

ASSESSING FINANCIAL DISINCENTIVES AND RESOLUTION OPPORTUNITIES, WORKSHOP #4

DECEMBER 1, 2004, 9:30 A.M. TO 3:00 P.M.

CONFERENCE ROOM 9 EAST, IDAHO POWER CORPORATE HEADQUARTERS, BOISE, ID

Facilitation Susan Hayman, North Country Resources, Inc.
Documentation Natalie Chavez, Chavez Writing & Editing, Inc.

Idaho Public Utilities Commission
Office of the Secretary
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Boise, Idaho

WORKSHOP OBJECTIVES

- 1) Confirm criteria to evaluate the applicability and desirability of potential mechanisms to remove disincentives/provide incentives for utility investment in DSM programs
- 2) Review two potential mechanisms:
 - a) Refined true-up mechanism
 - b) Performance-based ratemaking mechanism
- 3) Confirm the type of report that will be submitted to the IPUC on December 15 and assignments for preparation and review

WORKSHOP DECISIONS AND OUTCOMES

Participants agreed to a set of evaluation criteria for potential disincentive/incentive mechanisms. The purpose of the evaluation would be to compare and contrast different mechanisms to determine their applicability and desirability.

Participants also decided to recommend a pilot of the performance-based mechanism proposed by IPUC staff for one program until the next rate case. They also want to simulate the true-up mechanism during the same period, based on real numbers, to consider it further and refine the mechanism. The next meeting is scheduled for December 13, 9:00 am to 12:00 pm at IPC to discuss the details of these recommendations. The final report and an application for the pilot program will be submitted to the IPUC some time in January (dates to be determined December 13).

ACTION ITEMS

What?	Who?	When?
1) Draft and distribute status report for review and comment	Susan Hayman and Scott Woodbury	December 3
2) Prepare the outline and anything else necessary for developing the proposal for a pilot performance-based incentive mechanism; bring to the next meeting	IPC (Darlene Nemnich)	December 13
3) Design the simulation for the true-up mechanism; bring to the next meeting	IPC (Mike Youngblood)	December 13

WORKSHOP INTRODUCTION

Susan Hayman, North Country Resources, welcomed participants (Appendix 1), reviewed workshop objectives (above), and then reviewed the agenda (Appendix 2). She also reviewed posters with the principles of meeting conduct, purpose and products of the workshop series, and important definitions.

MECHANISM EVALUATION CRITERIA

Hayman distributed a handout with potential mechanism evaluation criteria (Appendix 3). She compiled these criteria after telephone conversations with many of the participants prior to the November 8 workshop. Hayman said that the list served as a starting point for developing a final list of criteria against which to evaluate potential disincentive and incentive mechanisms. Participants first clarified their understanding of the criteria, and then revised criteria until they were acceptable to all. Appendix 4 includes flipchart notes taken during the discussion. However, most changes were captured on the wall poster of the preliminary criteria during group discussion. The final revised list is included in Appendix 5.

POTENTIAL MECHANISMS

Refined True-Up Mechanism

Ralph Cavanagh, Natural Resources Defense Council, spoke about the requested revision to the strawman proposal for an Idaho Power true-up mechanism (introduced at Workshop #2 on September 27, 2004). A handout summarized points of the original proposal as well as the proposed revisions (Appendix 6). These proposed revisions included true-up based on actual customer counts for residential and commercial customers (rather than on forecasted sales for all customer classes as originally proposed).

Cavanagh, in cooperation with Idaho Power staff, looked into how often a true-up tied to actual customer counts would have increased or reduced rates for the residential and commercial classes since 1990. For any year during which such a mechanism would have been in effect, rates would have gone down if the class's retail sales had grown more rapidly than the class's customer count, and vice versa. For the commercial sector, electricity use grew more rapidly than the customer count in 10 of the 14 years since 1990. For the residential sector, electricity use grew more rapidly than customer count in 2 of the 14 years, while rates of growth were essentially identical in 3 years (including 2003). These findings confirm the potential for rate decreases as well as increases for both classes under a true-up mechanism, although based on historical data, the likelihood of a rate decrease is substantially greater for the commercial sector than for the residential sector. Cavanagh emphasized that annual class-specific rate increases necessary to ensure recovery of the authorized fixed-cost revenue requirement would never have exceeded 2% under the true-up mechanism. In most years, for both classes, rates would have shifted up or down by 1% or less.

During his presentation, Cavanagh shared the following:

- A bar chart showed the net benefit of expanded energy-efficiency efforts for the Idaho system. The high case indicated the greatest net benefit to the system at just over a \$100 million (Appendix 7). Given the net benefits, financial disincentives need to be removed so that Idaho Power is encouraged to promote energy efficiency through conservation programs.
- This true-up mechanism provides symmetry in that it addresses both lost revenues and found revenues. Therefore, it discourages "perverse incentives" and DSM programs that "look good on paper but aren't effective in practice."
- The revised strawman proposal avoids cross subsidies and is fundamentally fair to the customers.
- A second bar chart showed the annual household energy use (in kWh) for entertainment electronics that will likely be typical of households in about 10 years (Appendix 7). It's expected that combined energy use for plasma TVs, DVD/VCRs, and set top box/satellite receivers will be about 1,200kWh annually, up from about 500 kWh now with analog TVs. Workshop participants were cautioned through this example that technological advances and changes in customer habits do not necessarily lead to reduced per-customer electricity usage. This underscores the importance of well-designed energy efficiency incentives, as well as and the merits of the revised NRDC true-up proposal (which ties any increases in fixed cost recovery for the residential and commercial classes to increases in the number of residential and commercial customers).
- A performance-based mechanism could be used in conjunction with the true-up mechanism.

Follow-up discussion among participants focused on how big the impacts of implementing a true-up mechanism would be to residential and commercial customers and how rate adjustments would be calculated. Flipchart notes made during this portion of the workshop are included in Appendix 8.

Performance-Based Ratemaking Mechanism

Lynn Anderson, IPUC, distributed a two-page strawman proposal for a performance-based mechanism (Appendix 9). Before talking about the proposal summarized on the second page, he asked that participants review the hypotheses included on the first page. Until he compiled this list, he had been unable to draft the proposed mechanism. The following issues were raised during discussion of hypotheses:

- Cavanagh questioned the exclusion of increased gas market share from fixed-cost losses in hypothesis #7. Idaho Power may be motivated to retain electric market share for water heaters if the company is unable to recover the fixed-cost revenue losses resulting from customers' conversion to more efficient gas water heaters. This approach seems to penalize the company for these conversions and encourage inefficiency. IPUC staff pointed out that Idaho Power could implement a DSM program that reimburses customers for converting to energy-efficient gas water heaters.
- Some workshop participants see some inconsistency in the IPUC's view on factors outside Idaho Power's control. For example, the strawman proposal disallows Idaho Power from collecting fixed-cost revenue losses unless incurred through DSM efforts. Yet reimbursement of fuel costs through the company's Power Cost Adjustment (PCA) mechanism does allow for factors outside the company's control.
- The means for verifying savings resulting from DSM programs are likely to be "complex, tedious, and expensive."

Following discussion of the hypotheses, Anderson explained the actual proposal, found on the second page of the handout. The IPUC staff's strawman proposal would implement a mechanism to remove financial disincentives by allowing specific fixed-cost revenue recovery for all verified DSM savings with a bonus financial incentive for exceeding cost-effective DSM targets. He pointed out that the financial incentives component of the proposal could also be implemented as a stand-alone approach or with a true-up mechanism. This mechanism, as proposed, would be implemented as a trial restricted to the Residential New Construction program. Residential energy rates have a relatively high fixed-cost recovery component, which means that Idaho Power's financial disincentive for DSM in this class may be higher than for other customer classes. It's also a relatively small program, so effects of any mistakes made in the trial would be minimized. The following points were made during discussion of the performance-based proposal:

- According to Darlene Nemnich, IPC, Idaho Power rewards customers \$750 when they exceed building code on energy efficiency by 30% on new construction. Ideally, builders would want to make homes as energy efficient as possible, but they are unlikely to want to change codes. Therefore, code enforcement and training of code officials is important, and it is reasonable to credit utilities with work they do with code enforcement beyond typical DSM programs.
- Because of the trial nature of the mechanism, no penalties are included. Quality control is relatively straightforward, and the targeted customer group is narrow, but the potential for perverse incentives cannot be dismissed.

Flipchart notes pertaining to the performance-based mechanism are included in Appendix 10.

Additional Suggestion

David Hawk, J.R. Simplot Co., suggested that the group conduct an 18-month simulation of the two proposed mechanisms based on real numbers. He believed that all parties and participants had invested too much time discussing concerns with financial disincentives and potential corrective mechanisms for nothing to happen. Because participants may not be comfortable implementing one or both of the proposed mechanisms right now, an 18-month simulation would allow proposals to be studied further and problems worked out before the group forwarded a firm recommendation to the IPUC. The flipchart regarding Hawk's suggestion as well as other modeling options is included in Appendix 11.

NEXT STEPS

Mechanism Analysis/Evaluation

Ric Gale, IPC, requested that the interest groups (IPUC, Idaho Power, Northwest Energy Coalition, and Industrial Customers) caucus before presenting their views on each of the three proposals: true-up mechanism, performance-based pilot, and 18-month simulation of the two proposals. Hayman allotted 15 minutes for caucusing. Afterwards, she asked that group spokesmen share their groups' views on the three proposals and next steps. Industrial Customers felt that David Hawk's previous suggestion for a simulation adequately represented their view. Flipchart notes from the three interest reports are included in Appendix 12.

Idaho Power Company

Gale reported the following Idaho Power perspectives regarding the proposals:

- Idaho Power is concerned about disallowance of program costs. The company endeavors to manage program costs as effectively as possible. But disallowance of program costs and prudence reviews by the IPUC significantly deters DSM investment.
- In the intermediate or long term, the company may want to implement a true-up mechanism. In the next couple of years, Idaho Power wants to undertake the activities in the IRP but is probably unable to ramp up DSM any more than that. They are, however, amenable to simulating the true-up mechanism until the next rate case to at least identify unintended consequences. Gale isn't sure how much influence results of the simulation will have, but it could eliminate a degree of the uncertainties.
- The company is intrigued by IPUC staff's incentive mechanism and supports piloting it with one program until the next rate case and then evaluating its applicability to others.

Northwest Energy Coalition

Ralph Cavanagh shared the following viewpoints for Northwest Energy Coalition representatives:

- They are not convinced that a simulation will change people's minds. Therefore, the coalition isn't interested in pursuing a simulation unless the group is truly committed to moving forward, the simulation/test is credible, and the exercise establishes an architecture that can be used in the next rate case.
- The simulation may or may not be effective in evaluating how Idaho Power Company's appetite for conservation programs would change if a true-up were implemented. Rather, the simulation will give an indication of the rate impact of the true-up under hypothetical scenarios of conservation activity.
- Their commitment to the true-up mechanism hasn't diminished. Although they can forward the proposal directly to the IPUC, they prefer to continue working with this group. Gale commented that the simulation allows the group to refine the mechanism before the next rate case so that they can give the IPUC something feasible.

Idaho Public Utilities Commission

Randy Lobb reported the following points of view for IPUC representatives:

- They understand Idaho Power's concern about cost recovery and prudence reviews. But the IPUC will continue these reviews, and the company will likely continue to do a good job. They believe that, because of the Energy Efficiency Advisory Group (EEAG), the company is actually at less risk now regarding disallowances than it has been in the past.
- The IPUC is interested in piloting the performance-based mechanism on a single program. This pilot allows everyone to see whether the complexity can be worked out and the mechanism is feasible.
- The IPUC is also amenable to the 18-month simulation of the true-up mechanism if the other groups support it. The main purpose of the mechanism is to see how it changes company activities. A simulation may have some value. If nothing else, it keeps a mechanism that the IPUC staff is unlikely to suggest adopting at the moment on the table for future consideration. Working through it now may

provide the company information it needs when it starts making decisions for the next two-year IRP cycle.

Commission Reports and Timelines

Hayman directed participants to discuss the two reports—status and final—to the IPUC and timelines for continued activities. The following decisions were made:

- Scott Woodbury, IPUC, and Hayman will collaborate on the status report and send it out Friday, December 3, for review.
- This group will meet Monday, December 13, to discuss details of the pilot performance-based mechanism and simulation of the true-up mechanism.
- Idaho Power staff will prepare an outline for the pilot program and a design for the simulation for discussion and finalization at the December 13 meeting. The company would like to see the pilot start January 1 (or as soon as possible thereafter) when the DSM program begins. The pilot application does not have to be submitted with the final report, although the report will be supportive of the filing. The group agreed that the final report may precede the application filing unless they were submitted concurrently. The group decided to talk specifically about the timing of the filing and the report at the December 13 meeting.
- Bill Eddie, Advocates for the West, will coordinate the final report, which will likely be a recommendation to implement the pilot and simulation until the next rate case. The draft outline for the report was developed at the November 8 meeting.

WRAP-UP AND WORKSHOP EVALUATION

Hayman reviewed action items to be completed before the next workshop (Appendix 13). This workshop is scheduled for December 13, 2004, from 9:00 am to 12:00 pm. Mike Youngblood agreed to check on the availability of Conference Room 9 East for this workshop. During the workshop, participants will discuss details of the pilot performance-based mechanism and simulation of the true-up mechanism.

Hayman also requested that participants evaluate the workshop. She recorded positive items and possible changes on flipcharts (Appendix 14). Though feelings were mixed on preferable room size and temperature, for the most part, participants are pleased with the honest and frank discussion, facilitation and documentation, and refreshments.

APPENDIX 1—PARTICIPANTS

(Shading indicates work group participants unable to participate in person or by phone.)

Name and Affiliation	Name and Affiliation
Lynn Anderson, IPUC	Laura Nelson, IPUC
Maggie Brilz, Idaho Power	Darlene Nemnich, Idaho Power
Terri Carlock, IPUC	Peter Richardson, Industrial Customers of Idaho
Ralph Cavanagh, Natural Resources Defense Council	Brad Purdy, Community Action Partnership Association of Idaho
Bill Eddie, Advocates for the West	Don Reading, Ben Johnson Associates
Ric Gale, Idaho Power	Greg Said, IPC
David Hawk, J.R. Simplot Co.	David Schunke, IPUC
Nancy Hirsh, NW Energy Coalition	Tim Tatum, Idaho Power
Bart Kline, Idaho Power	Mike Youngblood, Idaho Power
Randy Lobb, IPUC	Scott Woodbury, IPUC

APPENDIX 2—AGENDA

**ASSESSING FINANCIAL DISINCENTIVES AND
RESOLUTION OPPORTUNITIES
WORKSHOP #4**

December 1, 2004
9:30am-3:00pm
Conference Room 9 East
Idaho Power Corporate Headquarters
Boise, Idaho

Objectives:

- 1) Confirm criteria to evaluate the applicability and desirability of potential mechanisms to remove disincentives/provide incentives for utility investment in DSM programs
- 2) Review two potential mechanisms:
 - a. Refined true-up mechanism
 - b. Performance-based ratemaking mechanism
- 3) Confirm the type of report that will be submitted to the IPUC on December 15, and assignments for preparation and review

Final Agenda

(breaks will be taken when most convenient for the group)

Time	Topic	Process
9:15am	Coffee/Tea available in meeting room	
9:30am	Welcome/Introductions/Meeting Overview – Susan Hayman	Information
9:45am	Mechanism Evaluation Criteria – Susan Hayman	Exercise / Discussion
10:30am	Potential Mechanism <ul style="list-style-type: none"> ▪ Refined true-up mechanism – Ralph Cavanagh 	Presentation / Discussion
11:30pm	Lunch (on your own)	
12:30pm	Potential Mechanism <ul style="list-style-type: none"> ▪ Performance-based ratemaking mechanism – Lynn Anderson 	Presentation / Discussion
1:30pm	Next Steps – Group <ul style="list-style-type: none"> ▪ Mechanism analysis/evaluation to be completed (using criteria, other?) ▪ Nature of the December 15 IPUC report ▪ Timelines 	Discussion
2:45pm	Wrap-up and Evaluation – Susan Hayman	Discussion
3:00pm	Adjourn	

APPENDIX 3—POTENTIAL MECHANISM EVALUATION CRITERIA

Potential Mechanism Evaluation Criteria

- 1) Balanced (fair) allocation of program costs across shareholders and ratepayers
- 2) Cross-subsidization of program costs across ratepayer groups are minimized
- 3) Removes financial disincentives to the max
- 4) Positive financial benefit (at least less negative effect), measured over time
- 5) Ratepayers are better off than they would be without the mechanism
- 6) Promotes rate stability
- 7) Simple mechanism
- 8) Costs easily tractable
- 9) Mechanism adjustments are predictable and easily understood
- 10) Monitors short and long term effects to customers and company
- 11) Incentives to manipulate the mechanism are not present
- 12) Close link between mechanism and desired DSM outcomes
- 13) Provides adequate incentive for the acquisition of all cost-effective DSM

APPENDIX 4—FLIPCHARTS REGARDING EVALUATION CRITERIA

Criteria

#4 Needs clarification

- “Benefit to all stakeholders from where they would have been otherwise”
- Drop “less negative”—should be net benefit

#10 Process needs to monitor mechanism

“Ratepayers” are “customers” [change throughout]

#8 Tractable

- Want mechanism that is affordable
- Costs known and manageable, not subject to unexpected fluctuations
- not talking about program cost recovery

#5 Difficult to know benefits to all stakeholders until after the fact

- #5 is the bottom line

#11 Avoid “perverse” incentives

Stakeholder =
company and customers
includes everybody

APPENDIX 5—REVISED VERSION OF POTENTIAL MECHANISM EVALUATION CRITERIA

Potential Mechanism Evaluation Criteria

- 1) Stakeholders are better off than they would be without the mechanism
- 2) Minimize cross subsidies across customer classes
- 3) Removes financial disincentives
- 4) Optimizes the acquisition of all cost-effective DSM
- 5) Promotes rate stability
- 6) Simple mechanism
- 7) Administrative costs and impacts of the mechanism are known, manageable, and not subject to unexpected fluctuation
- 8) Monitors short and long term effects to customers and company
- 9) Avoids perverse incentives
- 10) Close link between mechanism and desired DSM

APPENDIX 6—REVISIONS TO THE STRAWMAN PROPOSAL FOR AN IDAHO POWER TRUE-UP MECHANISM

PROPOSED REVISIONS TO STRAWMAN PROPOSAL FOR AN IDAHO POWER TRUE-UP MECHANISM

Submitted by Ralph Cavanagh
For discussion at 12/1/04 workshop

I. ORIGINAL PROPOSAL, DISCUSSED AT 9/22/02 WORKSHOP

1. Starting point: fixed-cost revenue requirement and retail rates approved by Idaho PUC in latest Idaho Power rate case.
2. If, after initial year, changes in retail electricity use lead to under- or over-recovery of fixed cost revenue requirement, a rate true-up would occur in the following year on the same schedule as the Company's current Power Cost Adjustment.
3. Until reestablished in the next Idaho Power rate case, the currently approved fixed cost revenue requirement would be automatically adjusted annually to reflect the same rate of increase (or decrease) shown for retail electricity sales, net of any DSM programs, in Idaho Power's latest IRP. True ups would occur annually based on any divergence between the total fixed-cost revenue recovery that forecast sales would have delivered and the fixed-cost revenues actually recovered (so if, for example, sales were forecasted to increased by 2 percent and actually increased by a larger percentage, Idaho Power would refund the difference at the time of the next Power Cost Adjustment; if retail sales increased by a smaller percentage than forecast, Idaho Power would get back the lost revenues at the time of the next Power Cost Adjustment).
4. True-ups would occur by customer class based on divergence between actual and forecast sales to each customer class.
5. Idaho Power would continue to absorb the risk or benefits of purely weather-related effects on fixed-cost revenue recovery, as it does now. This would mean weather normalizing actual sales before making the annual true-up calculation.

MAXIMUM ANNUAL AVERAGE RATE IMPACT OF THE TRUE UP MECHANISM, UP OR DOWN, UNDER EXTREME CONDITIONS = 1.5 PERCENT.

II. PROPOSED REVISIONS AND ANSWERS TO SUBSEQUENT QUESTIONS

- A. CHANGES IN CALCULATION OF ANNUAL FIXED COST RECOVERY:** Without a true-up, fixed cost recoveries grow in direct proportion to growth in total retail sales, averaging

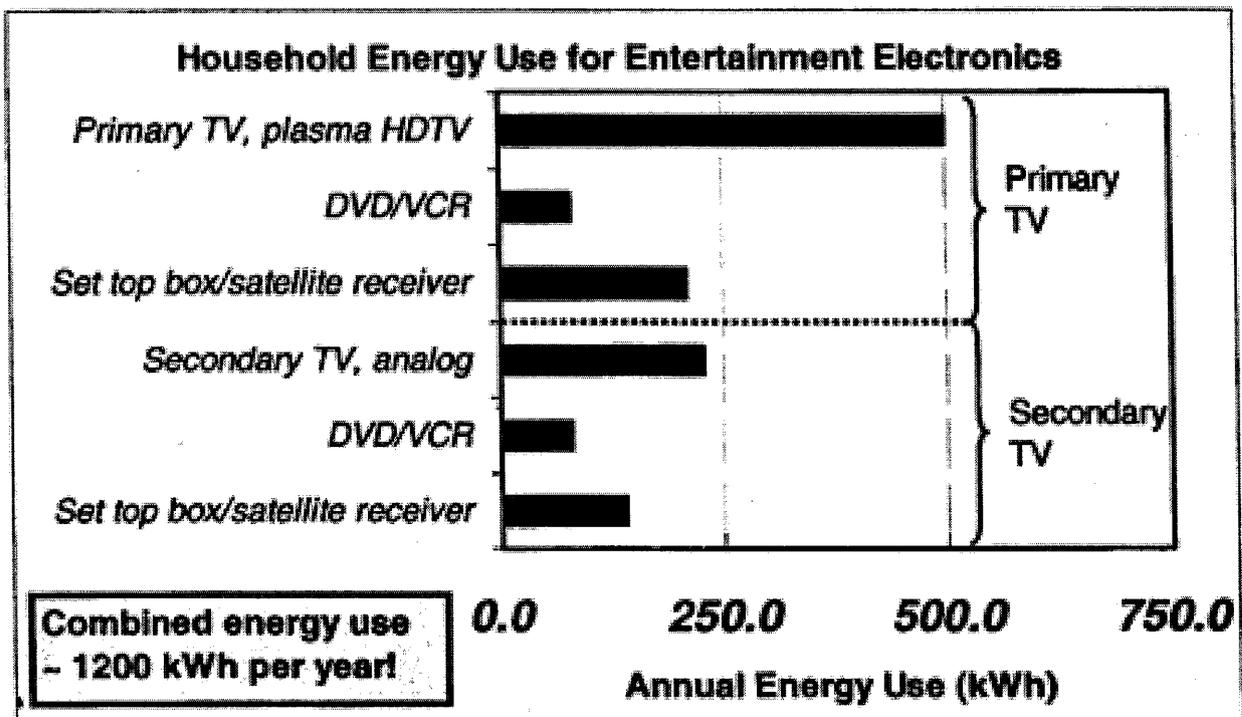
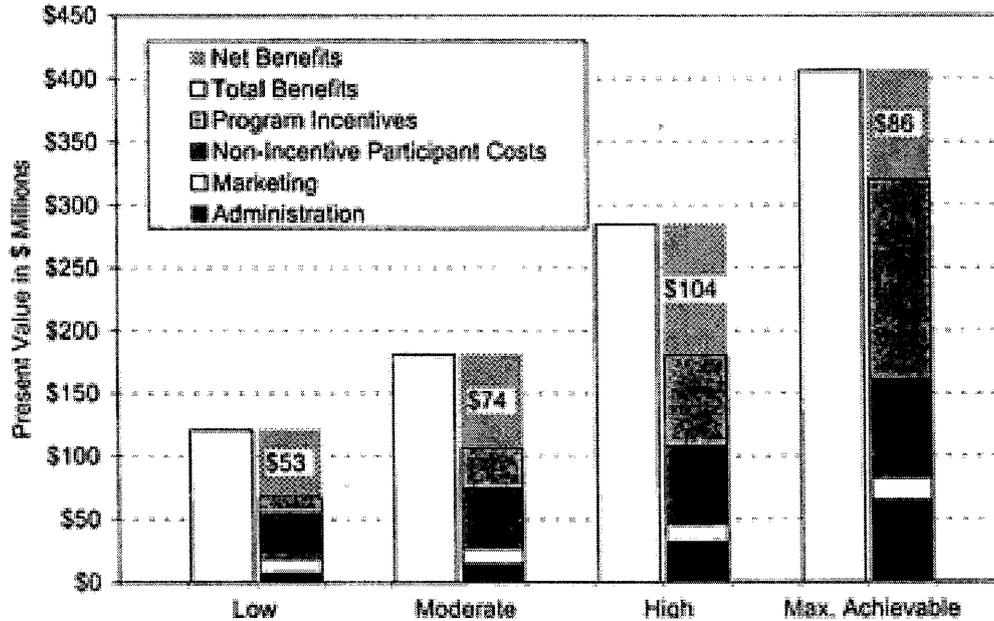
about 2 percent per year over the past decade. The initial proposal called for growth in fixed cost recovery to be tied to annual growth in the forecast of retail sales adopted in the Company's most recent IRP. Concerns were raised that, in the residential and commercial sectors particularly, growth in customer counts could substantially exceed growth in forecast sales, resulting in underrecovery of costs prudently incurred to serve new customers. **PROPOSED SOLUTION:** Tie growth in fixed cost recovery to actual measured changes in annual customer count for the residential and commercial sectors. This should allow a closer convergence between the fixed cost revenue requirement and actual costs of service.

B. RETROSPECTIVE ASSESSMENT: In cooperation with the Company, I looked into how often a true-up tied to customer counts would have increased and reduced rates, respectively, for the residential and commercial classes since 1990 (concerns had been raised that rates would always go up under such a mechanism). For any year during which such a mechanism had been in effect, rates would have gone down if the class's retail sales had grown more rapidly than the class's customer count, and vice versa. So we looked at how often the residential and commercial customer counts increased more rapidly than class-wide electricity use in each year, starting in 1990. For the commercial sector, electricity use grew more rapidly than the customer count in ten of the fourteen years from 1990-2003. For the residential sector, electricity use grew more rapidly than customer count in two of the fourteen years, and the rates of growth were essentially identical in three other years (including 2003). This confirms the potential for rate decreases as well as increases for both classes under a true-up mechanism, although based on historical data the likelihood of a rate decrease is substantially greater for the commercial sector than the residential sector. Finally, it should be emphasized that annual class-specific rate increases needed to ensure recovery of the authorized fixed-cost revenue requirement would never have exceeded two percent under the true-up mechanism. In most years, for both classes rates would have shifted up or down by one percent or less.

APPENDIX 7—BAR CHARTS DISTRIBUTED BY CAVANAGH

Exhibit ES-5

Present Value Costs and Benefits - Achievable Potential Scenarios



APPENDIX 8—FLIPCHARTS REGARDING CAVANAGH’S REVISED STRAWMAN

Assumptions for True-Up

- Last year’s consumption plus 2% to calculate the rate increase spread over kWh the next year.
- “Clear every year”—don’t want to carry significant over/underages/year
- If kWh sales exceed customer count in a class, there would be a rate decrease.
- Question: How to resolve true-up within schedules for irrigators and industrial? [how to true-up with subclasses to the classes]
- Rate impacts could be more volatile under multiple true-up values

APPENDIX 9—PROPOSED STRAWMAN FOR A PERFORMANCE-BASED MECHANISM

Strawman Proposal for DSM Performance Incentive

For Discussion at IPC Decoupling Workshop, 12/01/04

Hypotheses:

1) The primary DSM financial disincentives in question are those that affect shareholders, rather than managers. These disincentives are primarily “fixed-cost” revenues that are not collected when electricity is not sold; i.e. those portions of energy and demand prices that are based upon utility costs that do not vary with energy usage in the short run.

2) Idaho Power will fail to maximize demand-side management (DSM) potential benefits for its customers unless the primary financial disincentive is removed through a regulatory mechanism.

3) Idaho Power’s customers will be net beneficiaries if the company provides more cost-effective DSM as a result of customers paying to remove the primary financial disincentive.

4) Rate cases will occur too infrequently to sufficiently mitigate the primary financial disincentive.

5) The company is legitimately entitled to recover fixed-cost revenue losses caused by its DSM efforts regardless of the absence of rate case examination of overall costs and revenues.

6) Idaho Power is incurring new fixed costs due to customer growth and its incremental fixed costs exceed its incremental fixed-cost revenues. In other words, customer growth does not mitigate fixed-cost revenue losses.

7) It is unacceptable to the IPUC Staff to adopt a financial mechanism that would simply allow Idaho Power, without a rate case, to automatically collect all “fixed-cost losses” associated with all kWh per customer sales reductions, much of which is caused by factors not associated with the company’s DSM, e.g. increased gas market share. The 10-year lapse between Idaho Power’s last two rate cases, in spite of reduced sales per customer, is an indicator that profitability is largely independent of sales per customer.

8) It is unacceptable to Idaho Power to adopt a financial mechanism that considers only total sales; i.e. that does not account for growth in the number of customers.

9) Removing the primary financial disincentive for DSM can be reasonably accomplished through a mechanism that targets only DSM-caused sales reductions. There are two ways to do this: a) The financial disincentive could be removed by allowing specific fixed-cost revenue recovery for all verified DSM savings; b) The financial disincentive could be removed by providing other financial rewards for verified DSM accomplishments. Method b)’s financial rewards could be stand-alone or used in conjunction with method a) or with decoupling.

Strawman Trial Proposal

Unlike decoupling, both methods a) and b) above require precise measurement and verification of DSM program implementation details, baselines and DSM results, and, as such, are inherently complex, subject to measurement error, and require significant regulatory oversight. Thus, it is reasonable to implement either of these methods on a trial basis.

For a strawman trial, we have selected a proposal that combines methods a) and (b) above; i.e. recovery of DSM-caused fixed-cost revenue losses with a bonus financial incentive for exceeding cost-effective DSM targets. We suggest that the trial be restricted to the Residential New Construction program. Residential energy rates have a relatively high fixed-cost recovery component, which means that Idaho Power's financial disincentive for DSM for this class may be higher than for other customer classes. This is a comparatively small program, thus minimizing the effects of any mistakes made in the trial. Nevertheless, this program is projected to be very cost-effective for both energy and peak demand savings and "lost opportunity" will occur if it is not vigorously pursued.

The table below illustrates some of the projections for the Residential New Construction program as contained in the IRP. Also shown are discussion starting points for financially rewarding Idaho Power for significantly outperforming its projections. Whatever combination of indicators and incentives are used, the program must remain cost effective to customers.

Possible Indicators	Annual Targets	Fixed-Cost Rev. Recovery	e.g. Bonus Threshold	Bonus Financial Incentive (for illustration only)
MW reduction	0.19	n.a.	10% > target	20% of net \$ savings
MWh reduction	1,661	actual MWh saved x \$31.20	10% > target	10% of net \$ savings
Idaho Power \$/peak kW	5.30	n.a.	10% < target	5% of program costs
Idaho Power \$/kWh	0.036	n.a.	10% < target	5% of program costs
Total Resource \$/peak kW	8.50	n.a.	10% < target	5% of total costs
Total Resource \$/kWh	0.058	n.a.	10% < target	5% of total costs
Participant Payback	6.5 yr.	n.a.	10% < target	5% of participants' costs
Number of Participants	?	n.a.	10% > target	5% of program costs
Market Transformation	?	n.a.	?	5% of program costs

APPENDIX 10—FLIPCHARTS REGARDING PERFORMANCE-BASED MECHANISM

PBR/Hypothesis Discussion

- 1) Managers = utility company managers
- 2) This proposal does not address “found” revenues and has a narrow view of “lost” revenues (DSM-related only)
- 3) #7 Concern about not linking advantages of true-up with issues about increased gas market share
Staff wants fixed-cost recovery for DSM-related programs (utility co. control) → NOT consensus with group on this

- 4) Energy savings calculations would be difficult and problematic
- 5) Cost recovery may be a bigger issue than lost revenues
- 6) Proposal is for residential construction only (Energy Star program—exceeding building codes)
- 7) Some potential for perverse incentives—need to monitor closely

APPENDIX 11—ADDITIONAL SUGGESTIONS

Bin

- 1) 18-month financial simulation of proposals—real, documented numbers for FCR

Options

- 1) Model period of 10 years
 - a) “Council level” of conservation against IPUC staff proposal
 - b) True-up with “Council levels” of conservation
- Use maximum net benefit scenario:
 - rate impacts
 - IRP baseline

APPENDIX 12—INTEREST REPORTS

Interest Reports

IPC

- 1) Disallowance of program costs will kill DSM—first and foremost disincentive
- 2) Problem of lost revenues will have a...material impact on amount of load-reducing activities we undertake in short and long term
- 3) Next couple years, company will undertake DSM identified in IRP—can't take on any additional in this period (ramp-up ability limited)
- 4) 18-month simulation of T.U. mech. would help relieve uncertainties (unintended consequences) prior to next rate case
- 5) Intrigued with staff incentive mechanism, and piloting with one program then determining applicability to others

NWEC

- 1) Not convinced simulation will change minds—not interested in pursuing unless group is really committed to moving forward and simulation/test is credible with everyone and materially improve likelihood of approval by Commission
- 2) Retain right to bring proposal to Commission directly, but would rather work as a group

IPUC—Staff

- 1) Staff will continue cost-effectiveness/prudence review
- 2) Interested in pilot incentive based program. Can work on measurement and evaluation to see if doable.
- 3) 18-month simulation—main impact of T.U. mechanism is to see how it changes company's behavior. Wouldn't oppose proceeding with this, though unsure of real value of simulation. May be best we can do now to keep alive without killing it.

APPENDIX 13—NEXT STEPS AND ACTION ITEMS

Next Steps

- 1) Status report on 15th
- 2) Flesh out concept of pilot and simulation on 13th (9:00–Noon)
- 3) Provide full report in January with recommendation, what we discussed and why we're proposing this approach. Decision at end point.

- 4) IPC would submit application for pilot to commission—projected date by end of January (simultaneous with filing or at least final report first)
- 5) Assuming model can be set up, could possibly start accounting after first of year (January 1 if possible)

Action Items

What	Who	When
1) Draft status report for review and comment	Scott and Susan	12/03/04
2) Bring what is necessary for pilot proposal—outline for filing	IPC (Darlene)	12/13/04
3) Bring simulation design	IPC (Mike)	12/13/04

APPENDIX 14—WORKSHOP EVALUATION COMMENTS

+	ρ
1) Good job!	1) Room is too small and too warm
2) Frankness of conversation useful & appreciated	
3) Like smaller room	
4) Like facilitating	
5) Like someone "ramrodding it"	
6) Appreciate deadlines and follow-up	
7) First class job	

+	ρ
8) Like smaller room	
9) Like fruit!	
10) Like summaries—timely and well-structured	
11) Nice to get prework discussion items ahead of time	
12) Very important that everyone is here—adds to the process	

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13) Appreciate cheese and celery!	
14) Appreciate comprehensive summaries	
15) Enjoyed open and honest discussion, and movement in positions	
16) Like follow-up with meeting summary—that it is right	