TESTIMONY OF RANDY IWASE
CHAIR, PUBLIC UTILITIES COMMISSION
STATE OF HAWAII
TO THE
SENATE COMMITTEE ON
WAYS AND MEANS

February 21, 2018
10:08 a.m.

MEASURE: S.B. No. 2939 SD1
TITLE: RELATING TO ENERGY.

Chair Dela Cruz and Members of the Committee:

DESCRIPTION: On or before January 1, 2020, requires the public utilities commission to establish performance incentive and penalty mechanisms that directly tie electric utility revenues to the utility's achievement on performance metrics. Exempts member-owned cooperative electric utilities. (SD1)

POSITION: The Public Utilities Commission ("Commission") offers the following comments for consideration.

COMMENTS:

The Commission agrees that electric utility financial incentives should be better aligned with customer needs and the State's energy policy. The Commission is committed to protecting utility customers and ensuring that existing utility regulatory approaches are updated to reflect improving technology, changing customer preferences, and state policy goals.

The Commission is currently utilizing performance-based regulation ("PBR") through several active proceedings, including the decoupling re-examination (Docket 2013-0141), active general rate cases for each of the Hawaiian Electric Companies (Dockets 2015-0170, 2016-0328, and 2017-0150), as well as high priority initiatives such as the Demand Response portfolio and the upcoming Requests for Proposals for new renewable generation on Oahu, Maui, and Hawaii islands (Dockets 2015-0412 and 2017-0352).

As part of these proceedings, over the course of several years, the Commission has established numerous PBR components that now make up the current regulatory framework. Such components include a 3-year rate plan for each of the HECO Companies, with capped revenues in between rate cases. In addition, the Commission has adopted performance incentives for the HECO Companies, targeting customer service and grid reliability. The Commission is also developing new performance incentives to reward exceptional utility performance in successfully executing the upcoming solicitations for new renewable generation and acquiring grid services from customers.

In the first half of 2018, the Commission intends to open a proceeding to further examine PBR frameworks, which is expected to include additional performance incentives and further regulatory reform to better align utility incentives with customer needs and state energy policy.

Thank you for the opportunity to testify on this measure.

TESTIMONY BEFORE THE SENATE
COMMITTEE ON WAYS AND MEANS

S.B. No. 2939, SD1 – Relating to Energy

Wednesday, February 21, 2018
10:08 am
State Capitol, Conference Room 211

Kevin M. Katsura
Assistant Deputy General Counsel (Regulatory), Legal Department
Hawaiian Electric Company, Inc.

Chair Dela Cruz, Vice Chair Keith-Agaran, and Members of the Committee:

My name is Kevin Katsura and I am submitting testimony on behalf of Hawaiian Electric Company and its subsidiary utilities Maui Electric Company and Hawaiʻi Electric Light Company. The Companies support the intent of S.B. 2939, SD1, however, oppose it in its current draft because it is potentially too prescriptive and overbroad.

The Companies support carefully designed incentive based regulation, a.k.a., performance based ratemaking ("PBR"). Indeed, this bill may be unnecessary because the Companies have recommended in Hawaii Public Utilities Commission ("Commission") proceedings that an investigatory docket be opened to fully review and develop a comprehensive PBR Framework. In an order issued by the Commission last year, the Commission noted that it "intends to commence a separate proceeding to comprehensively review the issues of performance-based ratemaking and performance incentive mechanisms."[1] The Commission has reiterated its intention to open a comprehensive PBR proceeding in other decisions issued within the past year.[2]

In addition, the Commission recently directed the Companies to file Performance Incentive Mechanism and Revenue Balancing Account tariffs regarding reliability and call center performance to be effective January 1, 2018, in Docket No. 2013-0141. The Commission also expressed its intention to establish performance incentives that reward exceptional performance in the Companies' procurement of renewable energy (Docket No. 2017-0352), and in Demand Response Portfolio outcomes (Docket No. 2015-0412).

However, if the bill were to move forward, the Companies respectfully submit that it would be better to establish a framework of principles within which the scope of PBR and the incentives themselves should be developed rather than jumping ahead

[1] Order No. 34502, issued on April 13, 2017 in Docket No. 2015-0170, at page 15.
[2] For instance, see the Commission's Order No. 34664, issued on June 28, 2017 in Docket No. 2016-0328, at page 26.

and prescribing specific outcomes now. This is because PBR models can be designed in many different ways for many different purposes. Like any change in regulatory ratemaking, the basic principles of a PBR model should be first established, and great care should be given to avoid unintended consequences. Thus, PBR can more quickly and effectively be developed and implemented if principles, such as the following, are first established.

PBR is best considered as an adaptation to traditional rate-making rather than a completely new and different approach. All PBR plans are founded on cost-based rates determined in the same way as a traditional general rate case. Incentives can then be layered on top of the cost-based rates to encourage desired outcomes. If, over time, the desirable outcomes are achieved, the utility will earn a greater return than it would have done under traditional ratemaking. Conversely, if the desirable outcome is not achieved, the utility will earn a smaller return than it would have done under traditional ratemaking.

The utility should bear risk from factors that are within management control but should not bear the risk from factors that are outside its control. PBR plans frequently incorporate a mechanism to pass through changes in elements of cost that are outside management control, such as fuel prices or changes in taxation. PBR plans also frequently incorporate sales decoupling so that management does not have a conflict between the policy goals of energy conservation and promoting distributed energy resources and the fact that lower retail sales will lower profits. Targets should be realistic and attainable and consistent with funding levels and measurement of results should be objective.

A PBR plan must provide the utility with a reasonable opportunity to earn a fair rate of return. Employing a PBR plan does not change the applicable regulatory standards and protections associated with determining an authorized rate of return.

Incentives to achieve clean energy goals and other specific outcomes, can be developed based on and should be consistent with the underlying service and resource plan on which the PBR plan is based.

Well-designed PBR plans tend to have a small number of incentives in key performance areas. There are limits on the total amount of revenue that can be put at risk through incentive schemes, so if there are too many individual incentives the strength of any one incentive will be diluted.

As drafted, this bill does not establish a framework of principles that should anchor the development of specific incentives. It also requires that all aspects of rates should be tied to performance metrics, and prescribes the objectives that must be considered for outcomes, which are overbroad, too complicated and may be counter-productive. Such a framework would make the Company subject to penalties and rewards for factors outside of its control and potentially expose the Company and ultimately its customers to higher levels of risk that could affect the Company’s financial state, its ability to invest in electrical and renewable infrastructure and the provision of reliable service.

Finally, specific outcomes to be incentivized should support the Companies’ Power Supply Improvement Plans as accepted by the Commission in Docket No. 2014-0183 and/or desired outcomes established in the Commission’s ongoing Distributed Energy Resource (“DER”) docket (Docket No. 2014-0192) to name a few. The seven objectives listed in this bill seem to predetermine outcomes in those dockets.

Accordingly, the Hawaiian Electric Companies oppose S.B. 2939, SD1 as drafted.

Thank you for this opportunity to testify.