**Addendum to the EISA PURPA Standards Manual**
Kenneth Rose, March 17, 2009

## I. Technical Corrections in the American Recovery and Reinvestment Act of 2009 of the PURPA Standards in the Energy Independence and Security Act of 2007

The ''American Recovery and Reinvestment Act of 2009" (ARRA), also know as the "Stimulus Bill," corrected mistakes contained in the Energy Independence and Security Act of 2007 (EISA). These mistakes occurred in the sections that added four new standards to the Public Utility Regulatory Policies Act of 1978 ("PURPA). The relevant EISA sections are in the Appendix of the "Reference Manual and Procedures for Implementation of the 'PURPA Standards' in the Energy Independence and Security Act of 2007" (EISA standards manual), released on August 11, 2008. Section 1 of the EISA standards manual contains a discussion of the errors and implementation impact for state commissions and nonregulated utilities.

The following is the section in the ARRA with the "technical correction:"

> SEC. 408. TECHNICAL CORRECTIONS TO PUBLIC UTILITY REGULATORY POLICIES ACT OF 1978. (a) Section 111(d) of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. 2621(d)) is amended by redesignating paragraph (16) relating to consideration of smart grid investments (added by section 1307(a) of Public Law 110-140) as paragraph (18) and by redesignating paragraph (17)relating to smart grid information (added by section 1308(a) of Public Law 110-140) as paragraph (19).
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> (b) Subsections (b) and (d) of section 112 of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. 2622) are each amended by striking ''(17) through (18)'' in each place it appears and inserting ''(16) through (19)''.

Subsection (a) of this paragraph renumbers the smart grid standards that were added by section 1307(a) of EISA. The standards in section 532(a) of EISA remain numbered as they were in the 2007 statute. Both of the "smart grid" standards were in section 1307(a) – the second standard (now renumbered as "19") was not in section 1308(a) as stated in the ARRA paragraph (a mistake in the "correction").[1] However, since the paragraphs refers to PURPA section 111(d), which was amended by EISA, it should be apparent which standards to renumber. Unfortunately, the erroneous reference in the correction may still cause some confusion.

[1] Section 1308 of EISA is for the "Study of the Effect of Private Wire Laws on the Development of Combined Heat and Power Facilities." There is no PURPA standard in that section of EISA.

The renumbered EISA standards are:

(16) INTEGRATED RESOURCE PLANNING
(17) RATE DESIGN MODIFICATIONS TO PROMOTE ENERGY EFFICIENCY INVESTMENTS
(18) CONSIDERATION OF SMART GRID INVESTMENTS
(19) SMART GRID INFORMATION

Subsection (b) of the ARRA technical correction deals with section 112(b), "time limitations," and 112(d), "prior state actions." This corrects the problems discussed in section 1 of the EISA standards manual with the numbering of the standard references in those sections. First, the two standards previously labeled as "(16)" did not have a time limit specified. With the correction, state commissions and nonregulated utilities have one year after enactment (which was December 19, 2008) to begin consideration or set a hearing date for consideration and up to two years after enactment (December 19, 2009) to complete their consideration and make a determination on whether or not to adopt the standard for all four EISA standards.[2]

Second, the ARRA also corrects the two standards labeled "(16)" in EISA that, in effect, had no prior state action waiver since PURPA was amended previously to refer to specific standards and the 2007 statute only amended PURPA for the standards labeled as "(17)" (and a standard "(18)" that did not exist the way the 2007 statute was written). This correction means that states and nonregulated utilities are not required to consider and make a determination on the standards *if* they had previously considered those standards or comparable standards. However, this grandfathering provision of PURPA was also amended by the Energy Policy Act of 2005 (EPAct). When the U.S. Code was revised after EPAct was passed, the phrase in EPAct "before the enactment of this subsection" (section 1251(d)) was interpreted as the actual date of enactment of the 2005 law, or August 8, 2005 (see 16 USCA §2622(d)).[3] EISA in 2007 with the ARRA correction, only added the phrase "and paragraphs (16) through (19)" and did not change the specific date or define "enactment date" for PURPA §112(d). ARRA did not address the date either. As a practical matter, if a state or nonregulated utility took prior action before August 8, 2005, the grandfathering provision would apply. Given the way the statute is written, there is a possibility that action taken between August 8, 2005 and December 19, 2007 (EISA's enactment date) would not fall within the grandfathering provision.

[2] Because of the obvious errors in the statutory language, it was advised in the EISA standards manual to consider all four of the standards in the same time frame as that specified for standards labeled "(17)." State commissions and nonregulated utilities that were following this or a similar assumption are already past the beginning the consideration phase and are in the second phase of deciding whether to adopt the standards or not – or have already determined that a comparable standard has been considered or implemented.

[3] As modified by the Office of the Law Revision Counsel of the U.S. House of Representatives. It is not clear if Congress intended to permanently affix the date of enactment of this revised PURPA subsection as the date of the 2005 law. In previous amendments and other subsections, the phrase in the law itself was used, not the specific date of enactment.

## II. Discussion of the Section 410(a)(1) Requirements for Grant Qualification in the ARRA

Section 410 of ARRA provides that the grant money authorized by the law is available "*only if the governor of the recipient State notifies the Secretary of Energy in writing that the governor has obtained necessary assurances that each of the following [three requirements] will occur*."[4] The entire text of Section 410 is at the end of this Addendum; the first requirement in subsection 410(a)(1) is the focus here (this paragraph is shown in italics in the excerpt).[5]

Breaking the paragraph down into two segments, the first states that "*[t]he applicable State regulatory authority will seek to implement, in appropriate proceedings for each electric and gas utility, with respect to which the State regulatory authority has ratemaking authority . . .*." The implication is that the requirements apply to electric and gas utilities that are regulated by the state with respect to ratemaking. It appears, therefore, that this does not apply to nonregulated (non-jurisdictional) utilities in the state. The section requires that the "*governor has obtained necessary assurances*" that the "*regulatory authority will seek to implement*" the requirements of subpart (a)(1). This language appears to retain considerable state authority and discretion, in the context of their particular regulatory authority.

The second segment of the paragraph requires,

> *. . . a general policy that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently and that provide timely cost recovery and a timely earnings opportunity for utilities associated with cost-effective measurable and verifiable efficiency savings, in a way that sustains or enhances utility customers' incentives to use energy more efficiently*. [ARRA Section 410(a)(1).]

It is significant in terms of legislative construction that the requirement is broadly constructed and does not specifically mandate a particular ratemaking methodology, including "decoupling," which is generally defined as "decoupling revenues or profits

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[4] ARRA's § 410(a)(1) conditions apply to the funds authorized for State Energy Efficiency Grants authorized under Part D, Title III of the Energy Policy and Conservation Act (42 USC § 6321 et seq). Procedures for receiving financial assistance are provided by the U.S. Department of Energy in http://apps1.eere.energy.gov/wip/pdfs/sep_arra_foa.pdf. This includes how the governor is to "provide assurance" and the "Governor's Assurance Certification" (Attachment 3 of the DOE document).

[5] The second requirement concerns the adoption of building codes and the third that the state will "prioritize the grants toward funding energy efficiency and renewable energy programs." All three requirements are shown in the excerpt from ARRA at the end of this Addendum.

from utility sales" in the ratemaking process.[6] Decoupling is intended to provide recovery of lost revenue from energy efficiency programs, neutralize utility incentives to increase sales, and also reduce possible disincentives to implementing programs that could decrease sales. This ratemaking mechanism is discussed in part 4 of the EISA standards manual.

It is also important to note that section 410(a)(1) of ARRA is different than the PURPA standards in that PURPA standards do not require that state commissions actually implement the relevant standard (as discussed in detail in the EISA standards manual). In the past, the statutory language was neutral as to whether a commission should or should not adopt any particular PURPA standard. This section is different because the legislation requires states to "seek to implement" the policy stated in the paragraph in order to receive the funding. This language appears to indicate that a state commission will, at a minimum, consider whether and how to take steps to change their ratemaking practices to align utility incentives with helping their customers use energy more efficiently. It is not clear whether the "seek to implement" formulation gives the commission some ability to say "we tried and failed," since it is of a different character than the PURPA-type "consideration" process.

The question for regulatory authorities is, when giving assurance to their respective governors, what is "a general policy that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently . . ."? A "decoupling" policy would fit the description of the ARRA paragraph, but it clearly is not the only available policy that would conform to and meet the necessary assurance. Alternative policies or regulatory mechanisms for timely cost recovery of energy efficiency program costs that could possibly also fulfill the ARRA requirement include:

- More frequent rate cases to reduce regulatory lag in cost recovery.
- Use of a future test year in ratemaking, where costs, sales, and revenues are projected and forward-looking rates to send efficient price signals to customers.
- Rate design methods that limit the recovery of fixed costs through variable charges (such as a straight fixed variable rate).
- Utility incentives for efficiency investments, including accelerated depreciation for related capital investments, and incentive returns.
- Other methods that provide a return on the investment in energy efficiency.

[6] Previous versions of what became the ARRA legislation contained language that the state needed to implement that first two PURPA standards in EISA; that is, adopt standard (16) "Integrated Resource Planning" and standard (17) "Rate Design Modifications to Promote Energy Efficiency Investments" (the complete language of these standards with discussion are in the EISA standards manual). Since Congress dropped this specific language may indicate that Congress intended some leeway in how this paragraph is interpreted.

## Section 410 of the American Recovery and Reinvestment Act of 2009

SEC. 410. ADDITIONAL STATE ENERGY GRANTS. (a) IN GENERAL.—
Amounts appropriated under the heading ''Department of
Energy—Energy Programs—Energy Efficiency and Renewable
Energy'' in this title shall be available to the Secretary of Energy
for making additional grants under part D of title III of the Energy
Policy and Conservation Act (42 U.S.C. 6321 et seq.). The Secretary
shall make grants under this section in excess of the base allocation
established for a State under regulations issued pursuant to the
authorization provided in section 365(f) of such Act only if the
governor of the recipient State notifies the Secretary of Energy
in writing that the governor has obtained necessary assurances
that each of the following will occur:

*(1) The applicable State regulatory authority will seek to implement, in appropriate proceedings for each electric and gas utility, with respect to which the State regulatory authority has ratemaking authority, a general policy that ensures that utility financial incentives are aligned with helping their customers use energy more efficiently and that provide timely cost recovery and a timely earnings opportunity for utilities associated with cost-effective measurable and verifiable efficiency savings, in a way that sustains or enhances utility customers' incentives to use energy more efficiently.*

(2) The State, or the applicable units of local government that have authority to adopt building codes, will implement the following:

(A) A building energy code (or codes) for residential buildings that meets or exceeds the most recently published International Energy Conservation Code, or achieves equivalent or greater energy savings.

(B) A building energy code (or codes) for commercial buildings throughout the State that meets or exceeds the ANSI/ASHRAE/IESNA Standard 90.1–2007, or achieves equivalent or greater energy savings.

(C) A plan for the jurisdiction achieving compliance with the building energy code or codes described in subparagraphs (A) and (B) within 8 years of the date of enactment of this Act in at least 90 percent of new and renovated residential and commercial building space. Such plan shall include active training and enforcement programs and measurement of the rate of compliance each year.

(3) The State will to the extent practicable prioritize the grants toward funding energy efficiency and renewable energy programs, including—

(A) the expansion of existing energy efficiency programs approved by the State or the appropriate regulatory authority, including energy efficiency retrofits of buildings and industrial facilities, that are funded—

(i) by the State; or

(ii) through rates under the oversight of the applicable regulatory authority, to the extent applicable;

(B) the expansion of existing programs, approved by the State or the appropriate regulatory authority, to support

renewable energy projects and deployment activities, including programs operated by entities which have the authority and capability to manage and distribute grants, loans, performance incentives, and other forms of financial assistance; and

(C) cooperation and joint activities between States to advance more efficient and effective use of this funding to support the priorities described in this paragraph.

(b) STATE MATCH.—The State cost share requirement under the item relating to ''Department of Energy; Energy Conservation'' in title II of the Department of the Interior and Related Agencies Appropriations Act, 1985 (42 U.S.C. 6323a; 98 Stat. 1861) shall not apply to assistance provided under this section.

(c) EQUIPMENT AND MATERIALS FOR ENERGY EFFICIENCY MEASURES AND RENEWABLE ENERGY MEASURES.—No limitation on the percentage of funding that may be used for the purchase and installation of equipment and materials for energy efficiency measures and renewable energy measures under grants provided under part D of title III of the Energy Policy and Conservation Act (42 U.S.C. 6321 et seq.) shall apply to assistance provided under this section.