incentives. By December 31, 2008, the commission shall review any incentive plan for energy conservation improvement it has approved under section 216B.16, subdivision 6c, and adjust the utility performance incentives to recognize making progress toward and meeting the energy-savings goals established in subdivision 1c.

**On January 27, 2010**, the Commission issued its *Order Establishing Utility Performance Incentives for Energy Conservation*. Relatively minor changes were made to the performance incentives by way of orders on April 12, 2010 (reducing financial incentive calibration), March 30, 2012 (removing non-linear adjustment), April 12, 2012 (extending filing deadlines), and October 17, 2012 (modifying the effective date for measuring energy savings).

**On December 20, 2012**, the Commission approved a new shared-savings Demand Side Management (DSM) Incentive Mechanism.

**On November 19, 2013**, the Commission increased the incentive cap from 20 percent to 30 percent.

**On August 5, 2016**, the Commission made substantial modifications to the DSM Financial Incentive Plan to be implemented for the years 2017-2019. The Commission also asked the Department to submit an evaluation report by July 1, 2019.

**On February 20, 2020**, the Commission extended the DSM Financial Incentive Plan for 2020 with the same parameters as approved for 2019. The Commission asked the Department to work with other parties on exploring the possibility of revising the incentive formula for 2021-2023.


**On May 18, 2020**, the Commission received comments from several parties:

Xcel Energy

Minnesota Power
On June 11, 2020, the following parties submitted reply comments:

Xcel Energy
CenterPoint Energy
Otter Tail Power
Fresh Energy, et al
MN Department of Commerce

III. Department’s Proposal and Parties’ Comments

A. Department’s Proposal and Recommendation

The Department’s Proposal examined a number of elements of the shared-savings mechanism:

- Energy savings and incentives, for gas and electric utilities, for the years of 2014 to 2018, inclusive\(^1\),

- Utility net benefits minus shared-savings incentives, for gas and electric utilities, for the years of 2014-2018, inclusive (reporting a total benefit to customers of electric utilities of $1.36 billion, and a total benefit of $0.7 billion to gas customers),\(^2\)

- Conservation Improvement Program (CIP) changes for 2021-2023 that will affect shared-savings incentives,\(^3\)
  - Updated avoided cost assumptions, reducing shared savings, (approved by the Department of Commerce),
  - Reduced CIP Utility Discount Rate, potentially increasing shared savings (approved by the Department of Commerce),

- Potential 2021-2023 incentives under various scenarios,\(^4\) and

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\(^1\) Department Proposal, pp. 4-8
\(^2\) Department Proposal, pp. 8-10.
\(^3\) Department Proposal, p. 11.
\(^4\) Department Proposal, pp. 12-20.
Minnesota’s incentives compared to other states:

The Department’s analysis indicates that between 2017 and 2023, several changes will reduce Minnesota’s incentives by 30 percent overall. Despite the reductions, on a comparative basis, Minnesota’s incentives still appear to rank number 1 in the country when compared on a % of CIP expenditures, % of net benefits, and $/unit of energy saved basis.\(^5\)

The Department’s Proposal stated:

The Department recommends that the Commission approve a 2021-2023 Shared Savings DSM financial incentive mechanism with the following provisions:

A. For electric utilities:

1) Net benefits are calculated using the individual CIP Utility Discount Rates approved by the Deputy Commissioner in Docket No. E999/CIP-18-783 on February 11, 2020.

2) For a utility that achieves energy savings of at least 1.0 percent of the utility’s retail sales, the utility is allowed to collect a financial incentive.

3) For a utility that achieves energy savings equal to 1.0 percent of retail sales, the utility is awarded a share of the net benefits as set forth in Attachment A.

4) For each additional 0.1 percent of energy savings the utility achieves, the net benefits awarded to the utility is increased by an additional 0.75 percent until the utility achieves savings of 1.7 percent of retail sales.

5) For savings levels of 1.7 percent and higher, the utility is awarded a share of the net benefits equal to the Net Benefits Cap.

B. For gas utilities:

1) Net benefits are calculated using the individual CIP Utility Discount Rate approved by the Deputy Commissioner in Docket No. G999/CIP-18-782 on February 11, 2020.

2) For a utility that achieves energy savings of at least 0.7 percent of the utility’s retail sales, the utility is allowed to collect a financial incentive.

3) For a utility that achieves energy savings equal to 0.7 percent of retail sales, the utility is awarded a share of the net benefits as set forth in Attachment A.

\(^5\) Department Proposal, pp. 21-28, citation p. 28, footnote omitted.
4) For each additional 0.1 percent of energy savings the utility achieves, the net benefits awarded to the utility are increased by an additional 0.75 percent until the utility achieves savings of 1.2 percent of retail sales.

5) For savings levels of 1.2 percent and higher, the utility is awarded a share of the net benefits equal to the Net Benefits Cap.

C. For all utilities, set a Net Benefit Cap of 10 percent [no change from current cap].

D. For all utilities, set a Conservation Improvement Program (CIP) Expenditure Cap of 30 percent [no change from current cap].

The Department goes on to state that:

The following provisions from the current Shared Savings DSM Financial Incentive Plan are maintained, as follows:

A. CIP-exempt customers shall not be allocated costs for the shared savings incentive. Sales to CIP-exempt customers shall not be included in the calculation of utility energy savings goals.

B. If a utility elects not to include a third-party CIP project, the utility cannot change its election until the beginning of subsequent years.

C. If a utility elects to include a third-party project, the project’s net benefits and savings will be included in the calculation of the energy savings and will count toward the 1.5 percent savings goal.

D. The energy savings, cost, and benefits of modifications to non-third-party projects will be included in the calculation of a utility’s DSM incentive.

E. The costs of any mandated, non-third-party projects (e.g., the 2007 Next Generation Energy Act assessments, University of Minnesota Initiative for Renewable Energy and the Environment costs) shall be excluded from the calculation of net benefits and energy savings achieved and incentive awarded.

F. Costs, energy savings, and energy production related to Electric Utility Infrastructure Costs, solar installation, and biomethane purchases shall not be included in energy savings for DSM financial incentive purposes.

With respect to the Net Benefits Cap, the Department stated:

6 Department Proposal, pp. 31-32.

7 Department Proposal, p. 32.
The Department recommends that the *maximum* percent of net benefits that the Commission approves should be 10 percent. As shown ... when compared to other states, 10 percent of net benefits in Minnesota is equivalent to 11.1 percent of net benefits for gas utilities and 11.9 percent of net benefits for electric utilities.\(^8\)

With respect to the Expenditures Cap, the Department “opposes an exemption to the CIP Expenditures Cap because at 30%, Minnesota already has the highest Expenditures Cap in the nation,” however, the Department states:

In the event that the Commission wishes to allow flexibility in the Expenditures Cap ... the Department recommends that the Commission approve a methodology that sets a threshold based on energy savings as a percent of retail sales. For gas utilities, the Department recommends a minimum energy savings threshold of 1.2% of retail sales. For electric utilities, the Department recommends a minimum energy savings threshold of 2% of retail sales. If the utility achieves or exceeds these energy savings thresholds, the Commission could consider allowing the utility to receive an incentive equal to a maximum of 35% of CIP expenditures.\(^9\)

Note that in its reply comments, the Department provided updated information from the 2019 CIP Status Reports, information that was not available at the time it submitted its proposal in March 2020.\(^10\) That information did not cause the Department to alter its recommendation.

**B. Xcel Comments**

Xcel Energy recommends the Commission:

- Approve the Department’s modifications to the Shared Savings DSM Financial Incentive Mechanism for the 2021-2023 CIP Triennial Plan period;

- Initiate a docketed stakeholder process to explore other potential methodologies and mechanisms that can drive greater investments in energy efficiency in Minnesota ahead of the 2024-2026 CIP Triennial Plan period; and

- Consider an incentive for utilities that achieve permanent peak reductions through DSM programs.\(^11\)

Xcel is concerned that DSM savings have declined in recent years due to the stepping down to a lower percentage of net benefits and to declining avoided costs. Xcel believes that the current

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\(^8\) Department Proposal, p. 28, italics in original; see also p. 29.

\(^9\) Department Proposal, p. 30.

\(^10\) Department Reply, pp. 11-30.

\(^11\) Xcel Comments, p. 3.
reliance on a single metric, kWh saved, is leading to a situation where the interests of the customers and the utilities are less aligned. Xcel states that a ...

... focus on peak reduction would ... help encourage improved load factor through demand side management, making the grid more cost-effective for all customers. Since this avoided peak capacity disproportionately targets capital assets (and not fuel), it results in reduced earning opportunity for investor-owned utilities. The Company believes that such an incentive is in alignment with the statutory framework for CIP programs and that this component could be added to the existing Shared Savings DSM Financial Incentive Mechanism in a straightforward manner.¹²

1. **CPE Reply to Xcel**

CPE is open to discussion of Xcel’s proposal to discuss incentive for energy savings and reductions in demand for the 2024-26 triennium.

2. **CEE and ECC Reply to Xcel**

CEE and ECC support Xcel’s proposal to open a docketed stakeholder process to explore the development of incentives to encourage permanent peak reductions for possible implementation in the 2024-2026 triennium.¹³

3. **OAG Reply to Xcel**

OAG is interested in efforts to explore potential improvements in a shared savings plan and it would participate in future discussions.¹⁴

4. **Department Reply to Xcel**

The Department supports a continued stakeholder process under Docket 08-133 to ensure continuity of documentation.¹⁵

**C. MP Comments**

MP believes that ...

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¹² Xcel Comments, p. 9.

¹³ CEE and ECC Reply, pp. 1-2.

¹⁴ OAG Reply, pp. 6-8.

¹⁵ Department Reply, pp. 39-40.
... the financial incentive mechanism as laid out in the Department’s proposal will result in successfully meeting the State of Minnesota’s objective to encourage utilities to progress toward, sustain, and exceed energy-savings goals ... However, as avoided costs continue to decline and opportunities for the most cost-effective and feasible energy saving opportunities (such as lighting) decrease, it is more important than ever to continue evaluating the best way to measure and incentivize CIP performance and ensure that the mechanism aligns well with policy preferences.\(^{16}\)

MP recommends adoption of the Department’s alternative recommendation regarding the Expenditures Cap:

IOUs are allowed to exceed the 30% Expenditures Cap, up to a maximum of 35%, if gas utilities meet or exceed energy savings equaling 1.2% of retail sales and if electric utilities meet or exceed energy savings equaling 2% of retail sales ...\(^{17}\)

**D. MERC Comments**

MERC believes that its unique characteristics and challenges, compared to other gas utilities, will inhibit its ability to maximize incentive awards. MERC states that its expansive service territory makes savings efforts less cost-effective. Further, MERC states that it receives a greater share of its savings from low-income customers, but such savings are generally not cost effective. Most of MERC’s savings come from the commercial and industrial customers and such savings are less cost effective than for CenterPoint and Xcel.\(^{18}\)

**E. CPE Comments**

CenterPoint Energy states that it ...

... recommends the Commission adopt the Department’s recommendation. However, there are some aspects of the Department’s analysis where the Company believes it may be helpful to further develop the record. ... Although this is an important metric [incentive cost per unit of energy saved], it fails to put the cost of CIP incentives in full perspective. Energy savings are a resource, and so the full cost of acquiring the resource should be considered. Considering incentives in terms of percent of net benefits or percent of program cost both include (indirectly or directly) the cost of programs and both can therefore be useful to understand the incentive in context of this full resource cost. Examining incentives alone, however – whether in total or on a per-unit-of-energy-saved basis – does not. In the

\(^{16}\) MP Comments, p. 2.

\(^{17}\) MP Comments, p. 2.

\(^{18}\) MERC Comments, pp. 2-3.
Company’s view, analysis that considers only program costs or only incentive costs is incomplete; omitting either will result in an analysis that does not reflect the true cost of achieving energy savings through CIP and which could thus misinform decisions.  

1. **OAG Reply to CPE**

The OAG agrees that total cost per unit of energy saved is a relevant metric by which to judge a state’s energy-conservation programs. But it is not the only relevant metric, or even the most important metric, for evaluating shared-savings incentives. The relationship between these incentives and energy savings is complicated by other factors, such as Minnesota’s energy efficiency resource standard, favorable cost-recovery mechanisms, and the availability of decoupling. As a result, falling incentives in recent years have not driven a comparable decline in savings, and Minnesota ratepayers are likely still paying more than necessary to achieve energy savings consistent with the state’s savings goal. If ratepayers are overpaying for incentives, it is immaterial whether the total cost of CIP compares favorably to other states, and it would still be unreasonable to maintain the existing incentive caps.

2. **OTP Comments**

Otter Tail supports the Department’s alternative recommendation ...

... for a 2021-2023 Shared Savings financial incentive mechanism as found on page 2 of their March 3, 2020 proposal. The Department’s recommendation provides two key modifications to strengthen the existing financial incentive mechanism. The fifth bullet point on page two of the Department’s proposal is a modification to allow IOUs to exceed the 30 percent expenditure cap up to a maximum of 35 percent if gas utilities meet or exceed energy savings equal 1.2 percent of retail sales and if electric utilities meet or exceed energy savings equaling 2 percent of retail sales. The second modification is included in the sixth bullet point on page two and proposes to utilize IOUs specific CIP Utility Discount Rate approved by the Deputy Commissioner of the Department ... for calculating net benefits for the Shared Savings incentive. Otter Tail believes these two modifications to the existing financial incentive structure is a fair compromise between involved stakeholder groups. The modifications also improve the accuracy of the cost-effectiveness analysis modeling used for program evaluations.

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19 [CPE Comments, pp. 2-3, footnote omitted.]
20 [OAG Reply, pp. 5-6.]
21 [OTP Comments, p. 3.]
G. ACEEE Comments

ACEEE supports the Department’s proposal although it would suggest a more modest incentive level – a 20 percent expenditures cap with a possible increase to 25 percent if ambitious savings targets can be met (1.2 percent annual gas savings and 2 percent annual electric savings).  

ACEEE encourages further examination of the large reductions in avoided cost reported by the Department.

1. Xcel Reply to ACEEE

Xcel states that ...

... the avoided costs for the 2021-2023 CIP Triennial Plan period have been thoroughly reviewed and approved by the Department and were also the subject of extensive CIP stakeholder discussions. As avoided costs serve a significant role in determining the overall value presented by CIP programs, the Company takes seriously the tracking and calculation of avoided costs. We look forward to continuing to work with stakeholders to ensure that the methodologies for determining CIP program cost-effectiveness are accurate, consistent and transparent among all utilities.  

2. OAG Reply to ACEEE

OAG believes that declining avoided costs are not an issue that should be addressed through the shared savings plan, that the avoided cost assumptions underlying the net benefits are determined by the Department with stakeholder input in a separate proceeding.  

3. Department Reply to ACEEE

The Department states the ...

... avoided cost assumptions approved by the Department for use in the upcoming 2021-2023 CIP triennials were rigorously analyzed and well documented in Docket Nos. G999/CIP-782, E999/CIP-187-783 and E999/CIP-16-541. The Department concludes that no further examination of these avoided costs is required for use in the 2021-2023 CIP triennials.  

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22 ACEEE Comments, p. 2.
23 Xcel Reply, p. 4, footnote omitted.
24 OAG Reply, pp. 4-5.
25 Department Reply, p. 34. See also discussion pp. 31-34.
H. Center for Energy and Environment & Energy CENTS Coalition Comments

CEE and ECC offer three main recommendations:

1. CEE recommends that the Commission approve the Department’s recommended shared savings financial incentive mechanism for the 2021-2023 CIP Triennium as outlined on pages 31 and 32 of the Proposal.

2. CEE recommends that the Commission approve the Department’s alternative incentive cap on CIP expenditures discussed on page 30 of the Proposal. The Department’s alternative incentive cap on CIP expenditures would allow for high-achieving utilities to receive a financial incentive of up to 35 percent of CIP expenditures.

3. CEE recommends that the Commission ask the Department to work with stakeholders over the 2021-2023 CIP Triennium to explore and analyze other possible CIP financial incentive structures and compare those, along with the approved 2021-2023 CIP financial incentive mechanism, to each other and to how a similar sized - in terms of costs - supply-side investment would be rewarded financially through the cost-of-service model, and to present that analysis through this docket ahead of the Commission’s consideration of the CIP financial incentive mechanism for the 2024-2026 CIP Triennium.26

1. MP Reply to CEE

Minnesota Power is supportive of the recommendation that the Commission ask the Department to work with stakeholders to explore and analyze other possible financial incentive structures and compare them. As ... avoided costs continue to decline and opportunities for the most cost-effective and feasible energy saving opportunities (such as lighting) decrease, it is more important than ever to continue evaluating the best way to measure and incentivize CIP performance that aligns well with policy preferences while ensuring they deliver value for the customers who fund these programs.27

2. MP Reply to CEE

The financial incentive mechanism is an important part of the success experienced in Minnesota on delivering CIP programs and Minnesota Power looks forward to further discussion on this topic. As avoided costs decrease and utility resource mixes become increasingly renewable, continued collaboration around

26 CEE Comments, pp. 9-10, footnote omitted.

27 MP Reply, p. 3.
understanding these trends and further evolving the incentive mechanism will continue to be critical to the ongoing success of Minnesota CIP programs.\(^{28}\)

1. **Fresh Energy, et al Comments**

FE supports the Department’s proposal with one modification and with a suggestion for further examination. FE states:

> We believe there is a need for a monetary incentive tied to low-income energy efficiency program performance. Investor-owned utilities’ (IOUs) low-income (LI) energy efficiency programs are critical to achieving Minnesota’s public policy objectives yet are unlikely to contribute significantly (if at all) to utilities ability to earn shareholder incentives under the Department’s financial incentive framework. Adopting an incentive structure that includes a low-income performance metric, with our proposed criteria or something similar, would help ensure that Minnesota and its utilities continue to show a strong preference for energy efficiency while more equitably and effectively serving its most at-need residents.

Specifically, we propose a performance-based incentive structure for Minnesota’s electric and gas investor-owned utilities that meet the following criteria:

- Exceed low-income minimum statutory spending requirements by 50 percent; and
- Exceed the prescribed low-income energy savings thresholds presented in Table 3; and
- Spend at least 80 percent of LI budget on non-direct install measures.

With incentives capped at:

- 20 percent of a utility’s low-income program spend.\(^ {29}\)

FE proposes that the ...

... minimum incentive is met when a utility spends at least 50 percent more than its required low-income spend, and the maximum incentive is reached after a utility spends four times their required amount. For comparison, four times the min. spend is roughly double the achievement of the highest performer for both electric and gas IOUs looking over the 2017-2019 timeframe ... \(^ {30}\)

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\(^{28}\) MP Reply, p. 4.

\(^{29}\) FE Comments, pp. 1-2, footnote omitted.

\(^{30}\) FE Comments, p. 8.
FE summarizes its proposed incentive structure for electric and gas utilities in Tables 4 and 5 of its Comments.\textsuperscript{31} FE estimates that, under its proposal, Minnesota Power, Otter Tail Power and MERC would have been eligible to receive approximately $324,000 in 2019.

FE believes its proposal should be adopted for the 2021-2023 triennium and that waiting for the 2024-2026 triennium “jeopardizes the efficacy of Minnesota’s low-income CIP programs.”\textsuperscript{32} FE supports a stakeholder process to examine other mechanisms, such as incentives based on lifetime energy savings, that could be incorporated in the 2024-2026 triennium.

1. **Xcel Reply to FE**

Xcel states the “low-income incentive model put forth by the joint commenters should be thoroughly discussed and analyzed as part of such a stakeholder process,” and ...

Given the pivotal role that energy efficiency can play in achieving multiple policy goals, the Company believes that a docketed stakeholder process should be initiated to explore the potential for multi-factor DSM incentive structure, which should include a low-income energy efficiency program component. One focus of the workgroup could be to explore the multi-factor DSM incentive approaches utilized in other nation-leading states such as Massachusetts, Rhode Island, Vermont and New York. Each of those states are ranked in the top five by the American Council for an Energy-Efficient Economy (“ACEEE”)’s annual State Energy Efficiency Scorecard.\textsuperscript{33}

2. **MP Reply to FE**

MP states that it ...

... is supportive of adding a low-income specific performance-based component to the existing proposal for the financial incentive structure. Additionally, the Company believes the proposal described in Fresh Energy’s comments could serve as a good starting point for consideration. As indicated in past comments, Minnesota Power sees value in exploring a multifaceted approach to an incentive mechanism, and including a low income component would be one of the most meaningful ways to move in that direction. ... Minnesota Power believes further consideration and additional clarification is needed on some of the details of the proposal.\textsuperscript{34}

\textsuperscript{31} FE Comments, p. 10.
\textsuperscript{32} FE Reply, p. 1.
\textsuperscript{33} Xcel Reply, p. 2, footnote omitted.
\textsuperscript{34} MP Reply, p. 2.
3. CPE Reply to FE

CPE is open for consideration of implementation of a low-income component, but not for its implementation in the 2021-23 triennium. Stakeholders have not had sufficient opportunity to explore the issues.

4. MERC Reply to FE

MERC supports further discussion and consideration of a low-income incentive mechanism to encourage and reward spending and savings targeting low-income customers through a stakeholder process. While further clarification and refinement is needed around the proposed energy savings thresholds, limitations for direct-install measures, and interaction with the existing shared-savings incentive mechanism, MERC believes Fresh Energy’s proposal provides a strong foundation for the development of a low-income incentive mechanism.\(^{35}\)

5. OTP Reply to FE

Fresh Energy’s financial incentive proposal has merit, but the Company would request the Commission to convene a stakeholder group to further discuss how best to include low-income programming in a utility’s performance incentive. Otter Tail is also supportive of Fresh Energy’s request for further exploration by the Department to include metrics based on lifetime energy savings in the incentive calculations. While the net benefits calculation does reflect net benefits, Otter Tail is open to exploring this issue more in a future stakeholder group.\(^{36}\)

6. CEE and ECC Reply to FE

CEE and ECC recognize and support the overarching benefits that could be provided by a financial incentive mechanism to encourage utility performance in low-income energy efficiency programs. First, however, we believe that a broader and more robust stakeholder discussion is necessary to determine the best methods for expanding and improving energy efficiency services for low-income customers. Specifically, we believe that it is important to engage low-income advocates and program implementers to ensure that any incentive mechanism is designed to encourage the most effective programs and meaningful services for low-income utility customers. We also think it will be important to consider how a low-income-specific incentive mechanism will interact with the general CIP financial incentive mechanism.

\(^{35}\) MERC Reply, p. 2.

\(^{36}\) OTP Reply, p. 6.
We recommend that the Commission integrate the low-income discussion in the proposed stakeholder process and direct stakeholders and utilities to further explore, discuss, and, potentially, develop a financial incentive mechanism structure for utility performance in low-income CIP programs for inclusion in the 2024-2026 CIP Triennium. \(^{37}\)

7. OAG Reply to FE

OAG recommends the Commission approve the “proposed low-income incentive mechanism for 2021–2023 on a pilot basis, clarifying that low-income projects’ costs and benefits do not count toward the computation of the net-benefit or CIP-expenditure cap that applies to incentives for other projects.” \(^{38}\)

8. DOC Reply to FE

The Department states that it is ...

... intrigued with the Joint Commenters’ low-income incentive proposal. Before recommending approval or rejection or consideration for the future, the Department believes that some concepts should be modified or further developed.

For example, it is important for the parties and the Commission to hear from the utilities about the impact of requiring that 80% of the energy savings from low-income projects come from non-direct impact projects. It is not clear to the Department what impact that requirement may have on the IOUs’ abilities to achieve any level of low-income energy savings or if the savings level thresholds should be adjusted to take the specific requirement into account.

Second, the Department concludes that the Joint Commenters should consider placing a higher emphasis on achieving low-income energy savings than on low-income spending. The Department would like to receive input on this issue from other parties.

Third, legislation that would increase the low-income projects spending requirement may be considered during a special session. Knowing the outcome of that legislation would provide a clearer picture of the potential impact of the Joint Commenters’ proposal.

The Department recommends that the Commission allow a 30-day comment period on the Joint Commenters low-income incentive proposal. During that time, the Department could issue information requests asking the utilities to respond to the

\(^{37}\) CEE and ECC Reply, pp. 2-3.

\(^{38}\) OAG Reply, p. 10.
issues noted above and any additional issues identified by parties. That way the Commission would have a full record for making a decision.\textsuperscript{39}

The Department did an analysis of FE’s incentive structure if it had been implemented in 2017-2019. The results indicate that some of the IOUs would have benefited to some degree from the incentive plan.\textsuperscript{40}

The Department noted that ...

... in Docket ... 18-782,783, the Department’s Deputy Commissioner approved a 2024-2026 triennial cost-effectiveness discussion process that may consider avoided credit and collection costs in a modified version of the utility test. One option would be for parties to wait for the outcome of that discussion before making a decision on how to better value specific types of low-income projects. Another approach would be to conduct a pilot project to test the Joint Commenters proposal, potentially with modifications.\textsuperscript{41}

\textbf{J. OAG Comments}

OAG recommends the Commission “should build on past reforms to the shared-savings mechanism by capping a utility’s annual incentive at the lesser of 20 percent of the utility’s conservation-improvement spending or 8 percent of the net benefits generated by the utility’s conservation-improvement measures.”\textsuperscript{42} OAG does not dispute that energy conservation is an important regulatory policy, but it believes that such conservation can be achieved at a lower cost to ratepayers. OAG believes that other policies and programs have a greater success at achieving energy savings than do the state’s incentives, that Minnesota’s incentives are exorbitant relative to other states, and that Minnesota’s shared-savings plan incentives are not strongly correlated with the level of savings achieved. OAG stated, in reply comments:

If ... the Commission believes that the current expenditure cap would cause wasteful CIP spending, the best solution is not to increase the expenditure cap. Instead, the Commission should calibrate both caps so that the net-benefit cap is the incentive-limiting factor. This could be done either by reducing the net-benefit cap while maintaining the existing CIP-expenditure cap, or by reducing both caps while lowering the net-benefit cap relatively more. Either of these steps would ensure that utilities’ earnings are limited less frequently by the expenditure cap.\textsuperscript{43}

\begin{footnotes}
\footnote{39} Department Reply, p. 39.
\footnote{40} Department Reply, pp. 38-39.
\footnote{41} Department Reply, p. 37.
\footnote{42} OAG Comments, p. 1.
\footnote{43} OAG Reply, p. 3.
\end{footnotes}
With respect to the total cost of conservation-improvement programs, OAG argues, the total cost is not the only relevant metric, or even the most important one. Further, OAG states that if “ratepayers are overpaying for incentives, it is immaterial whether the total cost of CIP compares favorably to other states, and it would still be unreasonable to maintain the existing incentive caps.”

1. Xcel Reply to OAG

Xcel states that it agrees with OAG that …

... a wide range of factors beyond the financial incentive can impact our energy savings performance from year-to-year, including (but not limited to): regulatory requirements, decoupling, cost-effectiveness, market saturation, customer interest, and the overall economy. Those factors, however, do not negate the importance of a robust incentive. While the Company did not explicitly cite the declining incentive as a driving factor in its 2019 CIP performance, it did naturally motivate the Company to achieve significantly higher cost-effective energy savings in 2017 and 2018 before the incentive stepped down further to a lower level of net benefits. The incentive is an important driver in motivating higher CIP achievement, which unlocks numerous economic benefits throughout the state.

2. MP Reply to OAG (and ACEEE)

Minnesota Power believes that the proposed 2021-2023 Shared Savings DSM financial incentive mechanism recommendations for electric utilities, as detailed ... by the Department ... are appropriate for the upcoming triennial period. Minnesota Power does not believe that capping the financial incentive further would be beneficial for utility performance, especially considering the natural decrease in incentives related to declining avoided costs and the significant reductions made through the last triennial. Additionally, reduced incentives may impact overall savings if utilities divert resources or target the programs that are the most cost effective.

3. CPE Reply to OAG

In the Company’s view, many of the OAG’s criticisms stem from the error of focusing solely on the amount of the incentive without consideration of the full cost of achieving savings through CIP. CenterPoint Energy has repeatedly demonstrated ... that Minnesota’s natural gas energy efficiency programs represent the best

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44 OAG Reply, p. 6.
45 MP Reply, p. 4.
combination of high savings achievement at modest customer cost of any state in the nation.\textsuperscript{46}

And

The effect of the incentive mechanism may not be easy to incorporate into portfolio planning, and the precise magnitude of the correlation between the incentive and energy savings may be difficult to assess. The existence of the correlation, however, is unmistakable, and the importance of the incentive in encouraging utility efforts to go above and beyond established goals is likewise clear.\textsuperscript{47}

4. **MERC Reply to OAG**

MERC argues that OAG’s proposed changes “are not warranted and would risk undermining continued utility investment in conservation efforts.”\textsuperscript{48} Further, MERC states:

Contrary to the OAG’s assertion ... when considering the total cost of CIP savings (inclusive of program costs and incentives), the average cost of CIP savings is well below the commodity cost of gas, demonstrating that Minnesotans are getting a tremendous value when it comes to utility efficiency programs, even when shareholder incentives are included. A robust incentive mechanism is one of the driving forces behind Minnesota’s energy efficiency achievements. The shared-savings incentive mechanism encourages utilities to invest in energy efficiency beyond the statutory minimum and to propose programs that focus on measures with more long-term benefits to customers.\textsuperscript{49}

5. **OTP Reply to OAG**

OTP opposes OAG’s proposal to reduce the caps “when utilities are facing greater CIP challenges then ever with uncertain energy savings potential, declining avoided costs, and pandemic challenges that are ongoing.”\textsuperscript{50} OTP believes that performance incentives are an important component of efforts to improve energy efficiency and that it is nearly impossible to compare incentive structures across states.

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\textsuperscript{46} CPE Reply, p. 4.

\textsuperscript{47} CPE Reply, p. 7.

\textsuperscript{48} MERC Reply, p. 2.

\textsuperscript{49} MERC Reply, p. 2.

\textsuperscript{50} OTP Reply, p. 4.
6. CEE and ECC Reply to OAG

CEE and ECC disagree with the OAG’s analysis and recommendations. The OAG’s assumption that utilities would continue to achieve high levels of energy efficiency under rapidly decreasing financial incentives is based purely on speculation. ... The CIP incentive provides the business case for investing in cost-effective energy efficiency as utilities make resource allocation decisions about whether to simply comply with state CIP goals or to go beyond them. Aside from the CIP financial incentive, energy efficiency is not otherwise incented by the existing rate-regulated utility business model. We know of no reason that Minnesota utilities would strive to maximize cost-effective energy savings, absent a strong financial incentive.\textsuperscript{51}

7. Department Reply to OAG

The Department states that if ...  

... the Commission desires a lower incentive than the Department’s proposal, the Commission could consider a net benefits cap of 9 percent and a CIP expenditures cap of 25 percent. The Department hopes that its proposal, with a 10 percent net benefits cap and a 30 percent CIP expenditures cap, will help IOUs ease into the lower incentive levels while also still providing a high incentive to achieve high energy savings, which may also incentivize the types of investment that will stimulate Minnesota’s economy, which has been weakened due to the Covid-19 pandemic.

The Department notes that the Department’s recommended expenditures cap of 30 percent is 5 percent higher than the ACEEE’s suggested maximum of 25 percent. The Department continues to believe that a cap of 35 percent is unreasonable, not in the ratepayers’ interest, and should not be approved by the Commission.\textsuperscript{52}

IV. Staff Comments

The parties, in general, support much of the Departments’ proposal although there are several key areas of controversy.

Fresh Energy et al (FE) proposed the addition of a low-income component to the shared-savings mechanism for implementation in the 2021-2023 triennium.

   Specifically, we propose a performance-based incentive structure for Minnesota’s electric and gas investor-owned utilities that meet the following criteria:

\textsuperscript{51} CEE and ECC Reply, p. 3, footnote omitted.

\textsuperscript{52} Department Reply, p. 36.
• Exceed low-income minimum statutory spending requirements by 50 percent; and
• Exceed the prescribed low-income energy savings thresholds presented in Table 3; and
• Spend at least 80 percent of LI budget on non-direct install measures.

With incentives capped at:

• 20 percent of a utility’s low-income program spend.\(^{53}\)

FE proposes that the …

... minimum incentive is met when a utility spends at least 50 percent more than its required low-income spend, and the maximum incentive is reached after a utility spends four times their required amount.\(^{54}\)

FE summarizes its proposed incentive structure for electric and gas utilities in Tables 4 and 5 of its Comments.\(^{55}\)

There is general support among the parties for a low-income component, although most parties would recommend that FE’s proposal be examined more closely over the 2021-2023 triennium for potential implementation in the 2024-2026 triennium.

The Department proposed the Expenditures Cap remain at 30 percent and the Net Benefits Cap remain at 10 Percent, although the Department offered an alternative to the Expenditures Cap if the Commission wishes to introduce flexibility into the Cap. OAG recommends lower caps.

Parties offered topics for ongoing discussion, through a stakeholder process, of ways to improve the shared-savings mechanism for the 2024-2026 triennium.

V. Decision Options

1. Approve the Department’s recommendations for the 2021-2023 triennium as stated on pages 31 and 32 and Attachment A of its proposal filed on March 3, 2020, subject to modifications discussed and approved below. (Fresh Energy et al, Xcel and CenterPoint support the Department’s proposal)
2. Approve a modification allowing utilities to exceed the 30% Expenditures Cap, up to a maximum of 35 percent, if gas utilities meet or exceed energy savings equaling 1.2 percent of retail sales and if electric utilities meet or exceed energy savings equaling 2 percent of retail sales. (Minnesota Power, Otter Tail Power, Energy Cents Coalition, Center for Energy and Environment, (Department, as an alternative))

3. Approve a modification reducing the Expenditures Cap to 20 percent. (OAG)

4. Approve a modification allowing utilities to exceed the 20% Expenditures Cap, up to a maximum of 25 percent, if gas utilities meet or exceed energy savings equaling 1.2 percent of retail sales and if electric utilities meet or exceed energy savings equaling 2 percent of retail sales. (ACEEE)

5. Approve a modification reducing the Net Benefits Cap to 8 percent. (OAG)

6. Approve, for implementation in the 2021-2023 triennium, the addition of a low-income incentive component to the shared-savings mechanism as proposed by Fresh Energy et al on pages 7 through 10 of its comments of May 18, 2020. (Fresh Energy et al)

7. Approve, for implementation as a pilot project in the 2021-2023 triennium, the addition of a low-income incentive component to the shared-savings mechanism as proposed by Fresh Energy et al on pages 7 through 9 of its comments of May 18, 2020, but modified to exclude both low-income net benefits and low-income expenditures from the calculations of the Net Benefits and Expenditures Caps. (OAG)

8. Ask the Department to continue a stakeholder process, under the current docket, to evaluate ways of improving the shared-savings mechanisms for potential adoption in the 2024-2026 triennium including, but not limited to, a discussion of:

   - incorporation of a low-income incentive mechanism,
   - incorporation of lifetime energy savings into the incentive mechanism,
   - incorporation of an incentive for utilities that achieve permanent peak reductions through the shared-savings incentive mechanism, and
   - comparison of alternative mechanisms, along with the approved 2021-2023 CIP financial incentive mechanism, to each other and to how a similar-sized, (in terms of cost) supply-side investment would be rewarded financially through the cost-of-service model.

9. Ask the Department to continue a stakeholder process, under the current docket, to evaluate ways of improving the shared-savings mechanisms for potential adoption in the 2024-2026 triennium including, but not limited to, a discussion of:

   - incorporation of a low-income incentive mechanism,
   - incorporation of lifetime energy savings into the incentive mechanism,
   - incorporation of an incentive for utilities that achieve permanent peak reductions through the shared-savings incentive mechanism, and
   - comparison of alternative mechanisms, along with the approved 2021-2023 CIP financial incentive mechanism, to each other and to how a similar-sized, (in terms of cost) supply-side investment would be rewarded financially through the cost-of-service model.