

# Incentive Regulation Lessons Learned in Nevada

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# The Example of Sierra Pacific Resources

## □ Nevada Power Company---Electric only

- 5900 Megawatts summer peak
- 810,000 customers
- \$2.3B in annual revenues
- 3.5% annual growth
- 4000 sq. miles, Las Vegas, Henderson, Clark Co.

## □ Sierra Pacific Company—Electric and Natural Gas

- 1700 Megawatts summer/winter peak
- 360,000 electric customers, 150,000 gas customers
- \$1.0B in annual revenues
- 1.9% annual growth
- 50,000 sq. miles, Reno/Sparks, Carson City, Lake Tahoe
- Small California service territory



# History of Incentive Regulation in Nevada

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2001 PUCN Rulemaking - provided an incentive for electric DSM

“To calculate revenue requirements, the utility must base the rate of return to be applied to the balance of the subaccounts of Account 182.3 for each (DSM) program that the utility has carried out on the authorized return on equity [ROE] plus 5 percent.

2005 Legislation (AB3) - allowed 1/4 of RPS to be met by DSM

2007 PUCN Investigation - reconfirmed capitalization with 5% adder

2007 Legislation (SB437) - required “decoupling” for gas DSM

## 2 Key Issues Are Separate

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1. WHETHER TO DO DSM
2. HOW TO PROVIDE INCENTIVES FOR DSM

(In Nevada, some parties used arguments against doing DSM to try to undermine proposals for specific DSM incentive mechanisms)

# There are 3 Key Issues on Whether to Do DSM

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- ❑ DSM SPENDS MONEY **NOW** TO LOWER COSTS AND POLLUTANT EMISSIONS IN THE **FUTURE**
- ❑ IT LOWERS **BILLS** EVEN IF **RATES** ARE SLIGHTLY HIGHER
- ❑ IT SAVES **MOST** CUSTOMERS MONEY EVEN IF **A FEW** PAY A LITTLE MORE

# Arguments for and Against DSM

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## **FOR DSM**

- ❑ THE LONG TERM HEALTH OF THE STATE ECONOMY
- ❑ LOWER CUSTOMER BILLS IN THE LONG RUN
- ❑ PROTECTING THE ENVIRONMENT

## **AGAINST DSM**

- ❑ LOWER RATES, RATHER THAN LOWER BILLS
- ❑ LOWER BILLS TODAY, WITHOUT REGARD TO THE LONGER RUN
- ❑ AVOIDING ANYONE AT ALL PAYING MORE IN THE LONG RUN

# Arguments for and Against DSM: The Numbers for NPC in 2007-9

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- SPENDING \$33M ANNUALLY ON DSM WHICH WILL LOWER CUSTOMER BILLS OVER THE NEXT 20 YEARS BY \$74M -- A \$41M NET SAVING (2007\$)
- THIS WILL SAVE THE AVERAGE RESIDENTIAL CUSTOMER \$21 PER YEAR AND COST A CUSTOMER WHO DOESN'T PARTICIPATE IN DSM AT ALL \$1.40 PER YEAR (0.10%)
- THE AVERAGE RESIDENTIAL CUSTOMER WILL HAVE TO PAY AN EXTRA \$17 IN THE FIRST YEAR BEFORE HE OR SHE STARTS TO SAVE MONEY IN SUBSEQUENT YEARS
- EVEN THOUGH THE AVERAGE RESIDENTIAL BILL WILL BE LOWER BY \$10.40, THE RATE WILL BE HIGHER BY 0.01¢/KWH

# The DSM Decision in Nevada: A Lesson for Kansas

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THE NEVADA PUC DECIDED THAT  
DSM IS A HIGH PRIORITY

The Lesson: AFTER YOU OPT TO GO FOR  
DSM, PUT ASIDE ALL THE BAGGAGE ABOUT  
THE CONS OF DSM AND DON'T LET IT  
INTERFERE WITH HOW TO GO ABOUT  
PROVIDING APPROPRIATE INCENTIVES

# Approach to Incentive Regulation

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- ❑ NEED TO CREATE INCENTIVE REGULATION TO MAKE DSM A **PROFITABLE BUSINESS VENTURE**
- ❑ NOT A MATTER OF "MAKING THE UTILITY WHOLE"
- ❑ NOT A MATTER OF "REWARDING THE UTILITY FOR DOING WHAT IT DOESN'T WANT TO DO"
- ❑ THE GOAL IS MAKE DSM THE UTILITY'S **PREFERRED INVESTMENT**

# Two Key Questions for Designing Incentive Regulation

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- ❑ WHAT IS THE LOWEST **PERCENT OF NET PROFIT FROM DSM** THAT THE COMMISSION HAS TO PROVIDE TO THE UTILITY TO MAKE DSM THE UTILITY'S PREFERRED INVESTMENT?
- ❑ WHAT IS THE **APPROPRIATE MECHANISM** FOR PROVIDING THE UTILITY'S SHARE OF THE NET BENEFIT?

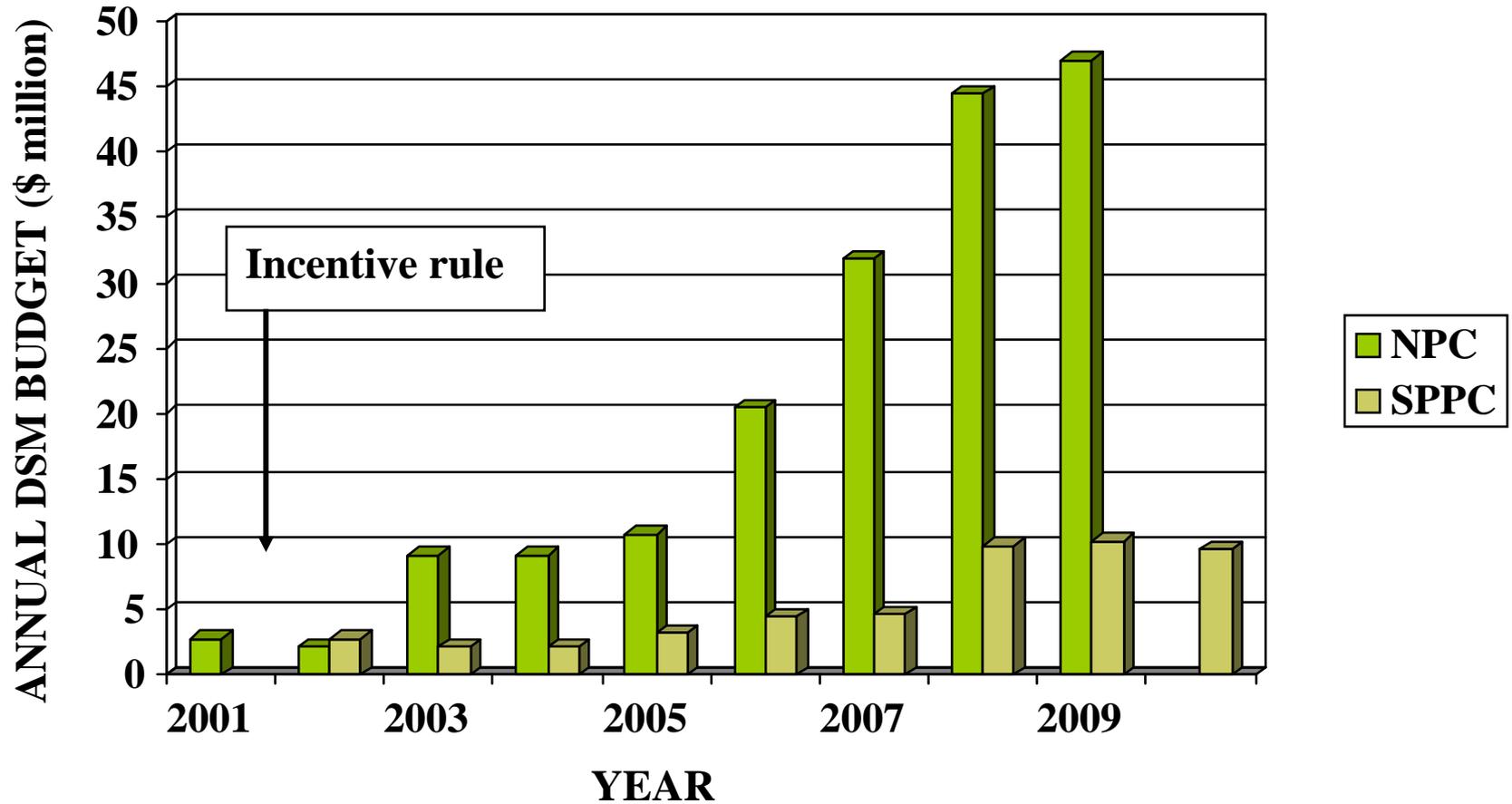
# In Nevada, 10% Is Enough

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- UTILITY DSM RECOVERY NEEDS TO
  - OVERCOME LOST REVENUE
  - INCREASE CORPORATE PROFIT
  - COMPETE INTERNALLY FOR CAPITAL FUNDS
  - COMPETE INTERNALLY FOR PERSONNEL
  
- NEVADA INCENTIVE REFGULATION PROVIDES
  - NPC: 8.1% OF NET BENEFITS
  - SPPC: 7.3% OF NET BENEFITS
  
- NPC & SPPC SAY “THAT IS ENOUGH”

**Note: NPC growth is higher than LBNL Prototype**  
**Nevada uses a historical test year for setting rates**

# SPR HAS EMBRACED DSM



# 2007-2009 Average 3-Year NPC Profitability from DSM

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- ❑ Total NPC Revenue: \$2.3B
- ❑ DSM Budget: \$33,300,000
- ❑ DSM % of Total Revenue: 1.4%
- ❑ NPV of Gross Benefit: \$73,900,000
- ❑ NPV or Net Benefit: \$40,600,000
- ❑ Profit from DSM: \$3,310,000
- ❑ Profit as % of Net Benefits: 8.1%
- ❑ Net Customer Benefit: \$37,300,000
- ❑ Consumer Portion of Net Benefit: 91.9%
- ❑ Portion of Profit from Adder: \$685,000
- ❑ Percent of Profit from Adder: 20.7%

**Note: NPC growth is higher than LBNL Prototype  
Nevada uses a historical test year for setting rates**

# 2008 SPPC Profitability from DSM

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- ❑ Total SPPC Revenue: \$1.0B
- ❑ DSM Budget: \$9,940,000
- ❑ DSM % of Total Revenue: 1.0%
- ❑ NPV of Gross Benefit: \$21,300,000
- ❑ NPV or Net Benefit: \$11,400,000
- ❑ Profit from DSM: \$827,000
- ❑ Profit as % of Net Benefits: 7.3%
- ❑ Net Customer Benefit: \$10,500,000
- ❑ Consumer Portion of Net Benefit: 92.7%
- ❑ Portion of Profit from Adder: \$133,000
- ❑ Percent of Profit from Adder: 16.1%

**Note: Nevada uses a historical test year for setting rates**

# Gas $\neq$ Electricity

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- ❑ Sales Growth Lower for Gas (bigger lost revenues)
- ❑ Gas DSM Harder (lower net revenues)
- ❑ Need Stronger Incentive(s) for Gas

# Status of Gas Incentive Regulation in NV

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- Gas incentive rulemaking is underway
  - required by legislation
  - requires “remove barriers”, not “decoupling”
- Proposed rule has 2 options
  - capitalization plus 5% ROE adder
  - Partial decoupling (lost revenue recovery)
- Decoupling outcome could go either way