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September 2, 2008

The Honorable Michael W. Sole, Secretary
Florida Department of Environmental Protection
Chair, Florida Governor's Action Team on Energy and Climate Change
3900 Commonwealth Blvd., MS49
Tallahassee, Florida 32399

Subject: Rebuttal to Florida Power & Light Company (FPL) Response to the Florida Climate Action Team Regarding Proposed Policy ESD-23

Dear Secretary Sole:

I read with interest Armando J. Olivera's letter to you regarding decoupling. While the subject of the letter is ostensibly decoupling of electricity rates, the discussion is framed in the context of a glowing report on the past history of energy efficiency in Florida.

Mr. Olivera suggests the discussion in the draft policy on decoupling being considered by the Florida Climate Action Team suggests "that utilities are not investing in conservation." Mr. Olivera claims that instead, "Florida's experience with energy efficiency reflects a history of outstanding support for these programs," and the further claim that FPL's programs have led to "industry-leading results."

With respect to the draft policy on decoupling, Mr. Olivera's characterization of the draft is incorrect as there is simply no discussion regarding the level of conservation investments by Florida utilities, positive or negative. The draft explains the general perspective that the state's regulatory framework results in "a perverse incentive for utilities to increase sales in order to boost revenues and minimize investments in energy efficiency . . ." This can hardly be characterized as a claim that utilities haven't or won't invest in conservation at some level.

The discussion about decoupling should be held on its own merits. Rate structures designed in the 20th century to ensure universal access to electricity and promote it as an engine of economic development are, in our opinion, not well suited to the 21st century mission of achieving energy independence and reduced global warming pollution through more efficient use of energy. Decoupling is a strategy to better align the interests of utility investors with the public interest in efficiency.

I would refer you to a letter of August 22 from Dale Bryk of Natural Resources Defense Council that engages the substantive issues surrounding decoupling. We are happy to continue the discussion further if need be.

For the remainder of this letter, I would like to engage two arguments that Mr. Olivera makes in support of his decoupling critique. First, he implies that as FPL is an industry leader in what he describes as energy efficiency, and there is no decoupling in Florida, therefore decoupling isn't needed and we can continue with the status quo. Second, he points the finger at other states which have failed to take any steps to offer energy efficiency programs at meaningful levels. We can hardly disagree with this latter point, as other states need to step forward. Nevertheless, Governor Crist's call to reduce global warming emissions can hardly be met by utilities operating in other states.

The data that Mr. Olivera cites as evidence that FPL is an industry leader fail to support critique of decoupling in two ways.

- FPL's track record on energy efficiency demonstrates precisely the shortcomings that decoupling would address.
- FPL's track record, while hardly that of an industry leader, is not representative of the even weaker performance of other large utilities in Florida.

Although energy efficiency is a cost-effective strategy to achieve energy independence and reduce global warming pollution, it runs counter to the financial interests of investor-owned utilities in maintaining a highly lucrative regulatory framework.

FPL Track Record On Efficiency

Among the 100 utilities with the largest sales in the country (see Table 1), FPL barely cracks the top twenty in terms of its annual reductions in energy sales (MWh) due to its energy efficiency programs. FPL deserves credit for being the only Florida utility to merit this recognition. Nevertheless, *FPL's performance is an order of magnitude lower* than several large, investor-owned utilities in California, the Pacific Northwest, the Midwest, and the Northeast.

Table 1: Energy Savings (Conservation) Performance of Large Utilities, 2006

Utility	State	Ownership	Total Sales (GWh)	Annual Savings	
				(GWh)	(%)
Massachusetts Electric	MA	Investor Owned	12,990	257	1.98%
Connecticut Light & Power	CT	Investor Owned	22,109	265	1.20%
Pacific Gas & Electric	CA	Investor Owned	76,817	780	1.01%
Southern California Edison	CA	Investor Owned	78,863	788	1.00%
Interstate Power and Light	IA	Investor Owned	16,026	134	0.84%
Puget Sound Energy	WA	Investor Owned	21,092	166	0.79%
Sacramento Municipal Utility	CA	Municipal	10,799	79	0.73%
Northern States Power	MN	Investor Owned	35,923	258	0.72%
Nevada Power Company	NV	Investor Owned	21,101	146	0.69%
MidAmerican Energy	IL	Investor Owned	23,389	156	0.67%
Wisconsin Power & Light	WI	Investor Owned	10,580	66	0.63%
City of Seattle	WA	Municipal	9,455	52	0.55%
Idaho Power	OR	Investor Owned	13,939	71	0.51%
Long Island Power Authority	NY	State	18,354	92	0.50%
PacifiCorp	WY	Investor Owned	51,797	193	0.37%
Arizona Public Service	AZ	Investor Owned	27,970	80	0.29%
Wisconsin Electric Power	MI	Investor Owned	28,189	68	0.24%
Public Service Elec & Gas	NJ	Investor Owned	34,354	68	0.20%
Florida Power & Light	*FL*	*Investor Owned*	*103,653*	*200*	*0.19%*
Tennessee Valley Authority	TN	Federal	33,008	61	0.19%

Source: Energy Information Administration, Form 861 Database.
Note: Large utilities are defined as the 100 utilities with the largest total electricity sales. When compiled at the level of parent companies, Progress Energy and Southern Company, each with a Florida affiliate, join FPL among the 10 largest utility systems in the nation. However, neither holding company has a distinguished level of energy savings performance and thus their affiliates do not appear on this list. See Table 2 for further details regarding Florida utilities.

In contrast to a ranking of 19th in terms of annual energy savings, Mr. Olivera ranks FPL as "the No. 1 electric utility in the nation." This accomplishment, along with all the other data presented by Mr. Olivera, reflects demand reduction, not energy savings. Demand reduction is a meaningful accomplishment, but it is not the correct measurement to apply in this context.

Energy Savings (Conservation) Compared to Demand Reduction

The most widely accepted benchmark for energy efficiency program performance is annual energy savings. For example, the *National Action Plan for Energy Efficiency* states that "well-designed energy efficiency programs are delivering annual energy savings on the order of 1 percent of electricity and natural gas sales" (page ES-4). FPL is currently achieving annual energy savings of 0.2 percent, which is significant but not "industry-leading."

The distinction is central to the issue of decoupling in the context of a vertically integrated investor-owned utility. Traditional electric rate regulation creates an incentive to increase sales during off-peak periods, and decrease sales (or costs) during on-peak periods. Theory suggests that when such utilities pursue "energy efficiency," they tend to focus more intensely on demand reduction programs that improve shareholder earnings.

Until the 2008 Florida energy bill was passed, there was a second factor in Florida law that reinforced the "natural" emphasis on demand reduction, which was use of the rate impact measure (RIM) test as the basis for identifying "cost-effective energy efficiency" programs that would be the basis for setting Florida's energy efficiency goals.

In the context of the mission of the Florida Climate Action Team, the distinction is even more important. Demand reduction (fewer MW) reduces the *number* of power plants, but energy savings (conservation, fewer MWh) reduces the *operation* of power plants. **Energy savings, not demand reduction, is the path to reduced global warming pollution from the electric utility sector.**

Energy Savings (Conservation) Performance of Florida Utilities

While FPL operates Florida's largest energy efficiency program in terms of both absolute demand (MW) and energy (MWh) savings, it is not unique in its overemphasis on demand reduction. One common industry benchmark to evaluate the character of an energy efficiency program is to compare the ratio of energy savings to demand reduction (GWh/MW).

This rather simple comparison can provide further insight into the program focus. A small GWh/MW ratio means that for the utility's programs, the results will tend to favor reductions in peak demand – a reduction in the number (or capacity) of power plants needed and overall customer *rates*. A large GWh/MW ratio means that the results will tend to favor reductions in energy savings – a reduction in the total amount of energy used and overall customer *costs*.

For the 20 utilities listed above (Table 1), the GWh/MW ratio averages approximately 0.54.[1] In contrast, of the 15 largest utilities in Florida (Table 2, selected by total utility sales), only two have large GWh/MW ratios that demonstrate a focus on energy savings. It is no accident that these two utilities are public and thus not subject to the structural disincentive to conservation that the current regulatory system favors.

The high GWh/MW performance of these industry-leading utilities tends to reflect goals that have been set at the state level to achieve strong results. For example, the California utilities have 2006-2008 goals established by the California Public Utilities Commission of 5,065 GWh in customer energy savings to 1079 MW in demand reduction, or a ratio of approximately 4.8.[2] Similarly, New York's System Benefits Charge program through 2007 has achieved 3,060 GWh of energy efficiency savings as compared to 1,200 MW of permanent and curtailable demand reduction, for a ratio

[1] One utility, PacificCorp, does not report peak demand reduction in 2006 and is excluded from the calculation. Only one utility, Wisconsin Electric Power, had a similarly low GWh/MW ratio to FPL. Other utility scores were at least double that of FPL.

[2] California Public Utilities Commission. Decision 04-09-060. Issued September 23, 2004.

of approximately 2.6.[3] Over a similar period, Texas investor-owned utilities achieved 2,005 GWh of energy reduction and 756 MW of peak demand reduction for a ratio of 2.7.[4]

In contrast, Florida's largest utilities have ratios of 0.03 to 0.26. This performance is precisely what one would expect in a state in which the utility shareholder's face a financial disincentive to support programs with an emphasis on energy savings (conservation). And if the lack of decoupling (or some other solution to the throughput incentive) creates a landscape that is tilted against energy savings, then the historical use of the RIM test to screen programs is the push that has sent Florida's largest utilities down to the bottom end of the scale.

Table 2: Energy Savings (Conservation) Performance of Florida Utilities, 2006

Utility	Ownership	Total Sales (GWh 2006)	Annual Energy Savings			Demand Reduction (MW 2006)	GWh/MW
			GWh 2006	% 2006	% 2007		
City of Tallahassee	Municipal	2,714	11	0.40%	0.33%	1	10.79
Florida Power & Light	Investor Owned	103,653	200	0.19%	0.21%	1,385	0.14
Gainesville Regional Utilities	Municipal	1,849	3	0.18%	0.75%	-	0.00
Tampa Electric	Investor Owned	19,025	26	0.14%	0.11%	166	0.15
Gulf Power	Investor Owned	11,429	12	0.11%	0.12%	47	0.26
Progress Energy Florida	Investor Owned	39,432	38	0.10%	0.11%	1,253	0.03
JEA	Municipal	12,800	13	0.10%	†	1	12.70
Lee County Electric Coop	Cooperative	3,505	4	0.10%	†	46	0.08
Sumter Electric Coop	Cooperative	2,571	3	0.10%	†	51	0.05
Orlando Utilities Commission	Municipal	5,465	†	0.00%	†	†	0.00
Withlacoochee River Electric Coop	Cooperative	3,571	0	0.00%	†	55	0.00
Clay Electric Cooperative	Cooperative	3,155	†	0.00%	†	†	0.00
City of Lakeland	Municipal	2,883	0	0.00%	†	†	0.00
City of Ocala	Municipal	1,380	-	0.00%	†	-	0.00
Kissimmee Utility Authority	Municipal	1,357	-	0.00%	†	-	0.00

Source: Energy Information Administration, Form 861 Database, except that 2007 data are per Florida Public Service Commission.
† - No data reported.
‡ - Demand reduction is calculated to include the actual demand reduction associated with energy efficiency measures installed in 2006 and the potential demand reduction associated with demand response measures operational in 2006.

[3] *New York Energy $mart Program: Evaluation Status Report Year Ending December 31, 2007. Report to the System Benefits Charge Advisory Group.* Final Report March 2008. New York State Energy Research and Development Authority (NYSERDA).
[4] *Energy Efficiency Accomplishments of Texas Investor Owned Utilities – years 1999 through 2006.* Frontier Associates LLC. Page 2. July 12, 2007.

In summary, our impression of Florida's track record with respect to energy efficiency is not as rosy as expressed by Mr. Olivera. We are not unique in this perspective. HB 7135 shows the Florida Legislature's intent to address barriers to greater efficiency as it tasked the Florida Public Service Commission to evaluate utility revenue decoupling, and make recommendations to the Governor and the legislature by January 1, 2009, as a potentially powerful tool to unleash greater energy efficiency in Florida.

Electricity consumers in Florida look to our utility regulators to best manage their electricity cost, risks and opportunities, to obtain reasonable value while assuring access to safe, reliable energy for everyday life, now and in the future. Decoupling is especially needed to help smaller consumers in dealing with capital costs vs. fuel costs. The basis for the rate structure and the rate-setting process in Florida has a lot to do with who bears the risks, the customer or the utility.

While we agree with Mr. Olivera that many states and utilities have failed to measure up to Florida's standard, we should be looking at the leading programs across the country, not failures, to set the bar. We have reviewed many of the energy efficiency programs across the country that deliver annual energy savings on the order of 1 percent of electric sales. Most of these programs meet one of the following criteria:

- Public utility
- Deregulated investor-owned utility (few or no power plants, primarily "load serving")
- Vertically integrated investor-owned utility with lost revenue recovery, decoupling, or a very strong financial performance incentive
- Third-party administrator

That energy efficiency programs can thrive with such a variety of strategies to ensure their financial sustainability should suggest to Florida that it has options – but should not stick with the status quo.

Leading utilities recognize the impact of strong performance on their bottom line. For example, Alliant Energy's two regulated subsidiaries, Interstate Power & Light and Wisconsin Power & Light, both have "top ten" energy savings performance (see Table 1). In Alliant Energy's annual report, the company notes that it is examining requesting what could be either decoupling or a lost revenue adjustment mechanism.

> With increased emphasis on energy conservation as a matter of public policy, IPL and WPL are continuing and, where appropriate, expanding initiatives to promote energy conservation and enhance customers' ability to manage their energy use more efficiently. IPL and WPL are also exploring rate making alternatives which are expected to maintain their respective financial stability in the event that energy use declines, and avoid penalizing IPL and WPL for successful energy conservation initiatives.[5]

Overall, when reviewing what factors determine a utility's enthusiasm for energy savings, two factors stand out: state policy direction (e.g., a mandatory state efficiency standard or similar policy direction from a state utility commission) and the

[5] Alliant Energy, Form 10-K filed with US Securities and Exchange Commission for year ending December 31, 2007.

absence of a financial disincentive to utility performance on energy efficiency. Notably, high electric rates are not as consistent a predictor of performance as many utilities suggest. Although many strong programs are operated in California or the Northeast (where electric rates are high), strong programs are operated in several states with rates comparable to or lower than Florida. For example, 2007 revenues for Alliant Energy are about 8 cents per kWh. In short, Florida has not adopted key best practices that lead utilities to perform at high levels of energy efficiency, and the lack of performance is evident.

Exaggerated claims about performance and limited results help show why the FL Legislature was correct to direct the PSC to replace the RIM test and develop a replacement that captures more energy efficiency, such as the total resource cost (TRC) test. We're looking for energy efficiency in Florida to reduce consumer electric bills, improve energy efficiency, avoid unnecessary capital investment, promote economic security and substantially reduce production of dangerous greenhouse gases. We are counting on your leadership to keep Florida focused on these outcomes.

Sincerely,

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