

Revenue Decoupling

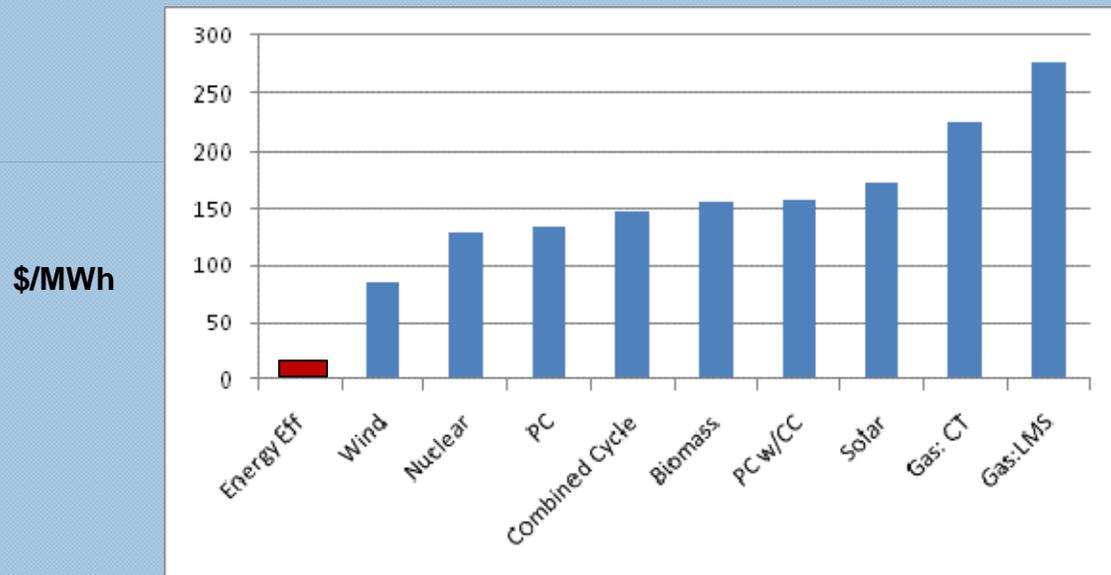
**Removing Ratemaking Disincentives to Utility
Energy Efficiency Programs**

Science, Technology and Telecommunications
Committee

July 19, 2010



Energy efficiency is PNM's least cost resource alternative



The power to make life better. **Together.**



Rate regulation creates disincentives to Utility investments in energy efficiency



- Utility revenues and profits are linked to sales (kW, kWh, Terms, etc.)
- Loss of sales due to successful implementation of energy efficiency will lower utility profitability

Revenue decoupling is a solution

A ratemaking approach that encourages Utility EE by eliminating the link between kWh sales and revenues.

Allows a utility to adjust rates to recover Commission approved revenues independent of sales level.

Rate design example

Fixed Cost = \$200

Customers = 10

200 kWh/Customer

Sales = 2,000 kWh

Straight Fixed/Variable Pricing

Fixed Cost of \$200

Divided by

10 customers

equals

Rate of \$20/customer

Variable Pricing

Fixed Cost of \$200

Divided by

2000 kWh

equals

Rate of 10¢ per kWh

The energy efficiency pricing problem

- One customer reduces electricity usage by 50%
 - Total sales are $(9 \times 200) + (1 \times 100) = 1,900$ kWh
- Earnings impact to the Company
 - Total Revenues are $1,900 \text{ kWh} \times 10\text{¢} = \190
 - But PNM's Total Fixed Costs = \$200
 - Resulting in a **Net Loss** = **(\$10)**

A decoupling example

- PRC establishes allowable revenue at \$20/customer
 - $\$20 \times 10 \text{ customers} = \200
- Utility collects an average of \$19 per customer
 - $\$190 \text{ divided by } 10 = \19
- Therefore each of the 10 customers are surcharged \$1
 - $\$20 \text{ allowed} - \$19 \text{ actually collected} = \1

Decoupling *Pros & Cons*

Pros

Removes utility disincentive to pursue energy efficiency

Avoids more frequent rate cases

Provides additional justification for inclining block rates

Cons

Customers who reduce consumption often see decoupling as a penalty

Customers may see decoupling as an added subsidization

12 States have decoupled electricity service

- California
- Connecticut
- District of Columbia
- Hawaii
- Idaho
- Maryland
- Massachusetts
- Michigan
- New York
- Oregon
- Vermont
- Wisconsin