PROJECT NO. 33487

AMENDMENTS TO ENERGY EFFICIENCY RULES AND TEMPLATES	**§**	**PUBLIC UTILITY COMMISSION OF TEXAS**

ORDER ADOPTING THE REPEAL OF §25.181 AND §25.184 AND OF NEW §25.181 AS APPROVED AT THE MARCH 26, 2008 OPEN MEETING

The Public Utility Commission of Texas (commission) adopts the repeal of §25.181, relating to Energy Efficiency Goal, and §25.184, relating to Energy Efficiency Implementation Project, and adopts new §25.181, relating to Energy Efficiency Goal. New §25.181 is adopted with changes to the proposed text as published in the November 2, 2007, issue of the Texas Register (32 TexReg 7833). The repeal of §25.181 and §25.184 are adopted without changes to the proposal and will not be republished. New §25.181 as adopted raises electric utilities' energy efficiency goals from ten percent of growth in demand to fifteen percent of growth in demand by January 2009, and twenty percent of growth in demand by January 2010, and also establishes an energy goal. The new section also establishes an energy goal and updates the cost-effectiveness standard by adjusting the avoided cost of energy; provides the utilities the flexibility to set incentives for energy-efficiency programs, subject to the cost-effectiveness standards in the rule; and establishes a cost-recovery factor to compensate a utility for reasonable expenditures on energy efficiency and a performance bonus for exceeding its goal. The repeal of §25.184 removes the energy efficiency program templates from the rule, so that they may more easily be modified to reflect changes in circumstances relating to energy efficiency. Many of the changes in the energy-efficiency program are a direct response to House Bill 3693, enacted during the 80th session of the Texas Legislature. Project Number 33487 is assigned to this proceeding. This rule is a competition rule subject to judicial review as specified in PURA §39.001(e).

In addition to comments on the proposed rule language, the commission invited comments on the following questions:

1. Should §25.181 specify a third party to advertise or act as an informational clearinghouse for the utilities' energy efficiency programs? If so, who should that third party be and how should this function be funded?
2. Should the calculation of avoided costs include avoided transmission costs?

Written comments were timely filed by December 4, 2007. The commission received comments on the proposed repeals and new section from Steering Committee of Cities Served by ONCOR (Cities), Governmental Aggregation Project (GAP), Office of Public Utility Counsel (OPC), Sierra Club, TXU Energy, Electric Utility Marketing Managers of Texas (EUMMOT), CenterPoint Energy Houston Electric, LLC (CenterPoint), El Paso Electric Company (EPE), Xcel Energy (Xcel), Reliant Energy (Reliant), Texas Ratepayers' Organization to Save Energy and Texas Legal Services Center (Texas ROSE and TLSC), Public Citizen (filing separate comments), a coalition led by Public Citizen, Environmental Defense, and Sustainable Energy and Economic Development Coalition (SEED Coalition), Air Liquide Large Industries' (Air Liquide), Appliance Recycling Centers of America, Inc. (ARCA), Free Lighting Corporation (FLC), Good Company Associates, Inc. (Good Company), Alliance for Retail Markets (ARM), Climate Master, Inc., Center for the Commercialization of Electric Technologies (CCET), EnerNOC, Efficiency Texas (Efficiency Texas), Nucor Steel (Nucor), Texas Industrial Energy Consumers (TIEC), Texas Combined Heat and Power Initiative (TXCHPI), CAF Energy Inc., and UTC Power. The organizations and individuals filing joint comments with Public Citizen

were SEED, Environment Texas, Texas Impact, Texas Interfaith Power and Light, Citizens' League for Environmental Action Now (CLEAN), Clean Air Institute, Citizens Organizing for Resources and Environment (CORE), Environmental Integrity Project, Dr. Mary Landon Darden, Southwest Workers Union, Austin Physicians for Social Responsibility, Galveston Houston Association for Smog Prevention (GHASP), Solar Austin, and People Organized in Defense of Earth and her Resources (PODER). All parties commenting on the repeal of §25.181 and §25.184, and adoption of new §25.181, supported the adoption of the new rule. However, the parties provided comments, as articulated below, suggesting alternate language to be included in the adopted rule.

A public hearing on this rulemaking was held at commission offices on December 10, 2007, at 10:00 a.m. Representatives from Public Citizen, Texas ROSE, Good Company, SEED, TXU Energy, Reliant, ARM, GAP, TXCHPI, Environmental Defense, R and L Energy Technology and OPC provided comments at the hearing. To the extent that these comments differ from the submitted written comments, such comments are summarized herein.

Question 1: Should §25.181 specify a third party to advertise or act as an informational clearinghouse for the utilities' energy efficiency programs? If so, who should that third party be and how should this function be funded?

The following commenters did not support a third party functioning as a clearinghouse: Cities, TXU Energy, EUMMOT, CenterPoint, EPE, Reliant, Public Citizen Environmental Defense, SEED Coalition, FLC, Good Company, ARM, and Efficiency Texas.

The following commenters supported a third party functioning as a clearinghouse: GAP, OPC, and Texas ROSE and TLSC. The Sierra Club filed a position allowing for the possibility that a third party would be specified to function as a clearinghouse.

Cities stated they saw no apparent benefit associated with requiring a third party to serve as a clearinghouse, and that the creation of such a position would likely increase the programs' administrative costs. Reliant agreed. EPE agreed and noted that it is not clear how the clearinghouse would function to provide usable information reflecting statewide areas. Good Company agreed, and also stated that the investments in marketing made by ESCOs (energy service companies)—and in the future, REPs (retail electric providers)—would help to ensure their dedication to the program. Efficiency Texas also agreed, and noted that HB 3693 required a study and analysis of issues and options related to the energy efficiency programs, and directed that REPs in Electric Reliability Council of Texas (ERCOT) and utilities outside ERCOT provide customers with energy efficiency educational materials.

TXU Energy stated there would be inherent challenges to a third party being designated to advertise or act as informational clearinghouse for utilities' energy efficiency programs. TXU Energy stated that one challenge would be the source of funds for payment, and it recommended that payment come from the utility administration fee. TXU Energy also noted that a "call for action" with third party advertisements would pose an additional challenge, as the REP or the Energy Efficiency Service Provider (EESP) could be placed in the awkward position of being required to continue to offer programs advertised by someone else or face repercussions for

discontinuing a program. TXU Energy questioned who the customer would call to get more information regarding programs' availability. TXU Energy stated that the transmission and distribution utilities should not be placed in a role of direct customer contact, and TXU Energy suggested that the commission consider conducting a workshop to identify opportunities and challenges associated with using a third party as a clearinghouse. TXU Energy noted that if, in spite of the challenges, the commission determines to use a third party that it may be more appropriate for the commission to select a third party through an RFP process.

EUMMOT believed that it would be difficult to operate an effective advertising campaign or clearinghouse for the utility programs. EUMMOT noted that the EESPs compete with one another, and it would be difficult for the administrator to fully monitor services being offered. CenterPoint stated it does not believe that a third party would be needed, because the transmission and distribution utilities have had great success in advertising and promoting energy efficiency both on their own and through third parties chosen by the transmission and distribution utilities.

The SEED Coalition stated that it does not believe that the Texas statutory framework leaves much operating space for a third party administrator for the energy efficiency programs. It noted that the responsibility and resources for advertising should not be separated from the reward/risk position of the utility, and that a regulated utility should retain sufficient motivation and flexibility of action to earn a performance bonus and avoid an administrative penalty. It also stated that such a clearinghouse function to make information accessible to the public could be developed with information already required to be reported. In addition, it noted that REPs

should be required to use their direct customer access to periodically provide notice of availability of all energy efficiency programs within a utility service territory. The EEIP (Energy Efficiency Implementation Project) information requirement would be even more important if an Energy Efficiency Cost Recovery Factor would appear on customers' bills.

FLC commented that if a project sponsor invests money itself for advertising, it is much more likely to maintain control over the costs. ARM stated that the use of a third party is not necessary. ARM noted that PURA §39.905 states that retail customers' access to the energy efficiency programs would be through the market, and subsection (a)(1)-(3) does not contemplate that they access those programs directly from the electric utilities.

GAP, on the other hand, recommended that the commission consider being the third party to develop, implement and administer a proactive outreach program focused on utilities' energy efficiency programs. GAP stated that HB 3693 envisioned an increase in the mix of parties in energy efficiency programs, and each party may choose to advertise and market its programs. GAP noted that a clearinghouse should provide access to educational materials to enable the consumer to discriminate among the programs and choose from various program sponsors and service providers. GAP stated that to participate in programs, the consumer must have timely information and tools that save them time and money and that the Texas Electric Choice education program has performed this function to guide consumers in choosing their electricity provider. GAP requested that if the commission was not able to perform a clearinghouse function at this time that the commission seek funds in the next legislative session to carry out this vital role.

OPC recommended that the commission appoint a third party to act as a statewide clearinghouse and resource center for consumers with online computer access to the information. OPC stated that the advertising of the energy efficiency program should be the responsibility of the commission, the utilities and market participants. OPC noted that a statewide resource center could be funded by a portion of the energy efficiency budget from each utility. OPC stated that the advertising funding should be considered cost of doing business and recovered through prices and general rates.

Texas ROSE and TLSC stated that the rule should direct that a neutral third party act as an information clearinghouse for consumer information on energy efficiency programs. They noted that today only EESPs have contact with residential consumers. They further noted that REPs to date are not engaged in energy efficiency discussions with their customers, that a third party contact would comply with the competitive energy service rules and be of service to residential and low-income customers, and a third party provider would be the solution to the information problem. In addition, they stated that the commission should adopt a third party even if only on temporary five-year basis, noting that a temporary program could make consumers more aware of energy savings potential and more engaged in making wise energy choices.

The Sierra Club recommended that the commission should explore the possibility and cost-effectiveness of hiring a third party to advertise and promote energy efficiency programs. The Sierra Club noted several options, such as having the commission serve as the clearinghouse and

advertiser; having the utilities maintain their own clearinghouse and promote their own energy efficiency products; or, selecting a third party through an RFP process.

Commission response

The commission appreciates the thoughtful comments on the question that it posed. A number of the commenters raised valid concerns with the use of a third party to advertise or be an information clearinghouse. This issue is also one that the legislature included in the scope of the report that the commission is directed to submit prior to the beginning of the next legislative session. There may be a value in continuing to explore this issue, particularly in connection with the higher energy-efficiency goals that the legislature adopted in 2007. In view of the concerns that have been raised with respect to this matter, the commission is not taking any action to amend the rule to require the use of a third party.

Question 2: Should the calculation of avoided costs include avoided transmission costs?

OPC, Cities, and Reliant opposed inclusion of avoided transmission costs, whereas the following commenters supported it: GAP, Sierra Club, TXU, EUMMOT, CenterPoint, Texas ROSE and TLSC, Public Citizen, SEED, Good Company, ARM, Efficiency Texas, Nucor and TXCHPI.

OPC recommended that the calculation of avoided costs not include the avoided transmission costs. Cities agreed, noting that it would be difficult to ascertain the impact of individual energy efficiency programs on transmission investments, and that the existing incentives for energy

efficiency are generous. Reliant stated that it had concerns about inflating the avoided costs through the addition of a generic transmission avoided cost amount. Reliant suggested that the avoided capacity cost of generation be based on the capital cost of a new gas turbine, the avoided cost of distribution be based on distribution avoided cost data filed by the utilities, and that the avoided cost of generation capacity be $80/kilowatt (k/W) per year.

GAP, however, commented that the avoided cost for residential and commercial customers is the retail costs avoided by the customer. GAP also suggested that the avoided cost (retail cost) be calculated by each utility service area. GAP suggested estimating commercial rates by escalating the MCPE averages by use of adders that would account for the retailers' additional costs and transmission and distribution rates by utility service areas. The Sierra Club agreed and suggested a more flexible calculation of avoided costs for certain types of programs so that they could be competitive and become more commonplace.

TXU Energy commented that the calculation of avoided costs should include the avoided transmission costs so the calculation represents true market expense and does not place demand-side options at a disadvantage to supply-side options.

EUMMOT commented that it had no objection to the avoided transmission costs being included in the calculation of avoided costs, and noted that investments in transmission infrastructure that could potentially be avoided or deferred by energy efficiency investments tend to very location-specific and can vary over time, so the calculation of such costs would involve extensive analyses and prove extremely burdensome. EUMMOT suggested that if the avoided

transmission costs would be included in the calculation that a simple formula or "proxy value" be adopted to avoid a complicated and controversial study. CenterPoint agreed with EUMMOT, but noted that transmission costs are driven by considerations beyond increases in demand or energy flow. In addition, it stated that the calculation of avoided transmission costs would be difficult without simplifying assumptions, and that the dollar magnitude of avoided transmission costs should be small in comparison to the properly-calculated avoided generation and energy costs. On balance, CenterPoint recommended against the inclusion of transmission in estimating avoided costs.

Texas ROSE and TLSC stated that including transmission and distribution costs in the incentive calculations would be a fair and reasonable strategy for achieving accelerated acceptance of the highest efficiency equipment, noting that choosing an efficient measure should carry a higher level of compensation than the standard program choice. Public Citizen, Environmental Defense, and SEED Coalition agreed and stated that the goal of the energy efficiency legislation is to increase deployment of energy efficiency. They suggested that to ensure that adequate investments are encouraged in energy efficiency, the cost effectiveness should reflect avoided costs of additional transmission and distribution and that a reasonable way to do this would be for residential and commercial customers to use the retail costs avoided by the customer. Good Company agreed, commenting that demand reduction can substantially reduce the need for new transmission and distribution infrastructure.

ARM stated they do not oppose the inclusion of avoided transmission and distribution costs as long as the calculation of those avoided costs is reasonable and does not over-inflate incentive

payments. ARM agreed that value of an energy efficiency program could include avoided transmission and distribution capacity costs for the same reasons it could encompass an avoidance of generation capacity and energy costs. ARM proposed that one possible way to calculate avoided transmission and distribution costs would be to divide the total transmission costs incurred by transmission and distribution utilities in ERCOT for a specific year and divide that amount by the number of kW for the same year. ARM noted that the calculation is similar to the ERCOT postage stamp rate for wholesale transmission service, and the calculation could be updated every two years to be consistent with the two-year adjustment required for generation capacity and energy avoided costs under proposed subsection (d)(2). Nucor suggested a similar approach and encouraged the commission to take avoided transmission costs into account in the presents rule or at a minimum study the subject further for possible future inclusion in the energy efficiency rule.

Efficiency Texas believed that the calculation of avoided costs should include avoided transmission costs. Efficiency Texas stated that it is well known that by increasing our energy efficiency we lessen the need for new power plants. Efficiency Texas noted that this is today reflected in the avoided costs calculation of the present energy efficiency rule, as well as the proposed rule, which established the baseline for energy efficiency incentives. Efficiency Texas stated that excluding transmission costs would underestimate and undervalue energy efficiency. Efficiency Texas proposed including avoided investment in transmission and distribution that can be credited to energy efficiency in the calculation of avoided costs. Efficiency Texas noted that the utilities are given flexibility under the proposed rule to provide incentives at an amount they deem appropriate to achieve cost-effective energy and demand savings, but these incentives

cannot exceed the avoided cost. Efficiency Texas noted that increasing the avoided cost calculation does not automatically lead to raising the costs of the program, but it does allow the utilities to pay customers enough to create increased program participation and provides additional flexibility to meet or exceed the energy efficiency goals.

TXCHPI supported the inclusion of avoided transmission costs in the calculation of avoided costs. TXCHPI stated that all CHP (combined heat or heating and power) and many other energy efficiency measures reduce the need for transmission facilities and should receive credit for the value of the savings. TXCHPI noted that, in addition, line losses should be considered in the avoided cost calculation.

Commission response

The energy efficiency-programs have largely been successful without including transmission or distribution costs in the avoided cost calculation. Even under the current version of the rule that has caps on the incentives that utilities may provide that, for most rate classes, were well below the avoided cost in the rule, utilities have generally been able to meet their goals. Other changes that are being adopted in this rule would increase the energy avoided cost to reflect current market conditions and give the utilities latitude to set the incentives at any level below the avoided cost. Both of these changes could result in higher incentives, if the utilities conclude that they are appropriate. For the present, the commission does not believe that including transmission and distribution costs in the avoided cost calculation is necessary to meet the statutory goals, or that failing to include them will work to the disadvantage of any otherwise cost-effective energy-efficiency

measures. This is an area that may warrant further investigation, particularly if utilities have difficulties meeting the new goals prescribed by the legislature or that may be implemented in the future.

Under the current statute, utility energy efficiency budgets are subject to cost caps that will limit what the utilities may spend for energy efficiency. The commission believes that these caps will be the limiting factor for utilities in promoting energy efficiency programs in the near future. Thus, a higher avoided cost that included transmission and distribution avoided costs would probably not have any impact on the level of utility energy efficiency budgets. In addition, because of the opportunity for utilities to earn bonuses for cost-effectively meeting the statutory goal, utilities will have an incentive to select the most cost-effective programs. Thus, a higher avoided cost that included transmission and distribution avoided costs would probably not have a significant impact on the selection of utility energy efficiency programs. Moreover, ERCOT is structured as an energy-only market so that the cost of energy and any implied cost of capacity are included in the wholesale and retail prices of electricity. The structure of the cost cap in the rule is a wholesale energy price and a calculated generation capacity cost. This structure may over-state the cost of wholesale electricity, and it is probably a rough proxy for wholesale energy costs plus avoided transmission and distribution costs. A study could be undertaken to develop a better estimate of avoided production, transmission, and distribution costs, but the commission concludes that adopting the rule changes that are required to implement the 2007 legislative changes quickly is more important at this point than conducting a study to develop a better estimate of avoided cost. The cost differences among service areas are

relatively small, and the commission concludes that establishing avoided costs by service area would provide little benefit.

§25.181(a): Purpose

Cities proposed modifying §25.181(a)(1)-(3) to specify that electric utilities must administer cost-effective energy efficiency incentive programs that provide net economic benefits to retail consumers, including cost-effective energy efficiency alternatives that allow each customer to reduce energy consumption, peak demand, and net energy cost. Cities and the Sierra Club proposed modifying subsection (a)(1) to specify that energy efficiency programs are designed to obtain energy savings or peak demand reductions beyond savings that would otherwise be achieved in the marketplace.

TXU Energy proposed modifying subsection (a) to include the addition of a new purpose, to specify that each electric utility in the ERCOT region use its best efforts to encourage and facilitate the involvement of the region's retail electric providers in the delivery of efficiency programs and demand response programs.

Commission response

The commission concludes that it is not necessary to include "net economic benefits" or "net energy costs" in subsection (a), as these concepts are addressed in subsection (d). In addition, the commission concludes that adding a provision specifying that energy efficiency programs are "designed" to obtain energy savings or peak demand reductions beyond what is available in the marketplace is not necessary, since the rule being adopted

clearly reflects this purpose. Finally, the commission does not adopt an additional provision regarding "best efforts" to encourage and facilitate REP involvement, since the rule adequately addresses REP involvement in subsection (r).

§25.181(c): Definitions

CenterPoint suggested that the definition of "affiliate" in proposed rule §25.181(c)(1) should simply incorporate the statutory definitions of an "affiliate" into the new rule by reference.

Commission response

The commission does not adopt this suggestion. The definition in the rule specifically addresses energy efficiency service providers (EESPs). Using the statutory definition would require translating a definition relating to utilities to business arrangements involving REPs and would likely reduce the clarity of the definition, as applied to EESPs.

CenterPoint, Xcel, TIEC and ARM suggested clarification of the definition of "commercial customer" in proposed subsection (c)(2). CenterPoint recommended that, since the application of the rule and certain tariff applications will turn on this definition, the proposed definition should include "a governmental entity, including an education institution, a non-profit corporation, a hospital, or an institution of higher education taking service at a metered point of delivery at transmission voltage under an electric utility's tariff."

TIEC proposed that the definition of "commercial customer" would be "a non-residential, non-industrial customer taking service at a metered point of delivery at a distribution voltage under

an electric utility's tariff during the prior calendar year and a non-profit customer or government entity, including an educational institution. For purposes of this section, each metered point of delivery shall be considered a separate customer." In addition, TIEC suggested that a definition of "industrial customer" be added.

Xcel stated that the rule should clarify whether all non-profit customers and government entities are considered commercial customers and, thus, included in the demand and energy goals (and charged the energy efficiency rider), or whether these customers have the option of participating. Xcel noted that, to the extent these customers have the option of participating, the rule should clarify the terms of participation, such as the date the customer must "opt in" and whether or not the customer may change its election.

Commission response

The commission concludes that the definition of commercial customer should include those activities that are not regarded as industrial, such as government and non-profit organizations. The definition should also be practical, to facilitate determinations of eligibility, applications of rates and riders for energy efficiency, and determining load and load growth. The clarification suggested by CenterPoint and other parties is consistent with this approach, as is the provision suggested by TIEC that each metered point of delivery is to be treated as a separate customer. The other changes are not consistent with this approach and, accordingly, are not adopted.

TXCHPI suggested that a new definition be added for "combined heat and power" to be defined as "the simultaneous generation of electrical energy and useful heat from the same fuel source."

Commission response

The commission believes that the concept of "combined heat and power" is sufficiently well understood that a definition is not necessary for the rule.

Cities proposed modifying the definition of "deemed savings" in subsection (c)(5) to specify the use of deemed savings only in instances in which it is demonstrated that there are not cost-effective means to determine energy and peak demand savings determined through standard measurement and verification activities.

Commission response

The commission believes that experience has shown that rigorously developed deemed savings calculations are an efficient and effective way to assess the impact of energy-efficiency measures for mass-market customers. Establishing a preference for the use of measurement and verification protocols would probably make it more expensive to deploy energy-efficiency programs to residential and small commercial customers. With higher energy-efficiency goals and new limitations on the participation of industrial customers in the programs, it is more important than ever to be able to continue to develop and use effective programs for residential and small commercial customers. Accordingly, this suggestion is not adopted.

Sierra Club, Public Citizen, Environmental Defense and SEED suggested that a new definition be added for "demand response." They stated that "demand response" should include reliability programs administered by the independent system operator, and incentives should not be paid for "market signal" time-of-use rate programs offered by the retail electric providers. They stated that they would prefer that utility-based demand response programs employ long-term contracts for an aggregate response consistent with the average life of efficiency measures, and encourage demand reductions over deferral of consumption. The Sierra Club stated that the definition for "demand response" could simply refer back to "load management."

Commission response

The commission concludes that an additional definition for "demand response" is not necessary. Substantive provisions address the role of demand response and load management elsewhere in the rule.

Texas ROSE and TLSC noted that the exclusion of industrial customers from participation in energy efficiency programs is a fundamental change. Texas ROSE and TLSC stated they are unaware of any precedent for exempting a class of customers is from making a contribution to the energy efficiency goal of a utility system. Texas ROSE and TLSC stated that, because industrial customers are excluded from the program, residential and low-income consumers and commercial customers are responsible for achieving the goals and paying for the program costs. Texas ROSE and TLSC stated that the costs include higher rates for underwriting the program and personal investments on the part of residential and commercial customers who choose to be more energy efficient.

Public Citizen, Environmental Defense and SEED stated that the removal of industrial customers from the energy efficiency baseline has the unintended consequence of reducing the state targets and resource calculations. They believed that realizing the state's energy efficiency potential will require the participation of industrial customers and, recognizing that a few industrial customers successfully lobbied to be excluded from participation in the state's efficiency goals and programs, they stated that limiting this exclusion to those customers taking service at transmission voltage for industrial processes is an appropriate resolution. They supported the eligibility of non-profit and governmental entities for the full range of energy efficiency programs.

OPC acknowledged the industrial customers are to be treated differently and noted concern with the treatment of the industrial class in determining how costs should be allocated. OPC recommended the rule be clarified to ensure that the allocation of the energy efficiency incentive program costs consider the industrial class's participation.

TIEC stated that the expenditures made by industrial customers are more focused and tailored to meet their specific needs, and many industrial customers need a different level of energy efficiency measures than the limited programs offered by the utilities. TIEC recommended that the commission properly define "industrial customer" in this rule to develop a rule that fairly implements HB 3693. TIEC stated that the rule as proposed contains a significant flaw, in that it fails to exclude all industrial customers from participating in and funding the energy efficiency programs. TIEC stated the proposed definition of "commercial customer" applies to all customers that take service at distribution voltage, including many industrial customers. TIEC

noted this broad definition ignores the legislative directive that only residential and commercial customers are required to participate in these mandated programs. TIEC stated that many non-industrial customers take service at transmission voltage and many industrial customers take service at distribution voltage. TIEC noted that the proposed rule recognizes this distinction by creating an exception for non-profit and governmental entities in the proposed definition of "commercial customer." TIEC stated that many of these non-industrial customers take service at transmission level. TIEC noted conversely, industrial customers, typically identified by SIC or other codes as manufacturers or producers, can and do take service at distribution voltage.

TIEC submitted that a preferable way to distinguish between industrial and commercial customers is on the basis of business processes. TIEC noted there are many ways in which to accomplish this (through reference to SIC or other code), but one accepted method to distinguish industrial customers is the State's sales tax exemption process. TIEC noted that the Tax Code exempts certain industrial manufacturing and processing activities from sales tax on electricity. TIEC recommended relying on Tax Code exemptions to define industrial customers.

Nucor stated that the rule should emphasize that energy efficiency is encouraged among all customer classes. In Nucor's view, the legislature specifically and purposely targeted the residential and commercial customer classes in PURA §39.905, but it explicitly did not intend to exclude industrial customers from the commission's energy efficiency efforts. Nucor stated that the legislature expressly provided that all customer classes must have a choice of and access to energy efficiency alternatives, even though it set specific goals only for residential and

commercial customers. Nucor believed the commission could revise its proposed rule to make it more inclusive, without changing its primary focus.

Air Liquide proposed modifying the definition of "eligible customers" in subsection (c)(7) so that industrial customers could be included as "eligible customers" to the extent that they meet the criteria for participation in load management standard offer programs developed for industrial customers and implemented prior to May 1, 2007, or the criteria for programs provided for under subsection (t) of this section. Air Liquide was concerned that CenterPoint, and possibly other utilities, have taken a position that unnecessarily penalizes industrial customers by eliminating energy efficiency programs for industrial customers. These are programs that the utilities budgeted for, that industrial customers paid into, and that customers have relied upon.

Commission response

As the commission noted above, important objectives in defining customer classes that will be eligible to participate in the energy efficiency programs are whether the definition is practical and it facilitates determinations of eligibility, applications of rates and riders for energy efficiency, and determining load and load growth. The commission believes that the criteria suggested by TIEC for identifying industrial customers do not meet these objectives. Relying primarily on voltage level, however, is practical and provides a simple means of identifying industrial customers for the various purposes that they need to be identified. In particular, the transmission customers are a separate class of customers with respect to rates for the ERCOT utilities. The commission does not agree with Nucor's view that the rule should continue to encourage the participation of industrial customers in the

programs set out in this rule. The clear import of the amendments in HB 3693 was to curtail industrial programs, except to the extent that they are grandfathered under PURA §39.905(a)(6).

The commission agrees with Air Liquide's recommendation for a limited grandfathering of industrial customers. As Air Liquide pointed out, the industrial customers are likely to continue paying rates that include the cost of industrial programs during 2008, so their ability to participate in the programs should not be abruptly eliminated. This provision is included in subsection (t).

Cities and Reliant proposed modifying the definition of "energy efficiency" in subsection (c)(9) to remove "with the same or higher level of end use service." Cities also proposed deletion of "and that do not materially degrade existing levels of comfort, convenience, and productivity." Reliant stated that the definition for energy efficiency simply creates confusion and invites debate and the phrase should be deleted. Reliant raised concerns with existing rule language that would have energy efficiency "maintain or improve existing levels of comfort, convenience and productivity," specifically stating that whether something provides for a higher or lower level of service may be in the eye of the beholder.

Texas ROSE and TLSC stated that HB 3693 defines energy efficiency as using less energy to provide the same or improved level of service to the energy consumer in an economically efficient way. The term energy efficiency as used here includes using less energy at any time, including at times of peak demand through demand response and peak shaving efforts. Texas

ROSE and TLSC stated HB 3693 amends the language in PURA describing programs to be offered from energy "saving" programs to energy "efficiency" programs. Texas ROSE and TLSC noted that there is a difference, and the proposed rule, as published, would have amended several provisions to allow utilities to implement programs that save only demand. Texas ROSE and TLSC commented that energy efficiency applies to programs that promote changes that reduce electricity use without any degradation of comfort level, but the new definition adds language that permits a degradation of comfort level, convenience and productivity. HB 3693 allows such degradation of service to be eligible for incentives, but these impacts should be directly associated with load control and load management and that the rule should continue to distinguish between programs that do and do not impact service and comfort levels.

Commission response

"Energy efficiency" has been understood to involve using less energy to provide the same benefits that electric service brings to customers, such as heat, light, cooling, and the power for appliances that customers regard as necessities or important conveniences. The commission definition in the proposed rule would have modified the prior definition by referring to reductions in energy or demand that do not "materially degrade" a customer's comfort level, convenience or productivity. This change would provide latitude to include programs such as air conditioner cycling programs as eligible energy-efficiency programs. These programs may result in changes in room temperature, but the expectation is that most customers would not regard them as resulting in a material degradation in comfort levels, and the programs have the potential to provide significant demand savings. The commission believes that this concept should remain a part of the rule, for this reason.

In addition, the commission does not believe that different standards for customer impact should be adopted for programs that are primarily demand reduction programs. The simple message for all energy-efficiency programs should be that customers have the potential to benefit from the programs, and existing light, heat, cooling, information, and other benefits will not be materially affected.

Cities proposed modifying the definition of "energy efficiency measures" in subsection (c)(9) to remove the last portion "so long as the customer need satisfied by the appliance is still met," and seeks to include language expanding the measures that can be included to say that such measures "may include but are not limited to thermal energy storage and removal of an inefficient appliance." ARCA supported the Cities' proposed definition of "energy efficiency measures" as it provides the clarification necessary to fully allow wider adoption of cost-effective energy efficiency programs such as ARCA's appliance recycling programs.

CAF provided professional engineering data supporting the new proposed definition of energy "efficiency measures." CAF stated that restrictions placed on certain technologies in the prior version of §25.181 should be repealed.

Commission response

The commission is not adopting the deletion proposed by Cities. Energy efficiency does not include eliminating an electricity-driven function, but consists of providing the same function with less demand or energy. The commission concludes that an appliance

recycling program would not be disqualified under the definition in the proposed rule and that there is, therefore, no need to adopt this suggested change. The commission is adopting the proposed definition, as suggested by CAF.

Texas ROSE and TLSC stated that "practices" listed in proposed subsection (c)(10) are not eligible for incentives under the current rules and should not be eligible for incentives in the future, since the incentives paid for energy efficiency should be those that will persist over time. They commented that when materials and equipment are physically installed at a customer site for the purpose of reducing energy use and demand, the load reduction realized at the time of the installation will persist for the useful life of the measure. Practices, on the other hand, are dependent on behavior, not technology.

Texas ROSE and TLSC further stated that it is inappropriate to mention one technology and one program without mentioning all of them as it could be argued that a measure does not qualify for the program unless it is specifically stated in the definitions. They asserted that the decision as to whether and how a measure is incorporated into the energy efficiency programs should be made after a thorough evaluation and review by the commission. They added that since HB 3693 directs the commission to consider and evaluate options, listing options in the definitions is not compliant with PURA §39.905(d), which requires evaluation and approval of program options by the commission.

The Sierra Club largely agreed with Texas ROSE, and commented that "thermal energy storage and removal of an inefficient appliance," as specific measures, should not be included in the

definition. The Sierra Club believed that the definition of energy efficiency measures as "equipment, material and practices at a customer's site that result in a reduction in electric energy consumption or demand" may need further refinement. The Sierra Club supported including both physical infrastructure and behavioral changes in the definition of energy efficiency, but it wanted to make sure that money is spent on practices that will actually persist. The Sierra Club suggested that the definition include a requirement that the energy reduction persist over at least a five-year period.

Commission response

The commission does not agree with the proposition that practices should be eliminated from the definition. Technologies like thermal storage may depend on both installation of equipment and changes in customers' practices for buying and using energy. The coupling of the technology and changes in practices has the potential, however, to produce demand savings in a cost-effective manner. The commission does not intend to foreclose such options in adopting the rule; rather, the rule will put the onus on EESPs to develop cost-effective energy-efficiency projects that provide verifiable savings and put the onus on the utilities to select the programs that will best meet the goals of the statute and rule.

The commission also concludes that that it is appropriate to mention specific technologies in the definition to resolve the uncertainty that has existed with respect to such technologies. Mentioning specific technologies does not imply a preference for these technologies, and their proponents will still have to satisfy the utility that a technology proposed to the utility delivers demand and energy savings in a cost-effective manner.

The commission does not adopt the Sierra Club's proposal to add to the definition that an energy reduction persists over at least a five-year period. The commission believes that measures with a shorter life, such as air conditioner tune-up programs, may be able to provide cost-effective savings.

Cities proposed modifying the definition of "energy efficiency program" in subsection (c)(11) to ensure the aggregate of the energy efficiency activities are specifically "cost-effective."

Commission response

The commission does not believe that this change is necessary. The limitation on incentive payments in subsection (g) is 100% of avoided cost, and the cost caps and bonus calculation provide incentives to meet the savings goals in a cost-effective manner.

Good Company proposed modifying the definition of "energy efficiency service provider" in subsection (c)(13) to limit a commercial customer acting as its own EESP to a customer with a peak load exceeding 50 kW.

ARM contended that the definition of "energy efficiency service provider" in proposed subsection (c)(13) should include only REPs and competitive EESPs, and not customers of any kind. ARM expressed concern that if an electric utility can distribute program funds directly to a commercial customer, a REP's ability to fulfill this expanded role would be undermined. ARM suggested that allowing REPs to access program funds on behalf of their commercial customers

would not deprive those customers of the benefits of the utility's energy efficiency programs. TXU agreed with ARM.

Commission response

The commission agrees with Good Company's proposed modification and disagrees with ARM's proposal to include only REPs and EESPs. The commission believes that Good Company's proposal would allow for the inclusion of commercial customers that are of a size that they are likely to have the expertise and other resources to participate directly in the program as EESPs. Customers have participated in the program as EESPs in the past and the commission believes that this has been a valuable feature for these customers. It does not believe that including commercial customers in this role would inhibit REP participation in the program.

Cities proposed modifying the definition of "energy savings" in subsection (c)(14) to specify the quantifiable reduction in a customer's consumption of energy "that is attributable to energy efficiency measures."

TXCHPI supported modifying the definition of "energy savings" to specify a quantifiable reduction in a customer's consumption of energy, including the net energy savings from combined heat and power (CHP). TXCHPI stated that, without this change, the definition may be considered too limiting.

Commission response

The commission is adopting Cities' clarification that the definition of energy savings should refer to savings attributable to energy efficiency measures. However, the commission does not adopt TXCHPI's proposal to modify the definition to include CHP. There is no need to refer to a specific technology in this definition.

Cities proposed modifying the definition of "growth in demand" in subsection (c)(15) to specify the annual increase in "electric" demand in the Texas portion of an electric utility's service area at time of peak demand, as measured in accordance with this section.

Commission response

The commission does not believe that it is necessary to include "electric" in the definition of "growth in demand." In context the definition clearly refers to electric demand.

Cities proposed modifying the definition of "inspection" in subsection (c)(18) to clarify that the energy saving or demand reduction is "attributable to that measure."

Commission response

The addition of "attributable to that measure" is unnecessary, because the definition refers to an energy efficiency measure that "is producing" energy savings.

Texas ROSE and TLSC commented, with regard to subsection (c)(19), that load control is defined as an activity that can be conducted by the utility or an independent system operator.

Noting their concern about the reliability of such intermingling of these activities as discussed elsewhere in these comments, they recommended the definition be amended by deleting "an independent system operator." Public Citizen, Environmental Defense and SEED Coalition commented that reference to the independent system operator is potentially misleading, that "electric utility" should replace "independent system operator," and that it should specifically state that "load control activities of the independent system operator are not subject to this rule." The Sierra Club also recommended that this subsection not refer to "an independent operator."

Commission response

The commission is also concerned about the intermingling of activities and payments. However, the commission does not agree with Sierra Club, Texas ROSE and TLSC's proposed deletion of "independent system operator," because there may be different control options that will result in cost-effective, verifiable demand savings but that do not represent duplicative payments for the same service. For the same reason, the commission does not adopt Public Citizen, Environmental Defense and SEED's proposal to replace "independent system operator" with "electric utility."

Cities proposed modifying the definition of "load management" in subsection (c)(20). Cities stated that load control activities are those that result in a reduction in peak demand on an electric utility system or a shifting of "electric demand" from a peak to an off-peak period or from high-price periods to lower price periods. Nucor stated that the legislature chose specifically to endorse the continuation of existing load management standard offer programs

developed for industrial customers, and that the proposed rule should clarify that those successful programs are not frozen in place, but should be expanded by individual utilities.

Commission response

The commission does not agree with Cities' proposal to change the definition of load management. The commission concludes that the definition in the proposed rule accurately describes load management. The commission does not agree with Nucor's comments. This issue is discussed in more detail below.

Cities proposed modifying the definition of "market transformation program" in subsection (c)(21) to state that it is defined as a "Strategic program that induces lasting structural or behavioral changes in the market," instead of "strategic efforts to induce" those changes.

Commission response

The commission agrees with Cities' proposed modification, insofar as it suggests that the programs be referred to as strategic programs, but it concludes that the definition should retain the concept that the programs are efforts to induce changes and avoid implying that they must be successful. Obviously, the goal of the statute and rule is to implement successful programs, but the rule should recognize that pursuing innovative programs in a competitive environment involves some risk that programs will not immediately succeed and some may not succeed at all.

Good Company proposed modifying the definition of "peak demand reduction" in proposed subsection (c)(25) to refer to a reduction in demand on the utility system "throughout" the utility system's peak period, instead of "during" the system's peak period. In addition, Good Company proposed adding a new definition for "peak demand response," which would refer to the capability to reduce demand on the utility system throughout the utility system's peak period. Good Company noted that the previous definition of "peak demand reduction" calculated the reduction as the maximum average demand reduction over a period of one hour during the peak period. Good Company stated this definition was addressed in the Summit Blue report (Project Number 30170), which stated that these one-hour reductions may not meet commission requirements that measures contribute to a "reduction in growth of demand ... measured at the utility's annual system peak." Good Company stated that Summit Blue recommended that the new definition require load reductions to occur throughout the entire Peak Period. Good Company noted that the new definition, as written, is quite vague, and could be interpreted to mean either one hour during the peak period, or throughout the entire period. Good Company noted that it is important to distinguish demand reduction resulting from energy efficiency measures, which should be sustained over the entire period, from that associated with a demand response program, which should be "available" over the entire period.

Commission response

The commission agrees with Good Company's modification that would change the definition to mean a reduction in demand on the utility system *throughout* the utility system's peak period or, in connection with a demand response program, the availability for demand reductions over the entire peak period.

Sierra Club proposed modifying the definition of "peak period" in subsection (c)(26) since, in Texas, that period is from one p.m. to seven p.m. Nucor agreed, and also recommended removing the month of May and suggested that matching the peak period for this rule with the peak period utilized by the commission, ERCOT and utilities for utility planning and cost allocation purposes would be in the public interest.

Commission response

The commission agrees with modifying the definition from one p.m. to seven p.m., and removing the month of May.

Good Company proposed modifying the definition of "standard offer contract" in subsection (c)(28) to remove the reference to energy and peak demand savings achieved "through the installation of energy efficiency measures at electric customer sites."

Commission response

The commission agrees with the deletion of "through the installation of energy efficiency measures at electric customer sites." The definition of "energy efficiency measures," in subsection (c)(9), allows for removal or installation of an inefficient appliance. This change would make the two definitions consistent.

TXU Energy proposed a new definition for "capacity factor" to be defined as "the ratio of the annual energy savings goal, in kWh, to the peak demand goal for the year, measured in kW, multiplied by the number of hours in the year."

Commission response

The commission agrees with the inclusion of a definition of "capacity factor."

Sierra Club, Texas ROSE and TLSC proposed a new definition for "targeted energy efficiency program" to be "the targeted energy efficiency program under PURA §39.903 and §30.905 operated by local agencies and coordinated with other funds that are administered by the Texas Department of Housing and Community Affairs." Texas ROSE and TLSC stated that using this definition distinguishes the weatherization program that piggybacks on the federal program from the Hard-to-Reach standard offer program and other programs that may serve low-income consumers but follow different standards and guidelines.

Commission response

The commission does not agree with the inclusion of "targeted energy efficiency program" or "low-income targeted energy efficiency program," as there is not a need to refer to specific programs or specify that they be administered by another state agency. Funding issues have arisen with respect to this program in the past, and the rule should be flexible enough to continue the programs by different means, if funding is not available for the Department of Housing and Community Affairs to operate them.

25.181(d): Cost Effectiveness Standard

Cities proposed modifying proposed §25.181(d), the cost-effectiveness standard, as follows: "An energy efficiency program is deemed to be cost-effective if the total cost of the program is less than the net economic benefits of the program to retail consumers." In addition, Public Citizen, Environmental Defense, SEED, Nucor, Texas ROSE and TLSC argued that the cost effectiveness standard should reflect avoided costs of the additional transmission and distribution in the retail electricity cost avoided. Therefore, they stated that consumers would make decisions on the value of efficiency compared to their retail costs, which vary by service area, which will, in turn, attract EESPs into areas where they are most needed. Texas ROSE and TLSC argued that the avoided cost should include the cost of avoided transmission costs so that higher incentives can be allowed for renewable demand side management (DSM) measures and the highest efficiency end-use technologies that are not customarily installed under the standard offer programs. They commented that as standards in the market increase, higher levels of efficiency should be obtained through utility programs and accelerating the acceptance of the higher end, and higher cost, technologies may require a higher level of incentive to stimulate the market. The Sierra Club made a similar argument and also stated that one possibility of a cost more reflective of the actual cost of energy might be to use regional retail prices of energy, which might be more reflective of the true cost of competition and providing energy and transmission and distribution. Reliant's public hearing statement opposed Public Citizen proposal to rely on retail prices. Reliant believed that capacity and energy cost is already double dipping and inflating the avoided cost would be amplified under this proposal.

TXCHPI recommended the addition of a standard for the calculation of the value of the natural gas saved under the cost-effectiveness standard. TXCHPI noted all CHP applications will be accompanied by an engineering analysis of the project, including specifications for construction and a payback or cost benefit analysis of the project.

Commission response

The commission does not agree with Cities' proposed modifications regarding "net economic benefits" considered from the perspective of the customers. One of the objectives of the rule is to simplify key program elements, to facilitate participation of energy service providers and customers in energy efficiency program. Different customer classes, different customers, and different energy efficiency measures are likely to have different "net economic benefits," and those costs would be difficult for utilities and EESPs to assess. The commission concludes that the rule will create incentives for utilities to operate these programs in a cost-effective manner. Presumably this will meet the Cities' objectives. In addition, the commission does not agree with the inclusion of avoided costs of transmission and distribution or establishing separate avoided costs based on retail costs in each service area. This issue is discussed in greater detail above.

The commission declines to adopt TXCHPI's recommendation to add a standard for the calculation of the value of natural gas. If each project will require a cost-benefit analysis, as TXCHPI indicated in its comments, the utility receiving a proposal for combined heat and power should have a basis for evaluating whether the benefits exceed the costs, from the utility's perspective. Based on their experience in evaluating such proposals, it may be

possible to adopt more specific standards for evaluating such proposals in a future revision of the rule.

EUMMOT proposed that actual or allocated research and development and administrative costs be excluded from the cost-effectiveness standard. CCET agreed.

Commission response

The commission disagrees with EUMMOT and CCET's proposal to exclude administrative and research and development costs from the cost-effectiveness standard. The commission believes that, in order to accurately assess the cost-effectiveness of individual programs, administrative costs, including costs for research and development, should be considered.

Nucor commented that the initial avoided cost of capacity should be $90/kW per year. Additionally, Nucor requested that the commission apply a simple inflator to the avoided cost of capacity figure used in the 2000 rule or, at worst, the figure in the 2005 rule, and work with interested parties to set a reasonable and transparent standard for determining the cost in 2009. Nucor stated that the cost effectiveness of energy efficiency programs will be appropriately evaluated against an avoided cost standard in the proposed rule. Nucor noted that while the commission's proposed rule develops a clear-cut standard for avoided energy cost, the avoided capacity cost standard is somewhat vague and the value assigned for purposes of the rule appears too low. Nucor stated the increase in the avoided cost of capacity from $78.50/kW in the 2005 rule to $80.00/kW in the proposed rule is too low. Nucor proposed that the commission raise the avoided cost of capacity in the proposed rule by at least the amount of inflation occurring in the

Consumer Price Index compiled by the Bureau of Labor Statistics since 2000. Nucor noted using that measure, the $78.50/kW used in 2000 would be $95.25/kW in today's dollars. Nucor noted that, at a minimum, the commission should allow for inflation based on the 2005 rule, which would set the avoided cost of capacity at $83.98/kW. Nucor stated this would be a good stopgap measure until the commission has a chance to evaluate and incorporate more precise methods for recognizing the enormous increases in the cost of gas turbine units, which have increased in cost in recent years far beyond the general rate of inflation. Nucor cited recent testimony before the Michigan Public Service Commission that suggested that gas simple cycle installed costs have gone from $517kW in 2005 to $713 per kW in 2007, and a study prepared for the Edison Foundation, by the Brattle Group that reported that the cost of gas turbines increased by seventeen percent during 2006 alone.

Nucor stated that underestimating the avoided cost of capacity will undervalue and minimize the cost effectiveness of energy efficiency programs. Nucor stated, in contrast, §25.181(d)(2)(B) adopts a straightforward measure for the avoided cost of energy, using the "simple average of the market clearing price in ERCOT for balancing energy for the previous calendar year." However, Nucor noted that the methodology, which reflects the previous year's energy prices, fails to reflect current and future energy costs. Nucor stated that since energy efficiency typically is captured over a long period of time, such as where residential consumers receive incentives to improve home insulation, a backward-looking avoided cost of energy standard is perhaps not the best measure to employ over the long term. Nucor recommended that the commission consider whether some inflation escalation factor should be applied to the avoided cost of energy to properly reflect these concerns.

Public Citizen, Environmental Defense and SEED commented that subsection (d)(2) should be amended to require that energy costs be based on retail electricity costs, such as fuel cost, generation, transmission and distribution.

CenterPoint recommended that the "cost-effectiveness standard" provide that adjustments, if any, to the avoided cost of capacity and the avoided cost of energy be calculated by May 31 of each year using the most recent data for avoided capacity costs and the most current twelve months of data for avoided energy costs, because budgeting for energy efficiency programs generally occurs around the middle of the calendar year and changes in programs and program incentives are usually announced in the Fall and go into effect on January 1 of the following year. Any revised cost-effectiveness standard resulting from those calculations would not apply until January 1 of the following calendar year. CenterPoint stated while the recalculation of avoided capacity cost every two years and the recalculation of avoided energy costs every year should not be time consuming processes, lead time will be necessary before the revised cost-effectiveness standard is applied to an energy efficiency program and the program costs, and particularly before the incentives could be adjusted, without prejudicing customers, contractors, or the EESPs who have already committed to the program. CenterPoint noted that the proposed rule calculates avoided capacity at the capital cost of a "peaking unit" and avoided energy on the average of the market clearing price for balancing energy across an entire year, and potentially that creates a mismatch in avoided costs; thus, CenterPoint believed the issue merits additional study and recommended not to change the rule at this time.

Commission response

The commission notes, in connection with Nucor's suggestion to include parties in determining avoided capacity cost calculations, that the commission intends to work with interested parties in developing avoided capacity costs. The commission held a workshop on the rule in late 2007, and parties had an opportunity to present their views on any aspect of the rule. Good Company provided a paper in support of including transmission and distribution costs in the avoided cost calculation. The commission will continue to work with interested parties with respect to the implementation of the rule. In the case of avoided capacity costs, the staff relied on a National Regulatory Research Institute study, which was also used in P.U.C. Docket Number 21074. The avoided capacity costs in the proposed rule were based on a study presented in *In the Matter of the Application of Consumers Energy Company for Approval of a Balanced Energy Initiative and for Other Relief*, Exh. WEG-4 at 14 (September 21, 2007). The commission recognizes that there have been recent reports of increases in the costs that are important in the construction of new electric generating facilities, but it believes that the adjustment process in the rule is adequate to capture the impact of these changes, and that it is not critical to adjust the avoided cost in the manner that Nucor suggests now. As is pointed out above, the budget caps are likely to be the limiting factor in utilities' decisions relating to program selection and incentive levels in the near future, and increasing the avoided costs would probably have little impact on their decisions. With respect to a "simple inflator" for the avoided cost of capacity, such costs are not likely to correlate closely with consumer cost indices. The commission is not adopting Nucor's suggestions relating to avoided costs.

The commission believes that CenterPoint's comments imply a need for greater flexibility in the rule and a target date for making changes in avoided capacity costs. The commission is adopting a rule providing for an annual review of capacity costs, with the objective of adopting any change by May 1, 2009, for use in 2010.

EUMMOT proposed an allowance for a transition from balancing energy prices to zonal average of locational marginal prices (LMPZs) in the future as a basis for changing avoided energy costs. EUMMOT noted that, upon implementation of the nodal market in ERCOT, the balancing energy market will be discontinued, and the analogous concept would be LMPZs. Reliant also proposed a similar use of zonal prices. EUMMOT suggested further that the avoided energy costs should be based upon the average energy price solely during peak hours; or, in the alternative, a minimum or "floor" price established to offset the detrimental effect of averaging extremely low or even negative energy prices as occasionally witnessed during off-peak periods. EUMMOT suggested including these extremely low—or even negative—prices in the average only serves to reduce the value of the avoided energy costs.

Commission response

The commission agrees with EUMMOT and Reliant's recommendation to use the zonal average of locational marginal prices in the future as a basis for changing avoided energy costs. As EUMMOT and Reliant have commented, although the $0.055/kWh cost is being adjusted annually based on MCPE and is appropriate in the current market, when the nodal market is implemented, a different calculation, based on a simple average of the load zone locational marginal prices will be more appropriate. The commission also agrees with

EUMMOT that using peak hour prices will more accurately reflect the avoided costs of serving customers during peak hours, which is consistent with the demand reduction goal of the program.

§25.181(e): Annual Energy Efficiency Goals

Cities proposed modifying the proposed subsection (e), annual energy efficiency goals, to require all programs to be "cost-effective" and "designed" to achieve at least a fifteen percent reduction in the electric utility's annual growth in demand of residential and commercial customers by December 31, 2008; and twenty percent of the electric utility's annual growth in demand of residential and commercial customers by December 31, 2009.

Sierra Club proposed that subsection (e) should require utilities to continue to make available, at 2007 funding and participation levels, any load management standard offer programs developed for industrial customers and implemented prior to May 1, 2007. It would also require utilities to report on industrial programs, and they would be encouraged to expand these programs if industrial consumers agree to participate and funding sources are available that do not take away from the other programs. The Sierra Club stated there was nothing in the law that would prevent a utility from offering new industrial efficiency programs, although how it could pay for such programs is unclear since, by statute, the payments must correspond to the amount that is contributed by customer class, and, with most industrial customers now exempt, it would be virtually impossible to add more programs using the required programs and funding source.

Commission response

The commission does not agree that Cities' proposed modification of proposed subsection (e) are needed. These changes merely amplify objectives and requirements that are expressed elsewhere in the rule. The commission also does not agree with the inclusion of the Sierra Club's proposed modifications to subsection (e) relating to load management standard offer programs. The commission recognizes that the amended law does not preclude the utilities from operating industrial programs, but, as is discussed above, the clear import of the amendments in HB 3693 was to curtail industrial programs, except to the extent that they are grandfathered under PURA §39.905(a)(6).

Cities also proposed modifying subsection (e)(1) to eliminate the provision that would permit any reduction in growth in residential and commercial peak demand that is achieved in 2007 in excess of ten percent of a utility's demand savings goal to apply to the required savings in 2008. Cities proposed modifying subsection (e)(1)(A) to require that each year's historical demand for residential and commercial customers be normalized to adjust for extraordinary weather fluctuations, using weather data for the most recent ten years. Texas ROSE and TLSC and Sierra Club also supported removing all language from subsection (e)(1) regarding "carry over" of reduction of growth in demand. The Sierra Club stated that they understand that this provision is offered as a transitional measure as the rule is implemented, but they do not believe it matches legislative intent, which was to maximize the amount of energy efficiency gained.

Good Company commented that §25.181(e)(1) allows a utility to carry over excess reduction in demand over ten percent in 2007 to 2008. Good Company stated if the efficiency rule changes

that will apply to 2008 expand the definition of "peak demand reduction" to reductions that occur "throughout the utility system's peak period," this section will allow utilities to carry over demand savings achieved under the previous definition, which allowed reductions to occur over a period of one hour, exaggerating the actual demand reduction achieved, and will result in underperformance by utilities. Good Company stated the new definition should be applied in determining the quantity of the carryover reduction in demand.

The Sierra Club also commented on the provision that would increase the savings achieved through the hard-to-reach (HTR) customers to reflect the reality that the calculation of demand is now based only on commercial and residential demand, and in most cases will not include industrial demand. At the public hearing, Texas ROSE and TLSC supported the Sierra Club's position for calculation the goals and what should be done for requirements for achieving savings for HTR. They stated that subsection (e)(1)(E) should be changed so that savings achieved through hard-to-reach programs would be no less than ten percent of the utility's demand reduction goal. Sierra Club agreed, but added that the commission should look at actual expenditures levels currently and attempt to find an appropriate percentage that would encourage more use of these funds, without taking away the flexibility of the utilities to adopt other needed programs.

EUMMOT stated that the proposed ratchet in subsection (e)(1)(D) in the demand goal should be removed. EUMMOT stated that, particularly over the next three years, there is no need for this ratchet as the goal as a percentage of load growth will increase significantly each year. EUMMOT stated this should translate into a higher goal in terms of megawatts each year. In

addition, EUMMOT stated there may be situations in which the proposed ratchet could result in the establishment of an unattainable goal. EUMMOT noted, for example, that if a utility sold a portion of its service area, then that utility could be saddled with the same megawatt goal, but a smaller customer base and geographical area through which it could be achieved. EUMMOT stated that PURA §39.905(a)(3) mandates that the utility achieve a certain percent reduction of its annual growth in demand, with "annual growth in demand" a clearly defined calculation in the statute. EUMMOT stated this definition does not include, nor purport to suggest, that a minimum, or "floor", of attainment be established based on a previous year's performance. EUMMOT stated, rather, the definition for growth in demand was crafted to recognize both the impacts of load growth within the utility's service territory, the impacts of the general marketplace for energy efficiency programs, and the broader effects of an annually fluctuating economy. EUMMOT noted it should be recognized that there is no guarantee of an escalating or even stable demand for energy efficiency initiatives. EUMMOT contended that market dynamics, such as program saturation, more stringent building codes, and tighter energy appliance standards, will potentially serve to reduce opportunities for energy efficiency programs and make the attainment of an annually escalating goal even more difficult. EUMMOT stated from a paradoxical perspective, this is ultimately what the rulemaking is trying to achieve. CenterPoint and Xcel agreed with EUMMOT. It recommended, rather than including a "ratchet" in the proposed rule under subsection (e)(l)(D), that it would be more appropriate for the commission to consider all aspects of such a provision when it conducts the study called for by PURA §39.905(b-2). CenterPoint stated that if the demand in a utility's service territory contracts, either because of economic conditions or because of overall increases in energy

conservation or both, the "ratchet" would not be needed to encourage energy efficiency efforts and could penalize a utility for not being able to meet a non-statutory goal.

Commission response

The commission does not agree with Good Company, Cities, Sierra Club, Texas ROSE and TLSC's recommendation to remove the language from subsection (e)(1) regarding "carry over" of the reduction of growth in demand. The commission believes that, particularly in light of the fact that the industrial customer class participation in energy efficiency programs will be limited, the utilities may need the ability to carry-over savings. The commission notes that these carry-over savings constitute savings that are over and above the utilities' previous year goals. The commission agrees with Good Company's suggestion, in light of the modified definition of "peak demand period," that the new definition of peak demand period should apply in determining the quantity of the carryover reduction in demand.

With respect to the Cities' proposal to utilize "normalized growth in demand," as suggested for subsection (e)(1)(A) and (e)(1)(B) require that the utilities' growth in demand be calculated using the average, weather normalized demand growth over the five preceding years in each utility's territory.

The commission does not agree with EUMMOT, CenterPoint, and Xcel's arguments that subsection (e)(1)(D) should be deleted. The parties suggested that the "ratchet" provision was unnecessary, not a statutory goal, and contrary to the controlling legislation. The

legislature has given the commission some discretion in how to implement the energy efficiency program under PURA §39.905, and that one of the important goals of the 2007 amendments to this section was to increase the level of energy efficiency improvements that utilities achieve. Demand growth can fluctuate with changes in the economy, but the projected long-term path for the Texas economy is significant growth. The commission believes that, in view of these circumstances, it is appropriate to maintain energy efficiency efforts, even if a short-term downturn occurs in a utility service area. Consistent policy in this area is also important to provide opportunities that will support the growth of independent EESPs in Texas. If a long-term economic downturn occurs in any of the utility service areas, or if a sale of service territory occurs, the commission will have the ability to address this matter in a rule revision or in reviewing utilities' programs.

Good Company and ARM commented that subsection (e)(2) should be eliminated. Good Company specifically noted that §25.181(e)(2) calculates the energy savings goal as the demand goal multiplied by a thirty percent capacity factor (CF). Good Company appreciated the intent to encourage additional energy savings, but was concerned that this may result in discouraging the pursuit of both energy efficiency and demand response. Good Company stated a thirty percent CF would require saving 2,628 kWh per kW, compared to the average 2005 and 2006 value, 2,433 kWh per kW. Good Company stated that the energy goal may eliminate all demand response programs and most programs that primarily save energy during peak hours, resulting in TDUs only implementing energy efficiency programs that produce "flat" consumption, saving proportionately more energy during hours when prices are lower and when renewable energy such as wind will provide a substantial portion of generation. Good Company noted that, given

the incentives created by the bonus structure, which encourages utilities to maximize net benefits, there is already a strong bias toward energy efficiency. At a thirty percent CF, an efficiency program would have avoided costs of $224 per kW as opposed to only $80 per kW for a demand response program. Good Company stated the proposed bonus structure provides sufficient incentives for the TDUs to make energy efficiency a high priority such that they would turn to demand response and load management after only they have exhausted cost effective energy efficiency opportunities. ARM raised similar concerns and noted that unlike the annual demand reduction goals specified in PURA §39.905(a)(3), the statute does not specify this energy savings goal. ARM was concerned that the imposition of this energy savings goal might unduly complicate the administration of the energy efficiency programs by electric utilities. ARM stated their strong view was that an appropriate energy savings goal is one that does not eliminate beneficial demand response programs. ARM noted given that proposed subsection (m) requires each electric utility to include energy savings information in its annual plan and report, the commission can assess the appropriateness of each electric utility's energy savings goal and, if necessary, direct the utility to modify it.

Commission response

The commission agrees with ARM's comments that the statute does not specify an energy savings goal. However, the commission concludes that including an energy savings goal is important and is within its discretion. It is obvious that many of the parties participating in this proceeding regard air emissions and global climate change as important concern to be addressed by the energy efficiency program. In addition, the Health and Safety Code directs that the air emission reductions resulting from energy efficiency programs be

estimated. Energy savings are also an important part of the benefit for customers. All customers pay for energy, and residential customers pay directly only for energy. The commission understands the concerns that an energy goal may bias utilities against demand response programs in favor of programs that include energy savings. The utilities already report energy savings to the commission, but they have not been subject to an energy savings goal. Because the adoption of an aggressive energy goal might result in program selections by the utilities that would de-emphasize demand-reduction programs, the commission believes that a less aggressive goal for energy savings should be adopted. Accordingly, the commission is adopting an energy goal for utilities that is based on a twenty percent capacity factor.

The Sierra Club suggested that in §25.181(e)(3) should be modified to assure that the expenditures for efficiency correspond roughly to the amount paid by the customers in the wires charges, and that the electric utilities disclose the value of the programs that come from these charges.

Good Company proposed modifying subsection (e)(3)(A) to permit each electric utility to establish programs or standard incentive payments to achieve the section's objectives. Good Company felt it was necessary to allow for market transformation programs that might not include incentive payments, but rather focus on market education efforts or removal of market barriers. In subsection (e)(3)(B)(ii), Good Company proposed adding a provision for measures with limited market penetration to reduce avoided by a Net-to-Gross ratio to account for free-ridership. Good Company stated that the section declares measures ineligible that would be

adopted in the absence of the project. Good Company noted this could limit many measures that have a component of free-ridership in a portion, but not all, of the population. Good Company recommended the commission could instead calculate a Net-to-Gross ratio for these measures, as adopted in California, that reduces incentive levels to account for free-ridership.

TXCHPI requested consideration of the prohibitions in proposed subsection (e)(3)(B)(i) relating to "eliminating an existing function," and take official notice of the functions that are purposefully eliminated by clean, efficient CHP installation and replaced with an alternative function.

Commission response

The commission does not agree with the Sierra Club's recommendation that language be added to ensure that the expenditures for efficiency correspond to the amount paid by the customers and that the utilities disclose the value of the programs. Such a provision would be duplicative of the cost-effectiveness standards in the rule, to some degree, and the rule requires reporting to the commission and participating customers, without the additional disclosure proposed by Sierra Club. The reports to the commission are readily accessible to customers on the commission's web site, and the utilities in recent years have posted a summary report on the Texas Efficiency web site that would be useful for customers.

The commission agrees with Good Company's recommendation permit utilities to adopt programs that do not include incentive payments, such as educational programs, and is amending subsection (e)(3) to permit, rather than require, incentives. The commission also

does agree with Good Company's recommendation to modify subsection (e)(3)(B)(ii) to permit some measures to be eligible in the program that would be adopted in absence of the project, with discretion to use a net-to-gross adjustment or other programs modifications to reflect the fact that some customers will adopt the measures, even in the absence of the utility program.

The commission does not agree with TXCHPI's suggestion to amend the prohibition in subsection (e)(3)(B)(i) relating to "eliminating an existing function." The commission concludes that combined heating and power is not specifically "eliminating an existing function." Rather, the commission believes that this technology represents an alternative choice, within the market, for customer to meet its energy needs and for utilities and customers to achieve energy savings.

First, Texas ROSE and TLSC proposed adding subsection (e)(3)(B) to require utilities to establish a program in which REPs pay incentives directly to end-use customers. Texas ROSE and TLSC, and the Sierra Club, also proposed adding subsection (e)(3)(C) to require an electric utility to establish standards to encourage the value of the incentives to be passed on to the end-use customer. Texas ROSE and TLSC also proposed adding subsection (e)(3)(D) to prohibit projects or measures that would reduce demand or energy by eliminating an existing function or shutting down a facility or operation; would be adopted even in the absence of the energy efficiency project; would result in negative environmental or health effects; would involve the installation of self-generation or cogeneration equipment, except for renewable DSM technologies; or would consist of a rate plan offered to customers by a retail electric provider.

Texas ROSE and TLSC noted that their proposed subsection (e)(3)(D)(i) is similar to a provision in the current rule, except that the proposed rule would permit an appliance recycling program. They recommended that any appliance recycling program be evaluated and discussed in a public process with final approval by the commission vetted, as required by statute, and that the language allowing the program be deleted.

Texas ROSE and TLSC also commented that it is the responsibility of the commission to make distinctions in the energy efficiency rule to assure that ratepayer dollars spent on energy efficiency programs are spent on investments that provide the greatest overall return to the consumer in lower electricity costs and environmental improvement. They stated the proposed rule makes no distinction and provides no guidance for directing utilities toward program decisions that are in the best interests of the consumer and environmental improvement. Texas ROSE and TLSC disagree with provisions of the proposed rule that permits incentives to be paid for equipment that generates electricity, which except in the case of renewable DSM technologies, is prohibited under the current rule. They argued in favor of a provision like that in the current rule that requires an energy efficiency measure to have a useful life of at least ten years. Finally, they noted that rate plans rely on customer practices to alter the timing of energy use and have no verifiable useful life or persistence of savings, and they asserted that residential and low income consumers will be paying surcharges to cover the costs of advanced meters, which will benefit the REPs.

Commission response

The commission does not agree with Texas ROSE and TLSC's proposal to modify subsection (e)(3)(B) to require each utility to establish a program in which REPs pay incentives directly to end-use customers. The commission concludes that payments to customers are not necessarily the most effective use of utility resources that are being devoted to the energy efficiency program. The commission declines to adopt the Sierra Club, Texas ROSE and TLSC proposal to add subsection (e)(3)(C) to encourage each utility to establish standards to encourage that the value of incentives to be passed on to the end-use customer. The statute requires that the rules encourage the value of the incentives be passed on to the customer, but does not require the utility to establish specific standards. This issue is addressed in greater detail below.

The commission does not agree with Texas ROSE and TLSC's proposal for an additional subsection (e)(3)(D), which would set forth criteria for determining the eligibility of standard offer and market transformation programs for compensation or payments. The rule provides requirements for standard offer programs and market transformation programs but leaves the utilities a good deal of latitude, within the rules, in establishing such programs. The commission concludes that this latitude will permit utilities to respond to the challenges of meeting higher savings goals more effectively than standards that limit the utilities' discretion. Similarly, the commission concludes that utilities should have the latitude to permit appliance recycling programs and CHP, which will permit customers to meet their energy needs more efficiently. This rule will establish broad policy and give the utilities the discretion and incentive to meet the goals of the section in a cost-effective

manner. This rulemaking proceeding has provided an opportunity to public comment on the benefits of appliance recycling and CHP, and the commission concludes that an additional opportunity is not warranted.

The commission does not believe that it should specify that "rate plans" do not qualify for energy efficiency program incentives. One of the objectives of the 2007 legislative changes was to encourage retail providers to participate in energy efficiency programs, and they may decide to do so through programs that have a rate component. Prohibiting them from receiving incentives for rates may narrow their options for participating in energy efficiency programs. However, the commission recognizes that the REPs have competitive reasons to develop and deploy innovative rate plans that provide benefits to their customers, and that in deploying such plans they seek to gain an advantage over other REPs that are competing for retail customers. The commission believes that the utilities will need to carefully assess proposals from REPs to ensure that they are consistent with this section and the objectives of the energy efficiency program, but it does not believe that the rule should prohibit programs that include a rate component.

§25.181(f): Cost-Recovery Factor

Cities proposed modifying subsection (f) to permit the utility to timely recover the reasonable "incremental" costs of providing energy efficiency programs "to the extent such costs are not already recoverable through the utility's base rates." Additionally, Cities sought to eliminate the "forecast" of the energy efficiency program costs and add that costs recoverable through the Energy Efficiency Cost Recovery Factor (EECRF) "shall be based on prudent test year levels

adjusted for known and measurable changes" and reflect the spending necessary to meet the utility's goals. Cities recommended that energy efficiency cost recovery provisions be based upon actual incremental costs incurred by utilities to encourage cost-effective energy efficiency and demand-side management programs that provide verified measurable net economic benefits to consumers.

Texas ROSE and TLSC proposed modifying §25.181(f) so that an EECRF rate schedule is permissible, rather than mandatory, and recommended that the forecast of the energy efficiency program costs reflect the spending necessary to meet the utility's goals under this section. Texas ROSE and TLSC commented that there is no statutory basis for setting the EECRF using future budgets, because the statute uses the term expenditures. They asserted that since payments to EESPs are based on completed work and actual costs, the same principle should apply to the EECRF. OPC and TIEC also argued that the plain language of the statute refers to "establishing an energy efficiency cost recovery factor for ensuring timely and reasonable cost recovery for utility expenditures made to satisfy the goal" and that "expenditures made" means recovery of costs incurred and not recovery of costs to be incurred. ARM also opposed the use of forecasted costs.

OPC also disagreed with the recovery of the cost of energy efficiency programs, based on forecasted budgets, and suggested that the commission amend the rule to allow recovery of historical costs through the surcharge. OPC noted that residential and small business customers will bear the brunt of the program costs, based on the proposal to create a non-bypassable surcharge to consumers to recover the costs of the energy efficiency programs outside a base rate

case and the exclusion of industrial customers from any energy efficiency programs. OPC stated that residential and small business customers have a right to prudent business operations on the part of the utilities and electric service providers, energy efficiency products that allow them to directly share in the financial incentives created by the energy efficiency programs, assurance that any costs utilities seek to recover through the proposed surcharge are necessary and reasonable to meet the energy efficiency goals, and an equitable distribution of benefits among and within the customer classes. OPC argued that a future test year cost of service would be problematic and run counter to the traditional use of a historical test year for ratemaking in Texas.

TIEC noted that, in general, the use of recovery factors to allow utilities to recover energy efficiency costs outside of a rate case is disfavored in ratemaking and should be discouraged. TIEC stated that if a utility is under-recovering its costs, it should initiate a rate proceeding to recover such costs. TIEC stated that if a utility is allowed to recover costs on a piecemeal basis, a utility may double-recover, or over-recover its costs. TIEC noted additionally, that a comprehensive rate proceeding allows the commission to consider the full impacts of load growth and decide whether increased revenue from additional customers may offset cost increases. TIEC stated that these are fundamental ratemaking principles and are essential to maintain balanced regulation.

TIEC recognized that HB 3693 authorizes the commission to establish a cost recovery factor to ensure timely and reasonable cost recovery of energy efficiency costs, but argued that the proposed rule would make a significant departure from traditional ratemaking practices. P.U.C.

Substantive Rule §25.231(a) provides that "rates are to be based upon an electric utility's cost of rendering service to the public during a historical test year, adjusted for known and measurable changes." TIEC noted that, with few exceptions, the commission has set rates based on historical costs. TIEC stated that similar cost recovery factors, such as the ERCOT TRCF, are based on historical costs. TIEC stated timely cost recovery does not mean that costs must be recovered contemporaneous with their occurrence. TIEC stated that using forecasted amounts could result in significant over- or under-collection of energy efficiency costs.

ARM's recommended a comprehensive revision to the proposed subsection (f). ARM noted that the "forecasted" costs that the proposed rule would permit in an EECRF are tied to PURA §39.905(b)(1), which requires the commission to adopt rules and procedures that establish an EECRF for "ensuring timely and reasonable cost recovery for utility expenditures made to satisfy the goal" of PURA §39.905. ARM commented that the "timely recovery" requirement in the statute is intended to permit the electric utility to recover its energy efficiency costs outside of the context of a general rate case, given the possibility of long periods elapsing between those proceedings. According to ARM, using historical annual costs would allow an assessment of the reasonableness of those costs prior to their inclusion in rates, and, consequently, the reconciliation proceeding in proposed subsection (f)(12) would not be necessary. ARM stated that the use of historical annual costs is consistent with the approach employed in proposed subsections (f)(4), (f)(6) and (h) to adjust the EECRF for historical annual under- and over-recoveries and for the energy efficiency performance bonus based on the electric utility's achievements in the previous calendar year. ARM stated, moreover, the use of historical energy efficiency costs would minimize the extent to which there is an under- or over-recovery of

annual costs and annual revenues, and that the use of forecasted annual energy efficiency costs could result in a mismatch between the forecasted costs and the costs actually incurred.

EUMMOT noted that by implementing a cost recovery mechanism consistent with HB 3693, the utilities will receive more timely recovery of the costs necessary to operate these successful programs. EPE agreed, and stated that the proposed rule changes should allow utilities to receive more timely recovery of necessary costs incurred to implement successful standard offer and market transformation programs. Efficiency Texas proposed that utilities be given timely cost recovery of their energy efficiency expenditures, as well as a financial incentive payment for exceeding the legislature's minimum energy efficiency goal. Efficiency Texas stated that HB 3693 made clear that utilities were to be given timely cost recovery and that a "bonus" would be given to those utilities that exceed the energy efficiency goals.

Commission response

The commission does not agree with Cities, Texas ROSE and TLSC, OPC, TIEC, and ARM's suggestion to utilize "historical" rather than "forecast" of energy efficiency costs to permit the utilities to timely recover the reasonable costs of providing energy efficiency programs. The commission notes that PURA §39.905(b-1) states that the energy efficiency cost recovery mechanism may not result in an over-recovery of costs but may be adjusted each year to change rates to enable the utilities to match revenue to energy efficiency costs and incentives. Therefore, the commission believes that the process in the proposed rule, which it is adopting without major changes, ensures that no over-recovery will occur. The commission recognizes that the EECRF is a departure from established practice with

respect to rate-setting, for energy efficiency expenditures, but it concludes that the legislature's directive for the utilities to meet higher savings goals and the explicit inclusion of provision for timely cost recovery in the statute supports this departure from past practice. As ARM notes, permitting recovery of historical costs outside of a general rate case affords utilities some benefit with respect to timeliness of cost recovery, but the commission concludes that, in view of the higher energy savings goals, the additional benefit of contemporaneous cost recovery, through the use of forecasted costs, is appropriate and consistent with the statute.

Texas ROSE and TLSC proposed that prior to implementing the EECRF, a utility would be required to file an independent review of its programs to verify that the programs are reasonable, prudent and nondiscriminatory. Texas ROSE and TLSC stated that efficiency costs should be included in rates with excess expenditures being covered by the EECRF between rate cases. This is consistent with standard ratemaking procedures and would permit energy efficiency costs to be reviewed by all parties, as are all other expenditures. Cities proposed modifying subsection (f)(2) to specify that a utility's base rates shall be "designed to exclude all" energy efficiency program costs.

Commission response

The commission does not agree with Texas ROSE and TLSC's proposed modification of subsection (f)(2) to require an independent review of utility programs prior to implementing the EECRF. The commission believes that such a prior review would impede the objectives of timely cost recovery and higher program goals; in addition, it

concludes that the rule adequately ensures that the programs are reasonable, prudent and non-discriminatory. The commission declines to include Cities' proposed modification to subsection (f)(2). The commission concludes that the rule being adopted will ensure that no over-recovery by the utilities will be permitted and that subsection (f)(2), as adopted, is more specific about the timing of excluding energy efficiency costs from base rates.

Cities proposed modifying subsection (f)(3) so that the EECRF would be calculated to recover the "prudently incurred incremental" costs associated with each "cost-effective energy efficiency" program from the customer classes that receive services under each program.

Xcel stated that the utility should be required to identify costs by customer class or submit factors to allocate costs among the customer classes "based upon the class allocation factors approved in the electric utility's last base rate case" and propose charges for the recovery of the costs. Xcel stated that class allocations are often very heavily debated in base rate case proceedings. It also recommended that the commission add a carrying charge component for over- or under-recovery balances. Xcel noted that carrying charges compensate both the utility and the ratepayer from balances due to over- or under-recoveries. Xcel stated in addition, carrying charges remove the financial regulatory lag from these expenditures and collections.

Commission response

The commission does not agree with Cities' proposed modification to subsection (f)(3). The concepts that the Cities would add to this subsection are adequately addressed in other provisions of the rule. The commission agrees with Xcel's suggestion that utilities should

provide factors for allocating energy efficiency costs, based on the most recent base rate case. Providing this information will facilitate the processing of EECRF cases. In addition, the commission may adopt a rate-filing package to facilitate the review of requests for an EERCF. The commission does not agree that carrying charges should be applied to over- and under-recoveries. The costs and revenues will be reviewed on an annual basis, and any over- or under-recoveries will be promptly reflected in a revised EECRF. In addition, the rule provides for much more timely cost recovery than the normal rate-case process, so carrying charges on under-recoveries should not be a significant issue for utilities.

Cities proposed modifying subsection (f)(4) to specify that each year, a utility with an EECRF must file an application to adjust the EECRF in order to "eliminate," any over- or under-collection of energy efficiency costs resulting from the use of the EECRF.

Commission response

The commission believes that the rule being adopted addresses the over- and under-recovery of program costs, by requiring that adjustments to the EECRF "minimize" such over- and under-recoveries. The elimination of an under- or over-recovery may not be practical, because it could involve small amounts allocated over a large number of billing determinants.

Cities proposed adding language to subsection (f)(5) to establish that the utility has the burden of demonstrating that the amounts requested through the EECRF are justified in light of existing

earnings of the utility during the test year period. TXU Energy proposed substituting "general rate proceeding" for "base rate case" in this subsection.

ARM noted that it is unclear how subsection (f)(5) works in concert with other proposed subsections. ARM stated that the establishment and adjustment of the EECRF in proposed subsection (f) is based on the concept of annual information, *i.e.*, forecasted annual energy efficiency program costs, the annual requirement to "true up" the EECRF to account for under- and over-recoveries, and the incorporation of an annual energy efficiency performance bonus amount based on the prior year. ARM noted that if the electric utility may change the EECRF in any general rate proceeding at any time during the year, as opposed to through a standardized annual process, it is unclear whether the new EECRF could properly reflect those annual adjustments. ARM stated that the only time that it would make sense for the electric utility to change its EECRF in a general rate case is when that proceeding involves the elimination of energy efficiency program costs from base rates, pursuant to proposed subsection (f)(2).

Commission response

The commission does not adopt Cities' suggestion with respect to burden of proof; subsection (f)(11), which describes the showing that a utility must make in an EECRF filing, implicitly establishes that the utility has the burden of proof in such a case. The commission agrees with TXU's suggestion that "base rate case" is better terminology. The commission agrees with ARM that a general rate proceeding may be impractical and could delay the implementation of cost recovery, but that this option may be useful, particularly in 2008. The schedule for adoption of this rule may make it difficult for utilities to file

EERCF proceedings before May 1, 2008, and if a utility files a base rate case in late 2007 or during 2008, it may be possible for it to use the base rate case to establish a 2009 EECRF. For small utilities, it may also be desirable to use a rate base case to establish or modify an EERCF. Accordingly, the commission does not adopt the ARM suggestion.

TXU Energy recommended that energy efficiency costs not be recovered through a monthly customer charge. ARM stated that it is unclear whether an electric utility with an EECRF is required to annually seek approval of a modified EECRF that reflects all changes to the EECRF rate components that are specified in proposed subsection (f)(6). ARM also commented that while proposed subsection (f)(6) requires the EECRF to be set in a manner that adjusts for past over-or under-recovery of revenues, based on PURA §39.905(b-1), nothing in the proposed rule directly requires that the electric utility also propose changes to the EECRF that relate to forecasted annual energy efficiency costs, historical annual performance bonuses, or other annualized factors that impact the EECRF, to the extent that any of those factors change from year to year.

Commission response

The commission does not agree with TXU Energy's suggested deletion of "or a monthly customer charge" from subsection (f)(6). There may be utilities that are participating in energy efficiency programs that use a customer charge for energy efficiency costs, and these utilities should have the flexibility to recover the costs through a monthly charge, with commission approval.

The commission does not entirely agree with ARM's suggestions. Subsection (f)(4) requires a utility to apply to adjust its EERCF on an annual basis to minimize any over- or under-recovery of costs. The rule clearly contemplates that changes in costs and bonuses be reflected in an order modifying the EERCF. However, wording changes are incorporated in the rule as adopted to make this explicit.

Cities proposed that a utility under subsection (f)(7) may "seek to" defer the costs of complying, and recommended including language regarding the recovery of deferred costs "to the extent such recovery is not prohibited by existing rate agreements."

CenterPoint proposed that subsection (f)(7) be amended to permit a utility that is unable to establish an EECRF as a result of a rate freeze to elect to defer the costs of complying with this section and any bonus that it would otherwise earn and to file notice of its election with the commission. Within thirty days of the utility's filing, the commission would issue an approval of the deferral, which could be done administratively. During the period of deferral, costs and bonuses would accrue carrying costs at the utility's last commission-approved weighted average cost of capital. The utility would be entitled to recover its deferred costs and bonuses through an energy efficiency cost recovery factor on the expiration of the rate freeze period. According to CenterPoint, its recommended changes to the deferral provision are intended to ensure that CenterPoint and other electric utilities that agree to multiple year rate freezes are not penalized by the rule. CenterPoint recommended deleting the reference to the year 2008, so that the provision is not interpreted to apply only to costs for the year 2008. CenterPoint would include carrying costs in the deferrals to allow electric utilities to recover the entirety of their costs and

bonuses, which it argues would not be unfair or disadvantageous to Retail Electric Providers and consumers. CenterPoint stated that the approval process it proposed would allow electric utilities to recognize the deferrals for accounting purposes.

Commission response

The commission disagrees with Cities that the rule should provide only an opportunity to seek a deferral of energy-efficiency costs. The purpose of this provision is to put utilities that have agreed to multi-year rate freezes on the same footing as utilities that are not subject to such rate freezes. The rule would establish that rate-freeze utilities would have a right to defer these costs, if it is not inconsistent with a prior rate agreement that has been approved by the commission. The commission is not requiring that utilities electing to defer costs and bonuses file notice of that election. The commission concludes that the procedures for approval of an EERCF will also work for approval of an election to defer costs. Other parties that have an interest with respect to the deferral of costs should have an opportunity for expressing them, and for this reason it does not adopt the CenterPoint proposal that such applications be processed administratively. The commission expects that the utilities that intend to defer costs will file an application to do so on a timely basis, and concludes that a separate notice of an election is not necessary. The commission agrees that the deletion of the year 2008 from subsection (f)(7) is appropriate, so that the provision is not interpreted to apply only to costs for the year 2008. The commission also agrees that carrying costs should be included in the utility's ultimate cost recovery in the event of a deferral order, because the costs may have to be deferred for several years.

Commission response

Cities proposed modifying subsection (f)(10) so that a hearing, if requested, would be held no earlier than the first working day after the 45th day after the application is "determined to be sufficient," instead of "filed."

Commission response

The commission has changed the rule to trigger the hearing timeline to the date that a sufficient application is filed. This means that a hearing can be delayed if the utility failed to file a sufficient application. The commission does not adopt Cities' specific proposal, because the hearing date should be tied to when the parties had access to a sufficient application, not to a subsequent, indefinite date when the presiding officer determine that the application that had been filed is sufficient.

Cities proposed modifying subsection (f)(11)(A) to ensure that the costs to be recovered through the EECRF are reasonable "and necessary" to provide energy efficiency programs and not based on "costs to meet the utility's goals under this section." In addition, Good Company commented that this subsection should specify that the energy efficiency programs are "cost effective."

Commission response

The commission does not agree with Cities' and Good Company's suggestions. These concepts are set out elsewhere in the rule, the necessity of costs in subsection (f)(11)(A), and cost effectiveness in subsection (g).

TXU Energy proposed that subsection (f)(12) be amended to require a utility to apply to reconcile the costs it recovered through its EECRF every three years. TXU Energy expressed the view that a reconciliation would ensure appropriate review of expenditures and revenues, particularly for utilities who do not file for base rate cases for several years.

CenterPoint commented that the rule should provide that the costs of contested case proceedings should not be considered part of program costs or included in the calculation of net benefits, but should be recovered through the EECRF. CenterPoint stated the subsections (f)(9) through (f)(12) of the proposed rule, as amended by the Staff memo dated November 1, 2007, create a somewhat cumbersome process for establishing an EECRF. CenterPoint stated that the process is compounded by adding a reconciliation of the costs recovered through the EECRF at least every three years. CenterPoint understood and appreciated the commission's desire to subject the recovery of costs and bonuses to review through the contested case process, but if each EECRF filing is going to be a contested case, then there is no point in having a reconciliation, and conversely, if there is going to be a reconciliation of costs at least every three years, there is no need to have each EECRF filing be subject to anything beyond commission staff review and administrative approval. CenterPoint noted that the key consideration here is that the encouragement to utilities to increase their energy efficiency offerings, and the operation of the EECRF consistent with PURA §39.905(b) and (b-1) should not get bogged down by the contested case process. CenterPoint stressed that the commission must recognize that the contested case process will impose costs on the utility, among which will be the utility's reimbursement of municipal "rate case" expenses.

ARM stated that proposed subsection (f)(12) appears to contemplate that all such changed factors can be addressed in a proceeding to adjust the EECRF, but it does not go so far as to require this. ARM's primary concern here was to ensure that the process in proposed subsection (f) provide REPs with adequate notice of proposed changes to the EECRF and that any adjusted EECRF be approved by the commission using a standardized process from year to year, so that there is a requisite degree of certainty with respect to what those adjustments may be and when they will occur. ARM supported a mandatory annual reconciliation of the EECRF, in which all components to the EECRF that have changed are addressed at the same time. ARM did not support the adoption of the inadvertently omitted language in proposed subsection (f)(12), as specified in the memo issued by commission staff.

Commission response

The commission agrees with TXU Energy that the rule should require a utility to apply at least every three years to reconcile costs recovered through its EECRF. With respect to CenterPoint's comments that an annual EECRF filing may not be useful in light of a three-year reconciliation proceeding requirement, the commission believes that an annual EECRF filing will provide timely cost recovery, which will be advantageous to utilities, particularly if their budgets increase to meet higher energy-efficiency goals. The scope of the annual filings is limited, so that the expedited approval process should be workable. The commission does not believe that it need address the issue of recovery of expenses related to the annual EECRF proceeding and reconciliation proceedings in the rule. It is not clear whether either of these filings will result in significant additional administrative costs or whether the cities with regulatory authority will choose to participate in them. The

reconciliation is intended to be a more thorough review of the energy efficiency programs and costs, and the commission does not believe that it is practical to conduct this level of review annually, as ARM proposed.

§25.181(g): Incentive Payments

Cities proposed modifying proposed §25.181(g) to provide that the sum of incentive payments and other program costs could not exceed the net economic savings to retail customers associated with such energy efficiency programs. Cities opined that the proposed energy efficiency incentives, cost recovery provisions, and electric utility performance bonus provisions are overly-generous and are likely to lead to inflated estimates of energy efficiency impacts and excessive spending on programs, and that such spending has the potential to eliminate any net benefit that otherwise might accrue to consumers. Cities supported a more deliberate effort to encourage energy efficiency, focusing on programs with the most promise and for which consumer benefits have been demonstrated.

TXU Energy proposed including language to permit utilities to adjust incentive payments "upwards" during the program year, and also proposed that such adjustments should be publicized in advance in the materials used by the utility. TXU Energy noted that subsection (g) could cause difficulty for REPs that design and administer programs under utility guidelines if those amounts were to be reduced during the program year. TXU Energy suggested that upward adjustments would not likely cause REPs this difficulty, but downward adjustments could.

EUMMOT proposed including a provision that would permit a utility to offer different incentive levels for the purposes of either encouraging energy efficiency measures that have been historically underutilized or to provide additional incentive for measures that have historically been over emphasized, under the standard incentive levels. EUMMOT believed that disclosure of incentives provided to program participants is unnecessary and may be difficult to impose. EUMMOT also suggested explicit authorization for a utility to offer higher incentive levels for projects in areas that have traditionally been underserved by the utility's energy efficiency programs.

Public Citizen, Environmental Defense, SEED suggested differential incentives. In their view, flexibility with respect to incentives would allow to utilities to reach hard-to-reach customers and underserved areas, and foster innovative and emerging technologies and market transformation, especially for renewable DSM. Sierra Club proposed that subsection (f)(9)(D) should include caps on incentive levels for a standard offer program not in excess of 100% of avoided cost for hard-to-reach customers, fifty percent of avoided cost for other residential and small commercial customers, and thirty-five percent of avoided cost for large commercial and industrial customers. It also proposed that for programs where there are additional avoided costs because of transmission and distribution constraints identified by the utility, the incentives could exceed these caps, as long as they do not exceed 100% of avoided costs. Texas ROSE and TLSC proposed that subsection (g) should include similar caps on incentive levels. In particular, they proposed the same cap for hard-to-reach customers; 100% of avoided costs, including the avoided costs of transmission and distribution, for installations of renewable DSM technologies; seventy-five percent of avoided costs for programs that produce energy savings; and fifty percent

of avoided costs for load control and load management programs. Texas ROSE and TLSC favored a cap of 100% of avoided costs for low-income and hard-to-reach customer programs, to make energy efficiency investments affordable for these customers. In their view, a program for these customers must be designed to require no payment from the consumer. In support of a cap of seventy-five percent of avoided costs for programs that produce both energy savings and demand reductions, they argued that current programs are fully subscribed at lower levels, and when the level of efficiency increases along with the costs to the consumer the higher incentive caps may apply.

Finally, Texas ROSE and TLSC suggested that energy savings are unlikely for load control and load management programs. Rather, energy use may increase. They commented that unlike other programs that permanently reduce electricity use, these programs are designed to reduce demand to maintain system reliability during peak periods. Because the programs have no track record for saving energy, they provide no value as an emissions reduction tool. Thus, the value should be capped at a lower level than programs that save energy and also reduce emissions.

The Sierra Club stated that the proposal gave considerable flexibility to the utilities in setting incentive payments, as long as they do not exceed 100% of the avoided costs. Sierra Club suggested that the importance of this section is directly related to how avoided costs are determined. In agreement with Texas ROSE and TLSC, Sierra Club believed that utilities should be permitted to offer higher incentives for renewable DSM measures because of the avoided transmission costs, which are not adequately addressed in the proposed rules. The Sierra Club stated they were supportive of this "flexible" language only if avoided costs were more reflective

of the actual retail prices that are avoided, and for renewable DSM, of avoided transmission costs. The Sierra Club noted that otherwise, this flexible language should be scrapped in favor of specific limits on incentives like the ones they proposed.

Commission response

The commission disagrees with Cities' proposed modifications to subsection (g). While the commission is sensitive to Cities' concern that costs be under control and associated savings be maximized to the extent possible, as stated in the commission's response to comments on subsection (d) above, the commission believes that these issues are adequately addressed in the rule, without these changes. The commission does not agree with TXU Energy's suggestion that, if adjustments to incentive payments are permitted, only increases in incentives should be permitted. The commission believes that the rule adequately allows the utilities to adjust their incentive payments as necessary to aid their achieving the energy efficiency goals. The utilities have significant experience in managing energy efficiency programs, and they should be able to recognize changes that would inhibit a program's success.

The commission does not agree with the recommendations of Texas ROSE and TLSC, Sierra Club, Public Citizen, Environmental Defense, and SEED regarding caps on incentive levels as percentages of avoided costs. The commission concludes that utilities should have the flexibility to establish incentive levels, subject to the avoided cost limit, in order to best achieve their energy efficiency goals. Different incentive levels may be appropriate in different areas of the state and at different time, and fixed limits in the rule

would impede utilities' ability to adjust their programs to meet the statutory goals. The commission is adopting language similar to that proposed by EUMMOT to describe reasons for different incentive levels. The commission is not adopting the EUMMOT proposal that changes in incentive levels need not be publicized. These programs depend on energy efficiency service providers' participation, and the incentive levels are clearly a matter of some importance to the service providers. The publication requirement that is included in the rule is not onerous, but is one that should help keep the service providers engaged in the utility efficiency programs.

The commission disagrees with Texas ROSE and TLSC's recommendation to provide the cost of avoided transmission costs so that higher incentives can be allowed for renewable DSM measures and the highest efficiency end-use technologies that are not customarily installed under the standard offer programs. This issue is discussed in the commission's response to Preamble Question Two.

§25.181(h): Performance Bonus

EUMMOT suggested that an energy efficiency bonus awarded under this section not be included in the calculation of the utility's energy efficiency program expenditures.

Cities proposed modifying proposed subsection (h) of the proposed rule so that a utility can receive a bonus only if it exceeds its demand reduction goal "through the implementation of cost-effective energy efficiency measures that provide net economic savings to retail customers." Likewise, Texas ROSE and TLSC sought to modify this section by allowing utilities to "apply"

for a performance bonus, and not simply providing that a utility be "awarded" a bonus if it exceeds its goal. They stated that PURA §39.905(b)(1) directs the commission to adopt rules to reward utilities that exceed the minimum goals established by PURA. In their view, a utility should have outstanding program results in order to be eligible for incentives. They defined a successful program as one that meets ninety percent of its stated energy efficiency goal.

Sierra Club and Reliant sought to limit those eligible for bonuses to utilities that keep administrative costs under ten percent of total program costs. The Sierra Club suggested in addition that, rather than require that a performance bonus be granted for utilities that exceed the limit as the current rule reads, the rule should permit such bonuses. The Sierra Club, Texas ROSE and TLSC proposed that at least eighty-five percent of the total demand reduction goal come from programs that save both demand and energy, so that the rule would promote more comprehensive programs. Public Citizen, Environmental Defense and SEED recommended that a utility not receive a bonus unless it exceeds its demand reduction goal and achieves at least eighty percent of its total demand savings from programs that save both demand and energy. The Sierra Club argued that a utility should not be eligible for a bonus, unless it meets at least 120% of its demand reduction goal with at least ten percent of its savings achieved through Renewable DSM Technology programs. Texas ROSE and TLSC urged that a utility should not be eligible for a bonus, unless it achieves at least five percent of its savings through Renewable DSM Technology programs.

Texas ROSE and TLSC asserted that to be eligible, the utility's programs should be very cost effective and administrative costs should not exceed ten percent of total program expenditures.

In the interests of promoting renewable DSM, they stated that a utility should achieve at least five percent of its goal with renewable DSM measures. Public Citizen, Environmental Defense, and SEED proposed for a utility that meets at least 120% of its demand reduction goal with at least ten percent of its savings achieved through Renewable DSM Technology programs an additional ten percent bonus.

OPC articulated several problems with the proposed bonuses to utilities for exceeding their demand and energy savings' goals. OPC noted that the calculation appears to be straight-forward for determining growth in demand, but it does not provide any standards for calculating the demand reductions, which are to be based on an average of the utilities' last five years of annual peak demand growth. OPC specified that any calculation of demand savings for the programs authorized by this rule should not directly or indirectly include demand savings obtained from other programs. OPC recommended that bonuses be contingent upon proof of administrative efficiency and proof that all energy efficiency program goals established were significantly met. At the public hearing, OPC stated that, unless a utility achieves 110% of the goal, the utility should not be eligible for a performance bonus. Reliant proposed that a utility would not be eligible for a bonus unless it achieves at least 120% of its demand goal.

Efficiency Texas urged that a bonus be available that would be a reasonable, but not excessive, incentive payment for those utilities that exceed their legislative energy efficiency mandate in a cost-effective manner. It also noted that increasing energy efficiency should always be the first public policy program to pursue. Efficiency Texas further proposed that utilities be given timely cost recovery of their energy efficiency expenditures, as well as a financial incentive payment for

exceeding the legislature's minimum energy efficiency goal. Efficiency Texas stated that HB 3693 made clear that utilities were to be given timely cost recovery and that a "bonus" should be given to those utilities that exceed the energy efficiency goals.

Commission response

The commission does not agree with Cities' proposed modification to subsection (h) that would provide that a utility could receive a bonus only if it exceeds its demand reduction goal through cost-effective measures providing a net economic savings to retail customers. As stated in response to comments on several sections in this rule, the commission believes that the structure of the rule, including its reporting and review processes, will ensure that utilities implement the programs in a cost-effective manner. The commission does not adopt the suggestion that the utility merely has a right to apply for a bonus, that is, that utilities that meet or exceed their goals "may" receive a bonus. The criteria for granting a bonus should be clear and predictable. The commission also believes that bonuses that result from the rule will be related to exceptional performance in the area of energy efficiency. The Cities' proposal is likely to make the determination of whether a utility qualifies for a bonus significantly more contentious, and would in the end not provide the inducement that is intended. The bonus structure is set up so that utilities that reach 100% or more of their goal receive a bonus. As is noted in connection with the Cities' comments, the bonuses are intended to reward exceptional performance in the area of energy efficiency, not result in a contentious contested case about whether a utility qualifies for a bonus. The commission believes that predictable incentives will provide a real inducement for exceptional performance.

The commission does not agree with the Texas ROSE and TLSC, and Sierra Club's proposal to limit bonuses to utilities that have kept administrative costs under ten percent of their total program costs. The proposed rule would have required that a utility meet cost limits prescribed in the rule, and the commission is amending this provision to explicitly refer to the caps in subsection (h), a ten percent cap on administrative costs and a ten percent cap on research and development. The commission does not agree with the Sierra Club, Public Citizen, Environmental Defense, SEED, and Texas ROSE and TLSC's suggestion to require a certain percentage of the total demand reduction goal come from programs saving both demand and energy, or that promote renewable DSM or that an additional bonus be provided for meeting a renewable DSM goal. The commission believes that this rule represents a higher emphasis on energy savings than existed in the prior version of the rule, but it also believes that the incentive structure should be relatively simple. Other commenters were strong proponents of demand response programs, and structuring the rule to provide additional emphasis on energy programs would be contrary to the interests of demand-response advocates. The rule emphasizes cost-effective energy efficiency programs, within broad guidelines, and includes reward mechanisms that are based on exceeding the specific goals in a cost-effective manner. The commission believes that the enactment of higher goals and authority for cost-recovery mechanisms and bonuses in HB 3693 reflects the conclusion by the legislature that energy efficiency programs are important today and that the programs that the utilities have operated have been quite successful. Based on this success, the commission concludes that details such as caps on incentives by rate class and multi-factor incentive programs are not appropriate.

The commission agrees with OPC that calculations of demand savings for the programs authorized by this rule should not directly or indirectly include demand savings obtained from other programs. With respect to Efficiency Texas's comments regarding bonus awards, the commission believes that the methodology for approving bonuses is consistent with the objectives of HB 3693.

The commission does not agree with OPC's comments that a utility should achieve 110% of its goal to receive a bonus or Reliant's suggestion that a utility must achieve at least 120% of its demand goal to qualify. The bonus structure is scaled, so that exceeding the goal by a small amount will result in a small bonus, while exceeding the goal by a large amount could lead to a large bonus, depending on cost effectiveness. The commission concludes that this structure will result in a clear emphasis among the utilities for meeting the goals, which is consistent with the legislature's decision to increase the demand goals in the statute.

Reliant proposed substituting "net of utility costs" for "net benefits realized in" in describing the calculation of a bonus for meeting the demand reduction goal. Texas ROSE and TLSC also recommended adding to subsection (h)(1) the following requirements: (1) the utility must document savings and other requirements through an independent review of its programs; (2) all of the programs offered by the utility must meet at least ninety percent of the goal for the program; (3) the utility must meet or exceed goals for achieving energy savings for goals for programs offered to hard-to-reach consumers; and, (4) there should be a cap on the performance bonus for a utility that exceeds its demand reduction goal. Reliant noted that although it does not

fundamentally oppose the concept of a performance bonus for exceeding the goals at a cost equal to or better than the budgeted amount, the bonus established in paragraph (3) may result in a bonus payment that is much greater than what is intended. Reliant commented that a quick "back of the envelope" calculation indicated that the bonus could be very close to the same amount as the total program costs. Based upon calculations from, for example, CenterPoint's energy efficiency report filed April 2, 2007, it found that bonuses could be excessive. Reliant proposed, therefore, that the bonus be capped at no more than ten percent of the program costs, as noted above.

Commission response

The commission understands Reliant's concerns regarding the potential size of bonuses that might be awarded to over-achieving utilities. The historical achievements are not necessarily indicative of results that will be achieved with higher energy efficiency goals and lower levels of participation by industrial customers. The commission believes that it is likely that the net benefits will be lower in the future, as utilities obtain more of their savings from residential and commercial customers. Nevertheless, the commission concludes that it is appropriate to establish a cap that is based on the program costs, rather than one that is based on net benefits. For this reason, the commission is modifying the cap in subsection (h)(2) to limit bonuses to twenty percent of program costs. This modification will preclude the award of disproportionately high bonuses. The commission concludes that an independent review of program results is not necessary for the award of a bonus. The commission believes that such a prior review would impede the objectives of timely cost recovery and providing effective incentives for performing above expectations; in

addition, it concludes that the commission has adequate authority to review reported program achievements, if necessary. The commission is not establishing a minimum ninety percent performance level for all of a utility's programs to qualify for a bonus. The utilities may need the latitude to adjust their programs if some are not as successful as expected. The more important point is that the utilities meet or exceed their goals. The commission concludes that requiring that the utility exceed its energy goal is also not necessary. The rule, as adopted, includes significant incentives for utilities to succeed in their energy goals, because the energy savings are a significant element of the net benefits calculation that is used in setting bonus amounts.

CenterPoint proposed that subsection (h)(2) be rewritten to exclude research and development (R&D) expenditures from program costs in calculating net benefits to avoid creating a disincentive for electric utilities to support R&D. ARM was additionally concerned that including R&D costs within the universe of administrative costs might result in decreased R&D expenditures, to the ultimate detriment of electric utility energy efficiency programs. ARM stated that this is particularly true if administrative costs are higher due to the new energy efficiency goals established in HB 3693 and if new types of administrative costs (*e.g.*, a third party advertiser/information clearinghouse) are borne by electric utilities. ARM noted that expenditures for R&D to formulate new and more efficient programs to reduce energy consumption, peak demand, and energy costs are essential to PURA §39.905. ARM stated that PURA §39.905(e) recognizes that such R&D expenditures can "foster continuous improvement and innovation in the application of energy efficiency technology and energy efficiency program design and implementation."

Texas ROSE and TLSC proposed that subsection (h)(2) permit the utility to receive twenty-five percent of the net benefits realized in meeting its demand reduction goal, that all utility costs be included in calculating net benefits, and that the customer classes responsible for the achievement of the net benefits receive seventy-five percent of the net benefits. Reliant noted that it is a misnomer to refer to the calculation in subsection (h)(2) as a "net benefits" calculation. Reliant noted that the current calculation of "net benefits" is total avoided costs minus all utility program costs. Reliant suggested that in reality the "net benefits" are the total avoided costs minus all utility program costs and the EESP's costs. Reliant stated the calculation in the rule does not reflect net benefits. Additionally, Texas ROSE and TLSC recommended language that entitles the utility to receive twenty-five percent of the net benefits and the customer classes responsible for achieving the savings and paying the costs of the programs seventy-five percent of the net benefits. They advocated that the amount of the benefit would be returned to the customer as a rate credit.

Commission response

The commission agrees with CenterPoint's proposal to exclude research and development expenditures from the calculation of the sum of program costs. This issue is also discussed below.

The commission does not agree with Texas ROSE and TLSC's proposal to include EESP costs in calculating net benefits and to require that the customer classes receive seventy-five percent of the net benefits. The commission believes that the bonus structure being

adopted adequately but not excessively rewards utilities and provides them incentives to achieve their goals. This rule is being adopted to modify an energy efficiency program that the utilities administer in competitive markets, through energy efficiency service providers. The energy efficiency program has worked by providing incentives to EESPs, who in turn may provide information and incentives to customers to induce them to participate in the program. For most customer classes, the customers typically make some investment in more efficient appliances or in improving the performance of a home or other building, and often the customer's investment is significant. Requiring utilities to determine and take EESP or customer costs into account in calculating a bonus would be difficult, intrusive, and costly. The commission does not regulate the EESPs and does not believe that it is practical to obtain information from them concerning their costs, without adversely affecting their interest in this program. The program has been successful in motivating EESPs and customers to participate in it, and the mandate that these parties propose is more likely to undermine the program than promote additional participation.

Xcel expressed concern with the proposal that a bonus can only be awarded above 100% of the goal. Xcel stated that because these goals are a significant step, at least a partial performance bonus should be awarded. Xcel noted that in other states such as Minnesota, the bonus starts at ninety percent of the approved goal. Xcel noted that SPS appreciated that the commission developed a performance bonus that encourages utilities to exceed their legislative goals and, based on its experience in other jurisdictions, believes that the percent of net benefits is a good approach.

Commission response

The commission does not agree with Xcel's suggestion that the bonus should be awarded for performance of less than 100% of the goal. The bonus is meant to reward utilities that meet or exceed the goal and should only be awarded to those utilities that do so.

Cities proposed modifying subsection (h)(4) to permit a bonus only when the bonus plus program costs are lower than the total economic savings achieved by retail customers as a result of the energy efficiency program. Texas ROSE and TLSC suggested that the threshold for an additional bonus for savings from programs for hard-to-reach customers be increased from ten percent to twenty percent, consistent with an earlier staff proposal that included an additional incentive for doubling the percent of savings attributable to programs for hard-to-reach customers. In addition, OPC believed that an additional problem is that the proposed bonus cap of twenty percent (and an additional ten percent) is too high; it recommended that the bonus cap be set at five percent, with an opportunity for an additional five percent if the utility meets 150% of its demand reduction goal with at least fifteen percent of its demand reduction savings achieved through Hard-to-Reach programs.

Commission response

The commission concludes that the bonus structure adequately balances the societal objectives of the program and utility obligations, by providing rewards for meeting and exceeding the goals and obligations. The commission believes that the objective of the Cities' suggestion will be met. Because the bonus is calculated as a percentage of net benefits, the bonus plus program costs should be less than the net benefits in all cases. (The

bonus is one percent of net benefits for each two percent of demand savings above the utility's goal, capped at twenty percent of program costs. Unless program costs are below avoided cost, there will be no net benefits on which to calculate a bonus.) The commission has modified the calculation of the cap that will reduce the possibility for very large incentive payments, but it believes that utilities should have the possibility for earning a significant bonus for exceptional performance, and that some of the changes that have been proposed would undermine this possibility.

CenterPoint proposed a new subsection (h)(6) as follows: "A bonus earned under this section shall not be included in the utility's revenues or net income for the purpose of establishing a utility's rates or for any required filing of earnings by the utility." CenterPoint commented that it is conceivable that a party in a future utility rate case will argue that an electric utility's energy efficiency performance bonus should be included in a test year's revenues. CenterPoint stated this would effectively negate the bonus earned and frustrate the intent of the legislature in enacting PURA §39.905(b)(2) directing the commission to adopt rules to reward utilities for exceeding the minimum energy efficiency goals. CenterPoint stated, in fact, that reflecting the bonus in net income for ratemaking purposes could penalize the electric utility if it was unable to exceed its demand reduction goals at the same or higher percentage levels in future years.

Commission response

The commission agrees with CenterPoint that, for the purpose of ratemaking and rate-setting, any performance bonus earned by the utility should not count towards its test year's revenues or for any required filing of earnings by the utility at the commission.

Texas ROSE and TLSC supported the idea that rewards should be accompanied by a corresponding penalty for poor performance. They supported adding provisions to the adopted rule that would penalize a utility that performs poorly, because such a system would be more transparent, direct, and efficient than the standard administrative enforcement process.

Commission response

The commission does not agree with Texas ROSE and TLSC's suggestion that specifically setting forth a bonus structure necessarily means that there should be a corresponding section establishing for penalties solely for poor performance. The commission believes that subsection (u) of the new rule, which provides for a discretionary administrative penalty, suffices to ensure that utilities be held accountable for poor or under-performance. The commission notes that PURA §39.905(g) permits the commission to provide a good cause exception to a utility's liability for penalties, under certain circumstances. The provisions that the commission is adopting are consistent with this approach, which implies that the commission must consider the circumstances for any utility that fails to meet its goal, rather than applying a formulaic approach.

§25.181(i): Program Expenditures

Cities proposed adding language to subsection §25.181(i) so that the costs of administration is "subject to a prudence review." Texas ROSE and TLSC commented that the cost of administration should not exceed ten percent of the total program "expenditures" without regard to the number of customers the utility serves. They further commented that many of the more-

burdensome administrative costs are being lessened by the proposed rule and nothing justifies a higher administrative cost to the utility. In addition, Texas ROSE and TLSC stated that if a utility's administrative costs exceed ten percent of total program costs the utility should be ineligible for a performance incentive bonus. ARM and OPC agreed that the cost of administration should not exceed ten percent.

The Sierra Club stated that HB 3693 does increase the requirements on utilities such that it requires informational programs and advertisements that were not required previously. Like Texas ROSE and TLSC, the Sierra Club suggested that, because this rule increases substantially the provision for administrative costs, only those utilities that keep administrative costs under ten percent of total program costs be eligible for performance bonuses. The Sierra Club suggested, in addition, that the utility be required to pay the costs of an independent measurement verification evaluator as was previously required. The Sierra Club suggested that this evaluation could help the commission make sure that administrative costs were kept as low as possible. Furthermore, the Sierra Club concluded that if the commission considers having a third party contract to promote information and advertising of energy efficiency programs throughout Texas, the rule should specify that administrative costs would fund this third-party contract.

Commission response

The commission does not agree with Cities' proposed "prudence review" language, noting that the rule provides that the utilities will annually report their programs results and that the EECRF would be adjusted to minimize over- and under-recoveries. The commission believes that the reviews of utility programs set forth in the rule, including cost of

administration, are sufficient and notes that the commission has added subsection (f)(13) to the rule, which requires a reconciliation of costs recovered through a utility's EECRF at least every three years.

The commission agrees with OPC, ARM, the Sierra Club, Texas ROSE and TLSC's argument that administrative costs should be set at ten percent of the program cost budget. However, the commission is adopting a separate ten percent limit on research and development costs. The commission expects that administrative costs and research and development costs may be higher than in the past, because utilities will have to rely on programs for residential and commercial customers to a greater extent than they have in the past to meet their energy efficiency goals. In addition, it is likely that building codes and appliance standards will play a bigger role in inducing consumers of electricity to improve the efficiency of their appliances, homes and other buildings. In this environment, the utilities are likely to have higher administrative and program development costs, because the remaining efficiency potential will be more difficult to reach, and innovative programs will have to be developed and implemented.

For subsection (i)(1)(B), TXU Energy proposed that the provisions relating to informational programs to improve customer awareness of energy efficiency programs and measures be limited to electric utilities outside of ERCOT. TXU Energy stated that proposed §25.181(i)(1)(B) would allow utilities to recover costs incurred by a utility in "providing informational programs to improve customer awareness of energy efficiency programs and measures." However, PURA §39.9025(a)(5) requires REPs in the ERCOT region and only the utilities outside of ERCOT to

"provide customers with energy efficiency educational materials." TXU Energy suggested that perhaps the simplest way to conform the language of the rule to the requirement of the statute would be to limit the application of §25.181(i)(l)(B) to "electric utilities outside of ERCOT." TXU Energy suggested alternatively, the rule could perhaps be clarified to avoid overlap with the REPs' statutory responsibility. TXU Energy suggested, however, that if the commission preferred to allow utilities within ERCOT to supplement the duty imposed on REPs by the statute, then the associated costs that are deemed necessary and reasonable be expressly limited to those incurred where the commission finds that the REPs cannot or have not provided the information provided by the utility within ERCOT. ARM recommended the deletion of proposed subsection (i)(1)(B) for the same reasons and noted that the proposed subsection (i)(1)(A) is sufficient to capture the appropriate subcategory of administrative costs relating to an electric utility's provision and dissemination of energy efficiency information.

Reliant argued that the subsection (i)(1)(B) requirement is an unnecessary new expense for utilities, and mass market customers do not have direct access to utility energy efficiency programs, but must go through EESPs to access the programs. Reliant stated that these entities are more suited to providing information, and as a practical mater will have to do so in order to get customers to participate in whatever programs the EESPs offer. Reliant noted that industrial customers are sophisticated enough to obtain information about the programs without the utility needing to establish a new requirement for outreach.

Commission response

The commission agrees with TXU Energy, ARM and Reliant's concerns with the confusion over providing informational efforts by utilities to customers, and agrees that subsection (i)(1)(B) should be modified to reflect that providing information to customers is an appropriate administrative cost only for utilities outside of ERCOT.

EUMMOT proposed deleting subsection (i)(1)(C), stating that this subsection does not serve to foster and promote innovation, but rather to diminish it, based on its limited access to necessary funding. EUMMOT also reasoned that the funding structure as outlined in the proposed rule runs contrary to that proposed in HB 3693 and, in effect, undercuts the intent of the legislature. EUMMOT stated since administrative and management activities, which have been deemed by the commission to be reasonable and necessary, are truly essential to the operation of the programs. In its view, the utility's ability to sponsor the research and development that the legislature envisioned would be extremely limited under the proposed rule. Good Company, ARM and CCET agreed on the deletion. Good Company recommended that R&D expenses be included in a separate category, apart from administrative costs, and capped at the legislative mandated ten percent, to be used specifically for energy efficiency R&D. In addition, these commenters stated that to include these expenses in the same budget as administrators' salaries seems likely to undermine the legislature's intent, as utility management will be tempted to pay for current overhead at the expense of developing new efficiency measures. Good Company noted that HB 3693 allows the utilities to use up to ten percent of their efficiency program budgets on R&D, and does not address the administrative budget.

ARM recommended that proposed subsection (i) be revised to employ separate "buckets" for administrative and R&D costs, rather than lump those costs together in the same "bucket." ARM argued that both of these cost categories should be individually capped. ARM recommended the existing ten percent cap on administrative costs in the current version of P.U.C. Substantive Rule §25.181(i) should remain for that category of expenses, regardless of the size of the electric utility. ARM noted that the cap on R&D costs should track the wording of PURA §39.905(e): the costs of conducting R&D activities may not exceed ten percent of the greater of: (A) the amount the commission approved for energy efficiency programs in the electric utility's most recent full rate proceeding; or (B) the commission-approved expenditures by the electric utility for energy efficiency in the previous year.

Commission response

The commission agrees with EUMMOT, Good Company, ARM, CenterPoint, and CCET's comments that research and development costs should be separated from administrative costs. The commission is modifying this provision to adopt a cap on administrative costs that reflects the separate limit on R&D costs in §39.905(e). The limits that are being adopted are ten percent for administrative costs and ten percent for R&D.

Public Citizen, Environmental Defense, SEED Coalition suggested adding to the list of administrative functions "the funding of independent verification of program results ordered by the commission."

Commission response

The commission does not agree with the proposal of Public Citizen, Environmental Defense and SEED. The commission is not committed to requiring an independent verification of the utilities' reported program results, but in connection with the granting of additional flexibility in the management of energy efficiency programs it may be reasonable to periodically conduct third-party reviews, which would be at the utilities' expense. The commission believes that it has the latitude to require such a review, whether it is specified in the rule or not.

Reliant suggested that subsection (i)(3) should permit a utility to establish funding set asides or other program rules to foster participation in energy efficiency programs by retail electric providers. Good Company largely agreed, but would include municipalities and other governmental entities as potential targets for set-asides. ARM agreed with Good Company. Reliant noted, in contrast, that the statute specifically supports the facilitation of participation by REPs, whereas there is no comparable statutory language fostering participation by municipalities and other governmental entities. Reliant suggested, as an alternative, that the commission could delete the entire paragraph because one interpretation is that the utilities have the latitude implicitly to establish such set asides for REPs pursuant to PURA §39.905(a)(4). ARM agreed with the deletion of the proposed subsection in its entirety if REPs are not included within its scope, noting that PURA §39.905(a)(4) requires an electric utility to use its "best efforts" to encourage and facilitate REP involvement in the delivery of its energy efficiency and demand response programs.

Public Citizen, *et al*., proposed the creation of a special standard offer program to allow cities and counties to do retrofit programs for homes and other buildings. This would result in more energy efficiency in hard to reach areas, including low income communities. The American Institute of Architects found that existing homes and businesses can cut fifty percent of their energy use through retrofits. It also advocated for programs for cities to retrofit their own facilities.

Commission response

The commission disagrees with Reliant, ARM and Good Company's suggested modification to subsection (i)(3) to include a "set-aside" to foster REP participation in the energy efficiency programs. The commission notes that utilities are required to use best efforts to facilitate REP involvement, and this statutory directive is repeated in subsection (r) of the rule. The commission concludes that the utilities have broad latitude concerning their best efforts, and that there is not a need for an additional provision for "set-asides" to foster REP involvement in the program. Set asides could tie up program funds and impede a utility's efforts to meet its goals, if REPs do not actively participate in the program.

The commission does not agree with Public Citizen's recommendation to create special standard offer programs to allow cities and counties to retrofit homes and other buildings. Subsection (i)(3) permits utilities to use set-asides to foster participation in energy efficiency programs by municipalities and other government entities, which gives the

utilities flexibility to adopt the programs they believe will be effective in reaching their energy efficiency goals, consistent with other program requirements.

TXU Energy proposed modifying subsection (i)(4) to require that copies of the forms, procedures, deemed savings estimates and program templates also be provided to EESPs and retail electric providers. In addition, TXU Energy sought to add a provision directing electric utilities to work collaboratively with EESPs and retail electric providers regarding any changes to these program documents. EUMMOT proposed removing the phrase "program templates." EUMMOT stated that with this change, program templates would still be included in each utility's annual Energy Efficiency Plan, but a set of commission-approved templates would no longer be maintained by the commission. EUMMOT stated that, as with any other component of a Plan, it could be reviewed by the public. It also noted that the proposed §25.181(n) would also provide a forum for public input into a template.

Commission response

The commission is adopting a provision that would direct utilities to provide relevant documents to REPs and EESPs and to work collaboratively with them when they are changing these documents, to the extent that such changes are not considered in the Energy Efficiency Implementation Project described in subsection (q). The commission does not agree with EUMMOT's proposal to remove the phrase "program template." The commission recognizes that the utilities will normally provide program templates in their annual report that is filed with the commission. The requirement under subsection (i)(4) is still appropriate, because it would address any changes in program documents during the

course of a program year and require the use of standardized forms, procedures and program templates.

§25.181(j): Standard offer programs

Good Company and ARM, in commenting on subsection (j), stated that utilities should cooperate with REPs to foster their involvement in standard offer programs.

Commission response

PURA §39.905(a)(4) states that each electric utility in ERCOT shall use its best efforts to encourage and facilitate the involvement of the region's retail electric providers in the delivery of efficiency programs, which includes standard offer programs, and this statutory directive is repeated in subsection (r) of the rule. The commission concludes that an additional reference to this obligation in subsection (j) would be redundant.

§25.181(k): Market transformation programs

TXU Energy proposed that the last sentence of subsection (k) be modified to direct the utilities to assist in the development of programs for REPs' customers, and, where possible, either leverage existing industry-recognized programs or utilize new advanced technologies that have the potential to reduce demand and/or energy consumption in Texas. They noted that REPs can offer new technology to better serve their customers and give them the products they demand. In addition, TXU Energy stated the legislature's introduction of advanced metering should add significant benefit to the Texas market and allow REPs to provide these services to their customers. TXU Energy suggested a clarification that the programs should be described as

programs that may reduce demand and/or energy consumption, since demand response is an example of a program that may reduce demand but not necessarily energy consumption. TXU suggested that these types of programs can greatly advance the overall goals of reducing demand growth, and they should not be excluded. TXU Energy stated that in order to meet the significant energy efficiency mandates established by the legislature, the statute requires the commission to establish a procedure for reviewing and evaluating market-transformation program options. TXU Energy suggested that in evaluating program options, the commission may consider the ability of a program option to reduce costs to customers through reduced demand, energy savings, and relief of congestion. TXU Energy stated that utilities should be able to choose to implement any program option approved by the commission after its evaluation in order to satisfy the goal.

TXU Energy stated that all of these program alternatives listed in the statute have potential benefits for energy efficiency, including both energy and peak demand savings. TXU Energy stated that it understands that in order for these or any other program ideas to be acceptable to the commission and utilities that providers will need to demonstrate that their proposal can measure and verify savings. TXU Energy noted one hurdle, however, will be determining how the energy savings will be measured. TXU Energy noted that REPs and EESPs should have a good understanding from the commission and the utilities what will be expected and what will be needed to demonstrate savings using these options. TXU Energy stated it is important that the accepted measurement and verification protocols be sufficiently broad and flexible to account for demand and energy savings that may be available through non-traditional programs.

Texas ROSE and TLSC commented that the phrase "compliance with existing building codes and equipment efficiency standards" in subsection (k) should be deleted. Public Citizen, Environmental Defense and SEED sought to have subsection (k) explicitly permit market transformation programs that are designed to improve compliance with, or enforcement of, newly adopted state or local building energy codes for a transition period defined by a baseline study or by specific agreement with the adopting authority or to increase participation in standard offer programs. They also urged that this subsection provide that utilities should cooperate with the REPs, consider statewide administration where appropriate and, where possible, leverage existing industry-recognized programs that have the potential to reduce demand and energy consumption in Texas. They also suggested that the subsection should incorporate the recommendation of the Summit Blue Report to measure the impact of market transformation programs over a multi-year period, with multi-year targets, and allow incentives to be evaluated over the market transformation period, rather than by single year's results. In their view, achieving the available potential demand and energy reduction will require strategic market interventions on several fronts and a degree of mutual support between public policies affecting efficiency. For this reason, they recommended the addition of specific language intended to provide flexibility for utility programs to support adoption and implementation of state and local advanced building energy codes and efficiency standards. They requested that the commission approve and encourage net zero energy buildings market transformation program options. HB 3693 specifically includes, and the proposed rule should permit such programs. They requested that the procedures established by the commission for evaluating market transformation programs consider environmental and reliability benefits as well as reduced costs to customers through reduced demand, energy savings and relief of congestion. Also, they requested the

commission to consider reviews or workshops of best practices and program ideas on an annual or biennial basis.

Commission response

The commission does not agree with TXU Energy's suggestion to modify subsection (k) to include language regarding utilities' cooperation with REPs to "utilize new advanced technologies." The commission concludes that advanced technologies and "existing industry-recognized programs" both have a role in energy efficiency, and that utilities will have appropriate latitude to select programs that give them sufficient certainty of success in achieving their savings goals and also foster innovation through advanced technologies, recognizing that not all new technologies will immediately live up to their promise. With respect to TXU Energy's comments that it may be difficult to measure and verify savings in certain, newer or unproven technologies, the utilities have some flexibility in measurement and verification of savings, but this flexibility must be exercised with a recognition that customers are paying for the programs that are adopted under this section. The measurement and verifications procedures that the utilities use must produce an honest assessment of the savings resulting from a program.

The commission does not agree with Texas ROSE and TLSC's request to delete the phrase "compliance with existing building codes and equipment efficiency standards." While new building codes and appliance standards are being adopted that will require higher energy efficiency performance, there may be difficulties in enforcing these codes and standards, and the commission believes the energy efficiency program may have a role in helping to ensure that the promise of the codes and standards is achieved.

Finally, the commission agrees with some of Public Citizen, Environmental Defense and SEED's suggested additions to subsection (k) regarding market transformation programs. The commission believes that it is reasonable to clarify in adopting this rule that market transformation programs encompassing a multi-year period are appropriate and may demonstrate cost-effectiveness over a period longer than one year, but it is not necessary to refer, in this subsection, to programs developed with REPs. An encouragement for programs involving REPs is provided in subsection (r). In addition, the commission does not agree with Public Citizen, Environmental Defense and SEED's suggestion regarding periodic review or workshop on an annual or biennial basis. The rule continues the Energy Efficiency Implementation Group that has played a role in implementing the prior version of this section, and the commission has the latitude to schedule program reviews or workshops, as needed and as resources permit.

§25.181(l): Requirements for standard offer and market transformation programs

TXU Energy perceived potential ambiguity in proposed §25.181(l)(1)(C). TXU Energy noted that this paragraph appears to be intended to prohibit a utility from tying its standard offer or market transformation program to the customer's purchase of any other product or service from the utility or the utility's competitive affiliate. TXU Energy supported this goal, which is probably already achieved through other laws, including the Code of Conduct. TXU Energy proposed that programs shall not permit the provision of any product, service, pricing benefit, or alternative terms or conditions of the utility's standard offer and market transformation programs to be conditioned upon the purchase of any other good or service from the utility or taking retail

electric service from the utility's competitive affiliate, except that only customers taking transmission and distribution services from a utility can participate in its energy efficiency programs. TXU Energy also proposed that standard offer and market transformation programs must include incentives sufficient for retail electric providers and competitive energy service providers to acquire the targeted additional cost-effective energy efficiency for residential and commercial customers.

Texas ROSE and TLSC proposed that standard offer and market transformation programs shall offer, at a minimum, ten years of benefit to the customer.

EUMMOT proposed that a utility may offer higher incentive levels for projects undertaken in areas of its service area which have traditionally been underserved by the utility's energy efficiency programs. Reliant proposed that utilities may offer higher incentive payments for programs that result in incentive payments being passed through to end-use customers.

Commission response

The commission disagrees with TXU Energy that subsection (l)(1)(C) is ambiguous and with TXU Energy's proposed clarification regarding the sufficiency of incentives. The rule that is being adopted is based on the idea that utilities have considerable discretion in adopting programs and setting incentive levels to meet their goals, and it includes the prospect of bonuses if they meet them and penalties if they do not. Providing additional rule provisions on the sufficiency of incentives is not necessary. The commission agrees,

however, that the provisions on program eligibility should be clarified, along the lines suggested by TXU Energy.

The commission does not agree with Texas ROSE and TLSC that standard offer and market transformation programs must have a minimum of ten years benefit to the customer. The commission believes that certain programs, such as an air conditioning tune-up program, which has far less than a ten-year measure life, may still be viable alternatives. Therefore, establishing one uniform minimum would not, overall, help utilities meet their statutory obligations or ensure the energy efficiency sought in this rule is achieved.

The commission concludes that EUMMOT's proposal that utilities should be permitted to offer higher incentive levels for projects undertaken in underserved areas is not necessary. The utilities' latitude with respect to incentives would permit them to use higher incentives for underserved areas, subject to the cost-effectiveness standard. The commission disagrees with Reliant that higher incentive payments should be required for programs that result in incentive payments being passed on to end-use customers. The statute requires that the "value" of the incentive be passed on to the customer, not necessarily the actual incentive payment itself. Customers will benefit more by energy efficiency programs and society will benefit more in areas such as emissions reductions if as much program value as possible goes to supporting energy efficiency measures that result in increases in customers' energy efficiency. Customers obtain value because their demand and energy consumption is reduced through the energy efficiency measures. Incentives may play a role

in inducing EESPs and customers to participate in a program, but the primary objective of these programs is to reduce demand and energy consumption, which is where programs resources should be focused.

Texas ROSE and TLSC stated that the requirements for standard offer programs have been amended to assert the importance of passing the value of incentives on to customers. Texas ROSE and TLSC commented that the proposed rule mandates that the EESP identify peak demand and energy savings, but there is no mandate for the EESPs to pass on any incentives paid by the utility. Reliant, Texas ROSE and TLSC recommended to reinforce the importance of mandating the reporting of this important program element by including in the rule a requirement that the EESP explain how the value of the incentive is being passed on to the consumer, to comply with PURA §39.905(b)(5). Texas ROSE and TLSC commented this requirement to have the EESP inform the utility of how the customer will benefit from the incentives works hand-in-hand with other provisions that they asked the commission to add to the rules to assure end-use customers benefit from the programs. Reliant urged the commission to strengthen the rule provisions that relate to the statutory requirement "ensuring the program rules encourage the value of the incentives to be passed on to the end use customer." Reliant and TXU Energy suggested amending the reporting requirements to require the utilities report to include a description of what the utility is doing to encourage the value of the incentives to be passed on to the end use customer.

Texas ROSE and TLSC recommended under subsection (l)(2)(B) that utilities may not pay incentives for a customer to switch from gas to electricity. They stated that the current rule

prohibits the payment of any incentives for a project that would switch the energy source from gas to electricity. In addition, they noted that the proposed rule would allow a switch from gas to electricity in connection with the installation of high efficiency combined heating and air conditioning systems, which they opposed for a number of reasons. First, the exception allows gas end-use equipment to be replaced by equipment that operates using electricity. They stated that under PURA §39.905(a) the programs offered should allow each customer to reduce energy consumption, peak demand or energy costs, and that allowing gas end-use equipment to be replaced with electric equipment violates the statute by increasing electricity use. Moreover, they commented that allowing a switch from gas to electric is a violation of the purpose of PURA §39.905, which requires the commission to establish a procedure for reviewing and evaluating program options, and that utilities may choose to implement any program option approved by the commission after its evaluation. Texas ROSE and TLSC concluded that a program paying incentives for the customer to switch from gas to electric when installing high efficiency combined heating and air conditioning systems has not been reviewed, evaluated and approved by the commission. CenterPoint proposed that subsection (1)(3) be rewritten to state a market transformation program shall be neutral with respect to fuel.

Cities proposed modifying subsection (l)(2)(C) to require that all projects result in a reduction in purchased energy consumption, or peak demand, and a reduction in energy costs for the end-use customer. TXU Energy proposed that EESPs be required to identify peak demand and/or energy savings for each project in the proposals they submit to the utility.

EUMMOT proposed removing "not to exceed five years" from the market transformation design requirements. EUMMOT stated that §25.181(1)(4) appears to be designed to limit the life of a market transformation program to five years. EUMMOT noted the period of time that may be required in order to transform a market may be longer for certain markets. EUMMOT stated for example, the United States Environmental Protection Agency keeps raising the bar on the Energy Star New Homes program in order to promote higher levels of energy efficiency as the housing market changes and building construction practices improve. EUMMOT noted that there will always be opportunities to build more energy efficient homes, and this same program could be used in future years to promote "zero energy homes," green building, or a variety of other more-ambitious efficiency goals. EUMMOT suggested for these reasons deleting the phrase "not to exceed five years."

SEED Coalition proposed creation of a market transformation program for net zero energy homes, citing the actions of the American Institute of Architects, the U.S. Conference of Mayors and the National League of Cities in adopting a goal of having all new homes be net zero energy capable by 2030, and noting that the City of Austin plans to meet this goal by 2015. Public Citizen concluded that houses would become so efficient that their energy needs could be met with onsite renewable generation. In order to meet the net zero energy homes goal statewide, incentives should be made available to develop new energy efficiency and onsite renewable technologies, which would assure that the necessary equipment, personnel and distribution networks are in place. OPC asserted that a core set of energy efficiency programs should be required and include at the very least a residential customer energy rebate. OPC cited Austin Energy as a positive example of a successful energy rebate program, especially rebates for the

replacement of customers' appliances with more efficient appliances, as one of the most reasonable approaches to meeting energy efficiency goals.

Commission response

The commission does not agree with Reliant, Texas ROSE and TLSC's comments that the rule should require EESPs to report the extent to which they pass on any incentives paid by the utility to customers. The commission notes that the statute requires that the commission provide oversight to encourage that the value of incentives be passed on to the end-use customer, and the rule is consistent with the statute. The standard offer programs are competitive programs that are implemented through the activities of EESPs and REPs, and these entities are subject to minimal regulation by the commission. Additional reporting requirements would be inconsistent with this competitive approach. Such reporting might also require the disclosure of important, competitively-sensitive elements of the business relationship between an EESP and its customers that would make EESPs less willing to participate in the programs under this section, resulting in fewer options for customers and potential damage to the program. Finally, as is noted above, the commission concludes that resources are better employed in increasing customers' energy efficiency, and that it does not make sense to redirect program resources to providing incentives to customers.

The commission also disagrees with OPC, Texas ROSE and TLSC's suggestion to modify subsection (l)(2)(B) so that utilities may not pay incentives for a customer to switch from gas to electric end uses. The statute does not prohibit this practice, and the commission

believes that the rule should permit utilities to use whatever methods that can be quantified and verified in order to meet their energy efficiency goals. Efficient electric heating may be particularly appropriate, environmentally-beneficial measure in areas that do not meet or are on the verge of not meeting national air-quality standards for ozone.

The commission disagrees with Cities' proposed modification of subsection (l)(2)(C) to require that customers have a choice of and access to projects resulting in a reduction of energy consumption, peak demand "and" energy costs. PURA §39.905(a)(2) clearly states that customers should have access to and a choice of projects that result in reduced energy consumption, peak demand "or" energy costs, and both demand and energy savings have a value.

The commission disagrees with CenterPoint's suggestion that market transformation programs be neutral with respect to fuel, noting that the statute only requires that standard offer programs be fuel-neutral. There may be market transformation programs that could be offered that would not meet this criterion, and the commission concludes that it is preferable not to preclude the adoption of such a program without considering the specifics of the program. The commission agrees with EUMMOT's proposal to remove "not to exceed five years" from the market transformation design requirements, for the reasons expressed in its comments.

The commission does not agree with the SEED Coalition's proposal to create a market transformation program for net zero energy homes. The commission does not disagree

that net zero energy homes may be an important resource, however. In particular, PURA §39.905(d)(10) states that net zero energy homes may constitute an option for utilities in achieving their goal under subsection (a). The goals that other entities have adopted for zero energy homes, as described in the SEED comments, are long-term goals, while the utility programs under this section are expected to yield results in the near term. The commission concludes that this topic merits further discussion outside of the context of this rulemaking proceeding, to determine how it may fit into the utility programs under this section. The commission has a separate proceeding under way related to interconnection standards for small generation units and net metering. Modifications of rules in these areas will be important in developing a net zero energy home program, and the commission concludes that the rules related to interconnection and net metering should be adopted before the commission takes any further action with respect to a net zero energy home program.

The commission disagrees with OPC that a core set of programs should be required. The utilities have successfully implemented the statute, using a model in which they and EESPs have considerable latitude to develop programs in order to achieve the program goals. The utilities and EESPs have a responsibility for program selection, and the commission does not believe that, with its limited resources, it can do a better job. The Austin Energy rebate program that OPC discussed involves direct utility contacts with customers, something that is inconsistent with the standard offer concept and the role of utilities under the statute and this rule. In connection with the TXU Energy suggestion that EESP should be required to provide information on the expected savings for each program, the commission concludes

that such a requirement is not necessary for this rule. The utilities have the incentive to operate their programs to cost-effectively achieve the goals of the energy efficiency program, and they can require EESP to provide the information they need to select the EESPs that will best contribute to doing so.

Reliant expressed the view that there is a significant problem with the standard offer programs being granted on a first-come, first-served basis, namely, that EESPs offering low value programs who simply are more experienced with the process of securing funds may squeeze out other projects that may have greater merit. Reliant believed this problem should be tackled head on, and the best way is to require that utilities conduct competitive auctions. Reliant proposed specifically, that utilities be required to conduct a reverse auction for each standard offer program. Reliant suggested that such auctions could be implemented without great expense by the utilities, and that the benefits to the continued development of the energy efficiency market would outweigh the costs of developing an auction process. Reliant stated in a reverse auction, for a specified amount of demand savings, potential providers would bid to provide the savings at the lowest price. Reliant stated the utility would then select the lowest priced bids, moving up the stack until the auction goal is reached. Texas ROSE and TLSC also expressed the view that the rule would be improved by requiring competitive solicitations for market transformation programs. Sierra Club and Public Citizen, Environmental Defense and SEED also supported the use of a competitive solicitation process. Texas ROSE and TLSC recommended a competitive solicitation process in which every TDU issued an RFP once a year to ask for proposals for market transformation programs.

Commission response

The commission does not agree with Reliant's suggestion to require that utilities conduct a reverse auction for each standard offer program or with Sierra Club, Public Citizen, Environmental Defense, SEED, Texas ROSE, and TLSC's recommendation for a competitive solicitation process for market transformation programs. The commission believes that the proposed auction is inconsistent with the standard offer concept. While such an approach could be used for market transformation programs, the commission believes that such a significant change in the selection process should not be adopted without an opportunity for full comment on it by all of the parties. That opportunity did not arise in this rulemaking proceeding. In addition, one of the other goals of the energy efficiency program is to develop a network of companies that have expertise in energy efficiency and can provide assistance to customers who wish to improve the efficiency of their homes and businesses, regardless of the availability of programs under this section. The commission is not convinced that an auction process would contribute to the development of a strong EESP community throughout the state. Accordingly, the commission does not adopt the recommendation of these parties for a competitive selection process.

CenterPoint, Texas ROSE and TLSC urged deleting combined heat and power technologies as an allowable measure under subsection (l)(1)(E). CenterPoint stated that this paragraph of the proposed rule would include renewable DSM and combined heat and power technologies (CHP) as potential elements of standard offer and market transformation programs. CenterPoint noted that the inclusion of combined heat and power technologies (or, in other words, cogeneration) is

contrary to the purpose of the rule and the underlying legislation, which is to reduce the growth in electric demand and thereby reduce the need for additional generation. CenterPoint stated that regardless of whether CHP has benefits or needs to be encouraged, it is inappropriate for electric utilities to provide incentives and promote one form of electric power generation over others given the electric utilities' role in the competitive market.

Texas ROSE and TLSC stated that the current rule is correct in prohibiting incentives for power production technologies. Texas ROSE and TLSC commented that under the current rule, CHP would be ineligible to receive incentives because it produces power. Texas ROSE and TLSC recommended a requirement for all technologies to be reviewed by the commission prior to implementation by the utilities. Texas ROSE and TLSC expressed concern that despite the fact that the commission has conducted no evaluation or study of CHP technology, the proposed §25.181(l)(1)(E) allows utilities to permit the use of CHP technologies in the program. Texas ROSE and TLSC stated that allowing CHP would violate PURA, and this provision should be deleted from the proposed rule.

Good Company also opposed allowing CHP technologies to be included as measures in standard offer and market transformation programs. Good Company noted that this section does not comply with PURA §39.912, which requires that the commission study CHP to determine "how combined heating and power technology can be implemented in this state to meet energy efficiency goals." Good Company believed it would be premature to include CHP in efficiency programs before CHP technology is further delineated by the commission, or the commission determines the means with which CHP can be implemented to meet program goals. EUMMOT

expressed the view that CHP projects are not end-use energy efficiency, and CHP projects should not be permitted to receive energy efficiency incentives at all. EUMMOT proposed that CHP projects should either not be considered eligible or should have constraints placed on their eligibility, such as prohibiting them from making exports to the utility grid, a ten-megawatt size limit, or other restrictions.

EUMMOT noted that the commission's present energy efficiency rules do not promote CHP, unless a renewable energy source is involved. EUMMOT stated cogeneration really is not a "demand side" energy efficiency measure and might best be promoted through other programs or policies of the commission. EUMMOT stated that the promotion of CHP through energy efficiency programs also places the non-ERCOT bundled or vertically integrated utilities in an uncomfortable position of potentially subsidizing generation projects against which the utility might compete in wholesale generation markets. EUMMOT commented that their bigger concerns are practical ones. CHP projects can be enormous in size (*e.g.*, the facilities owned and operated by Oxy and Dow in ERCOT) and could take significant program incentive funds away from other demand-side efficiency projects. EUMMOT acknowledged that they understand that the proponents of this language are really hoping to promote medium-scale CHP projects in commercial and institutional facilities, but the lack of any constraints in the rule could open the door for large industrial-scale CHP projects as well.

ClimateMaster felt that the revised efficiency rule language, which provides that energy efficiency programs shall be neutral with respect to specific technologies, equipment or fuels, is appropriate and provides the necessary clarification that will remove what was a barrier to the

widespread acceptance of this highly important technology. ClimateMaster noted that by clearly stating that utilities may not pay incentives for a customer to switch from gas appliances to electric appliances except in connection with the installation of high-efficiency combined heating and air conditioning systems, the commission would ensure that informed consumers are not precluded from participating in efficiency programs. ClimateMaster stated that this revised language opens the door to an unrestricted analysis of all available technologies to maximum energy savings, regardless of the type of fuel used.

TXCHPI recommended, under §25.181(l)(1)(E), that the placement of the two types of technologies that appear in the sentence should be transposed so that "combined heat and power technologies" precedes "renewable DSM technologies." TXCHPI noted that Texas leads the United States in CHP applications; nearly one quarter (twenty-three percent) of all CHP generation capacity in 2005 was located in Texas. TXCHPI said that CHP technologies generate electrical and thermal energy in a single, integrated system close to the point of customer energy demand. TXCHPI stated that CHP technologies and systems are well understood, and have been in use since the first days of U.S. commercial power production. TXCHPI stated that heat is a by-product of electric generation and is typically wasted; in fact, cooling towers and ponds lower the efficiency and increase costs at most large power plants in the U.S. Cooling towers and ponds are required to dispose of "waste" heat, which is not useable because the large power plants are located far from customers. TXCHPI stated that energy consumers use boilers and other devices to make heat (hot water and steam) when and where they need it, with natural gas the most common fuel choice in Texas. TXCHPI stated the most obvious benefit of a CHP system is its efficient use of the energy released when the fuel is burned, and the average thermal efficiency

of a typical simple cycle power plant is about thirty-three percent, while combined cycle combustion turbines achieve efficiencies of fifty-five percent. TXCHPI noted the capture and use of waste heat allows CHP systems to achieve efficiencies of sixty percent to ninety percent, and capturing waste heat requires a capital investment that is returned in energy cost savings over several years.

TXCHPI noted over seventy-five percent of the CHP capacity in Texas is in industrial applications of 100 megawatts or greater, that is, in utility scale industrial applications. According to a study conducted by the Gulf Coast CHP Application Center, there is an additional 7,400 megawatts of potential in industrial settings and 6,200 megawatts of potential in commercial and institutional settings (hotels, hospitals, colleges, schools, office buildings, prisons, nursing homes). TXCHPI stated that seventy-five percent of the potential is in applications of 20 megawatts of less, divided more or less evenly in three blocks among applications of less than one megawatt, one to five megawatts, and five to twenty megawatts. TXCHPI believed that CHP applications that range in size from 100 kilowatts up to a few megawatts can help satisfy the energy efficiency goal in Texas. TXCHPI stated that energy efficiency incentive payments may have a significant impact on the decision of the customer to implement CHP, particularly for the smaller systems, where incentive payments could offset large capital investments. UTC Power agreed that the proposed rule properly included CHP as an eligible technology in the standard offer and market transformation programs.

Commission response

The parties that oppose including CHP as an eligible measure have not made a convincing case that the technology is either impermissible under the statute or is inconsistent with its purposes. The comments of the proponents have provided an accurate description of the benefits of CHP. These comments demonstrate that CHP provides a significant energy efficiency opportunity that, outside of large-scale industrial applications, is not being harnessed today. The commission concludes that CHP should be a permissible technology under the rule, with appropriate limits. The commission disagrees with Good Company that the proposed rule does not comply with PURA §39.912, which requires that a CHP study be performed in order to determine how best it can be implemented. The fact that a study is required of CHP does not preclude the commission from initiating a program that is otherwise consistent with the statute.

The commission agrees with EUMMOT's suggestion that eligible CHP projects should be limited to those that are ten megawatts or less in size. The commission has repeatedly noted that this rule provides utilities broad latitude in the selection of programs, so that a utility could decide that a program that was open to CHP would not help it achieve its energy efficiency goals, based on the circumstances in its service area. The commission believes that utilities' discretion with respect to program selection should reflect factors that relate to the likelihood of achieving savings, the ability of a sponsor to provide verifiable savings, and the cost-effectiveness of a project, however. CHP should not be arbitrarily rejected by utilities. The commission concludes that the other limitations that EUMMOT recommended are not necessary, and that the size limit, together with other

program restrictions will likely exclude CHP projects that would otherwise be problematic. The fact that industrial customers' role in the energy efficiency program is more limited than in the past will also help avoid projects that are primarily for energy export, rather than meeting a customers' energy needs. Finally, the rule requires that utilities' energy efficiency programs serve all classes of customers. This requirement and the budget limits that the legislature has established for 2008 and 2009 will necessarily limit the amount that utilities will have available to provide incentives for CHP and prevent the incentives for CHP from foreclosing other beneficial energy efficiency programs.

The commission disagrees with TXCHPI's suggestion to transpose "combined heat and power technologies" with "renewable DSM technologies." The order in which technologies are listed in a provision of the rule does not imply a preference for one over another.

Texas ROSE and TLSC proposed that incentive payments could vary by customer class, but not within a customer class. The proposed language permits utilities to practice discrimination in the payment of incentives, and, in their view, the explicit non-discrimination provisions in the current rule should be retained. The programs are funded equally by all customers in the residential and commercial classes, and the incentives that are paid should also be paid to all participating customers equally.

Texas ROSE and TLSC recommended under subsection (l)(5) that the programs operated by the TDUs be completely separate from the programs operated by ERCOT to assure that both the TDU and ERCOT have a sufficient amount of available load for curtailment when necessary.

Texas ROSE and TLSC noted that the ERCOT load resource programs are operating in a competitive wholesale market environment where values are assigned to loads acting as a resource, and these are market driven programs that should remain market driven and should not be eligible for energy efficiency incentives. Texas ROSE and TLSC concluded that PURA has no provision to support the co-mingling of load curtailment resources and the rule should be written to assure that there are two separate pools of resources available for two different levels of system emergency. They also recommended that the rule be improved by clarifying how TDU and ERCOT load control systems should work together to provide a higher level of system reliability.

Good Company noted that §25.181(1)(5) prohibited EESPs from receiving incentives under the utility program for the same demand reduction it is compensated for under an independent system operator (ISO) program. Good Company shared the commission's concern for "double-dipping," and noted that this more appropriately applies to industrial load management programs where a former participant in interruptible rate programs is forced to choose between selling the exact same demand reduction in either a load management program or the Emergency Interruptible Load Service (EILS) program, but not both. Good Company stated that this issue requires closer examination in the context of residential and commercial demand response, however, because a program may be encouraging investment in the capability to provide demand response. Good Company noted in that case, it would be counterproductive to prohibit the employment of this capability to provide services to ERCOT, requiring ERCOT to purchase additional resources. Good Company stated that Occidental Chemical argued in the Protocol Revision Subcommittee that participants in EILS should be able to also participate in arbitrage

(passive demand response) and activities to avoid transmission charges by reducing demand during periods when a peak is expected to be set during the four months that are critical in establishing ERCOT transmission charges. Good Company believed that there may be a benefit to permitting an EILS participant to also provide local reliability services to a TDU, as is currently the case in New York City, or to similarly engage in "passive demand response." Good Company stated the focus should be on cost effectiveness, not a buzz word like "double dipping." Good Company suggested if we are going to encourage demand response, we want to ensure market participants receive maximum value from this resource.

Commission response

The commission does not agree with Texas ROSE and TLSC's comments regarding discrimination. There may be valid reasons to provide higher incentives to one set of customers in a class than to other customers in the same class. The prior rule permitted higher incentives in areas that had either special environmental circumstances or that were transmission constrained. One of the concerns that is reflected in the proposed rule was that there may be a need to provide higher incentives in areas that have historically been underserved. The rule that is being adopted includes a requirement that utilities report underserved areas, and the commission may in the future decide that action to remedy geographic inequities is appropriate. In any event, the commission concludes that the specific non-discrimination provisions in the prior rule may be inconsistent with legitimate program objectives, and it is not adopting them in this rule. Just as distinct groups like the hard-to-reach customers may require a higher incentive, higher incentives may be required to reach customers in small towns, if there are fewer companies in small towns that have

the energy expertise to serve as EESPs and take advantage of the benefits of this rule. There may be other reasons that are not anticipated now why it would be reasonable to establish different incentives based on other appropriate criteria. The purpose of the change in the rule is not to promote discrimination but, rather, to facilitate cost-effective programs that will help the utilities reach their goals and reduce the disparities in participation that may have occurred under the current rule. If there are customers in small towns and rural areas that have not been able to benefit from the program, they have been paying for the program without directly benefiting from it.

The commission does not agree with Texas ROSE and TLSC's argument that the programs operated by utilities be completely separated from programs operated by an ISO or that the rule should clarify how utility and ISO programs separately contribute to system reliability. Subsection (l)(5) states that a load-control standard offer program shall not permit an EESP to receive incentives from both a utility program and a program conducted by an ISO for the same demand reduction. To the extent that a demand response measure provides demand reduction capability in a utility program and a program operated by an ISO in different periods, for example, there is no reason why the measure should not be able to receive incentives from both a utility and an ISO. There may be other instances in which a measure can provide distinct value in the utility and ISO programs, without getting paid twice for the same savings. The burden should be on the utility to determine whether there is a benefit from a utility program that is consistent with system adequacy and reliability objectives and does not provide double payment for the same system benefit.

The commission does not entirely agree with Good Company's comments on this issue either. The rule would prohibit an EESP from receiving an incentive for the same reduction in a consumer's demand for which it is receiving a payment from an ISO. The commission is concerned about the integrity of the program, both from an operational and payment perspective. If an EESP commits to provide two megawatts of demand reduction in an ISO program and a utility program, there is a risk that the ISO and the utility will expect a total of four megawatts of response. Both need to know exactly what level of minimum response they can expect to meet the objectives of the two programs. By the same token, as a utility and the commission are evaluating the cost effectiveness of the utility and ISO demand response programs, they need to be able to rely on the fact that the amount paid in each program represents a unique demand resource. Some of the examples provided by Good Company do not explain clearly how a resource that is providing demand response to ERCOT and a utility would be distinct. For example, a service that provides load reduction for ERCOT emergencies and local utility transmission system emergencies could be called on by both ERCOT and the utility for the same event, unless the program rules very clearly differentiate these emergency conditions. The rule that is being adopted will permit payments under a utility demand response program only if it is clear that a participant would not be paid twice for the same response.

§25.181(m): Energy efficiency plans and reports

Reliant proposed specifying that the proposed annual budget submitted in the plan and report would be subject to the budget limitations in subsection (f)(8) to provide clarity and consistency regarding submission of proposed budgets.

Good Company proposed specifying that the plan and report would include supporting documentation for the utility's total actual and weather-adjusted peak demand and actual and weather-adjusted peak demand and energy consumption for residential and commercial customers for the previous five years. Good Company expressed concern that without documentation and assurance that utilities are employing similar methods to calculate peak demand, it is conceivable that a utility might under-report peak demand and under-value annual demand growth, reducing required expenditures on efficiency programs and undermining the intent of the efficiency goal. Good Company recommended adding a section that requires information on utility administrative and R&D expenditures and allocations. Good Company believed a new section was needed because "historically, utilities have not been required to report on how administrative funds and R&D are expended."

Texas ROSE and TLSC recommended that information be provided in advance of filings to allow all parties, including the commission staff, to schedule processes for review and approval. Texas ROSE and TLSC suggested that the information include a brief explanation of programs, deemed savings updates and other filings the utility plans to make that will require review, evaluation, and approval by the commission.

Reliant proposed that the plans should include a discussion of how the utility is encouraging and facilitating retail electric providers to deliver energy efficiency and demand response programs. ARM and TXU Energy also proposed modifications regarding reporting of best efforts used to facilitate the involvement of the region's retail electric providers in the delivery of efficiency

programs and demand response program. TXU Energy proposed a requirement that the utilities describe their efforts, as absent such a regulatory requirement, the somewhat nebulous requirement of "best efforts" to encourage and facilitate the involvement of the region's retail electric providers in the delivery of efficiency programs and demand response program could become meaningless. TXU Energy stated that a description of the utilities' efforts would be a tool that helps the commission, the legislature, and other interested parties assess whether the goal of the statute is being achieved.

Cities proposed that the expenditures for the prior five years include the performance bonuses and other costs, along with total retail customer savings by program and customer class.

CenterPoint recommended deleting subsection (m)(1)(T) and stated that there is no standard that can be applied and no realistic way to determine whether a county is "under-served" by an electric utility's energy efficiency programs, and therefore there is no reason to include a metric that can not be objectively measured in the energy efficiency reports submitted to the commission. CenterPoint argued that the utility's energy efficiency programs are as much a function of the attitudes of the end-use customers in that area as it is a function of the promotional efforts of the electric utility and the energy service providers.

TXU Energy proposed addition of the requirement for identification of all specific actions that were undertaken by the utility to deploy net metering and advanced metering information networks as rapidly as possible. TXU Energy stated that the reporting requirement should be a tool that helps the commission, the legislature, and other interested parties assess whether the goal of the statute is being achieved. TXU Energy proposed that utilities be required to provide a

description of incentives for REPs and competitive energy service providers to acquire additional cost-effective energy efficiency for residential and commercial customers sufficient to achieve the annual energy efficiency targets.

The Sierra Club believed that the commission should require that utilities look more broadly at the gains they could make through energy efficiency programs by January 15, 2009. The Sierra Club was supportive of language submitted by Public Citizen, Environmental Defense and SEED that would require additional reporting of utilities, as well as better coordination between the reporting required by the commission, the State Energy Conservation Office (SECO), and ERCOT; provide information related to the commission's report to the legislature that is due by January 15, 2009; require the commission to report energy savings from the utility programs to ERCOT; and require the commission to develop reporting formats. Public Citizen, Environmental Defense and SEED asked the utilities to examine the full energy efficiency potential for their service areas, instead of limiting it to fifty percent. Public Citizen, Environmental Defense and SEED stated that the American Council for an Energy-Efficient Economy (ACEEE) recently found that Dallas could meet 101% and Houston could meet seventy-six percent of projected load growth through energy efficiency, combined heat and power and onsite renewable energy generation by 2023, saving twenty-four percent of their demand.

Public Citizen, Environmental Defense and SEED Coalition stated that utilities should be required to analyze the potential for combined heat and power in hospitals, universities, industrial, commercial and other facilities. They noted that the data from utility analyses should

be reported to the commission for use in tracking the progress of the projects and, in turn, the commission should report it to ERCOT for use in determining load growth projections. These parties recommended that the commission specify the format for reporting data to SECO and require incorporation of data from the reports made to SECO by municipal utilities, cooperatives and other governmental bodies into the ERCOT long-term demand forecast. They noted that this will ensure that the energy efficiency gains and projected energy savings made by these entities are included in calculations of long-term energy needs for the state.

Public Citizen, Environmental Defense and SEED urged that in order to ensure accurate and complete information about all potential sources of energy for Texas, the commission should require ERCOT to include the findings of SECO's ongoing renewable energy potential study in its long-term demand forecast. SEED Coalition stated taking these actions to strengthen energy efficiency implementation would help protect the health of Texans and our economy, while spurring the development of a new generation of efficiency products.

Commission response

The commission does not agree with Reliant's suggestions regarding consistency of the proposed budgets with other provisions of the rule. The commission concludes that consistency with other provisions of the rule is required without this change.

The commission agrees with Good Company's proposal to require that the plan and report include supporting documentation regarding the utilities' calculations showing demand growth. The rule the commission is adopting includes this modification to the reporting

requirements. The commission does not agree with Good Company's comments regarding research and development, and administrative cost reporting. The commission notes that proposed subsection (m)(1)(I), which is subsection (m)(2)(I) in the rule that is being adopted, requires the utilities' proposed annual budgets to detail administrative costs, including specific items for research.

The commission does not agree with Texas ROSE and TLSC's suggestions to require utilities to provide information about programs for other parties, and Staff, to review prior to filing the report required in this subsection. Under the rule, the utilities must report the results of these programs to the commission on or before April 1 of each year. This requirement should be sufficient to permit the programs to be reviewed and evaluated, and it would be difficult for utilities to report the prior year's and the next year's programs any earlier.

Reliant, ARM, and TXU Energy made similar suggestions that would require utilities to report on efforts to facilitate REPs' inclusion in the "delivery of programs." The commission concludes that it is reasonable to have the utilities include such information in their annual reports, and modifies the rule to include such a requirement.

The commission agrees with Cities that performance bonuses should be included in the annual reports, and that customer savings should be reported by program and customer class.

The commission does not agree with CenterPoint's suggestion to delete subparagraph (T). While the commission does not disagree that there is no standard for determining whether a county is "under-served," the commission believes that it is appropriate to require utilities to report information that will permit the commission to assess whether areas are "under-served." These reports should help the commission consider whether it should develop a standard for determining under-served areas in future revisions of the program.

The commission disagrees with TXU Energy that information relating to net metering and advanced metering networks should be included in subsection (m). The commission has adopted separate proceedings to deal with net metering and advanced metering, and reporting requirements on those topics can be addressed in those proceedings.

The commission does not agree with the Sierra Club, Public Citizen, Environmental Defense and SEED's proposed inclusion of reports of various data, calculations and assessments in the utilities' April 1, 2008 report, to support the commission's report to legislature in January 2009. PURA §39.905(b-2) requires the commission to make this report to the legislature, and the commission has issued a request for proposals (RFP) for an expert in this field to assist the commission in preparing the report. For this reason, the inclusion of information related to the report in the utilities' reporting requirements is not necessary. In addition, some of the assessments proposed by the commenters would not be possible for the utilities to produce by April 1, 2008. The commission does not agree with Public Citizen, Environmental Defense and SEED's request to utilities to examine the full energy efficiency potential for their service areas and not limit the potential to fifty percent.

As is noted above, the commission is issuing an RFP to hire an expert to prepare a report for the commission, and the utilities need not provide the information requested by these parties. In addition, the analyses for potential for CHP, and format for reporting data to SECO, are being handled by other means at the commission. With regard to the SECO report on renewal energy potential, the commission concludes that its activities in connection with the determination of competitive renewable energy zones represent an effort to incorporate a significant level of additional renewable energy in the state, consistent with recent amendments of PURA. To the extent that the SECO report is a useful policy guide, the commission will consider it when it is issued.

§25.181(n)

Regarding the review of programs under proposed subsection (n), Cities proposed in any event at least one such review shall be conducted every three years.

EUMMOT expressed concern that an interested person could initiate a review of a utility's programs based on "the failure of the utility to implement a program, as this language might lead product vendors or salesmen to initiate costly and burdensome regulatory reviews in hopes of persuading the commission to order a utility to start a new program for the purpose of promoting some specific technology or product." EUMMOT suggested that the EEIP, described in §25.181(q), be used as the forum to discuss new programs and the language referring to "the failure of the utility to implement a program" be removed from §25.181(n). EUMMOT stated that the responsibilities of the EEIP already encompass the development of new programs, so there is no need for the reviews described in §25.181(n) to include such activities.

CenterPoint strongly urged deletion of subsection (n) or at the very least limiting the review of an electric utility's programs to the commission's staff. CenterPoint noted a provision that invites "an interested person" to seek a review of an existing energy efficiency program or a proposed new program, or complain that an electric utility has not implemented a specific energy efficiency program that the "interested person" wants is an open door to mischief. CenterPoint stated that even if the proposed review process does not devolve into contested case proceedings, this subsection would impose costs on the utility and the commission's staff, and inject uncertainty into an electric utility's overall energy efficiency program. CenterPoint stated moreover, that the higher goals for energy efficiency are the responsibility of electric utilities, not "interested persons," and the electric utilities should have the flexibility to achieve those goals subject to commission oversight and without being subject to reviews by interested persons that may have another agenda. CenterPoint concluded because an electric utility's programs will undoubtedly be subject to review under subsection (f) of the rule either in setting the EECRF or in a periodic reconciliation of the EECRF, there is no reason to allow "interested persons" to initiate yet another review of those programs through this proposed subsection (n).

Texas ROSE and TLSC proposed modifying the subsection to require that, when a utility's energy efficiency program includes an EECRF or a performance bonus, the program be reviewed by the commission and interested parties be provided with the opportunity for a public hearing to assure that the programs and costs are just and reasonable and in the public interest. Texas ROSE and TLSC stated that the increase in a utility's minimum energy efficiency goal under HB 3693 should mean bigger and better programs that will save consumers money and reduce

emissions and the need to build more power plants. The amendments will also result in utility cost recovery outside of a rate case and performance incentives for utilities that exceed the goals. Texas ROSE and TLSC argued that any energy efficiency plan that includes a cost recovery factor or performance incentive should be subject to a review by all parties and approved by the commission. Texas ROSE and TLSC disputed language in the proposed rule that would allow planned activities to be carried out during a review, and that would permit a utility to move forward with planned programs even if a party makes a request for a formal review.

Commission response

The commission does not agree with Cities' suggestion to specify a review of each utility's programs once every three years. The commission believes that utility rate cases or periodic reviews initiated by the staff will afford adequate opportunity for the review of utility programs, and that specifying a time limit for the interval between reviews is not necessary.

The commission agrees with EUMMOT and CenterPoint's proposal to limit those who may initiate a formal review of a utility's programs to commission staff. In addition, the EEIP process provides an opportunity for informal public review of aspects of the utility programs. The commission believes that the proposed rule would have granted virtually any person the right, without adequate justification, to petition for review of any program. The commission believes that this could unnecessarily delay the program and increase costs.

Furthermore, the commission does not agree with Texas ROSE and TLSC's comments that any and all energy efficiency plans should be subject to review and approved by the commission. The commission believes that the utilities must be given flexibility to determine which programs will best ensure that they meet their energy efficiency goals and notes that information regarding the utilities' performance is publicly-available and open to scrutiny by any interested person. While the energy efficiency program has been successful in the past, the higher goals enacted as a part of HB 3693 suggest the need for increased flexibility, so that utilities can implement new programs and terminate programs that are out of date, without burdensome and time-consuming prior regulatory reviews.

§25.181(o): Inspection, Measurement and Verification

TXU Energy argued that the accepted measurement and verification protocols be sufficiently broad and flexible to account for demand and energy savings that may be available through non-traditional programs. TXU Energy suggested, for example, utilizing new advanced metering technology and measurement capabilities, programs that depend on customer behavior can be proven through statistical means to deliver demonstrated peak demand and/or energy savings.

Reliant proposed that an ESCO be permitted to either obtain a signed contract, or use other means that are acceptable to the utility to demonstrate that the measures have been installed prior to final payment being made to the energy efficiency service provider. Reliant envisioned situations where having to go to the customer for a wet signature to comply with this provision would be impractical and unnecessary. Reliant stated, for example, that if a REP offered a direct load-control pilot program, site inspections for a sample of the sites would be adequate to verify the equipment installation if the equipment is installed outside of the home, but it wouldn't be

necessary or practical to obtain a signature from each customer. Reliant concluded that development of a robust market for Smart Energy solutions will provide additional proof that properly structured competitive markets are the best way to deliver value to retail electric customers.

Cities proposed that a utility should not receive performance bonuses or cost recovery for incentive payments for any energy efficiency program until such programs are inspected and related savings are measured and verified. Cities proposed modifying the requirement under §25.181(o)(1) that the EESP would be responsible for the measurement of energy and peak demand savings to include that "the utility is responsible for verifying the reasonableness of the measured savings." Cities proposed modifying the requirement under §25.181(o)(2) that deemed savings may be used in lieu of the energy efficiency service provider's measurement and verification "only in such instances where it is not cost-effective or feasible to measure and verify savings through standard measures."

Commission response

The commission does not agree with Cities' suggested specific modification to ensure that a utility not receive performance bonuses or incentive payments until the programs are inspected and savings are measured and verified. The rule that is being adopted provides, "An energy efficiency service provider shall not receive final compensation until it establishes that the work is complete and measurement and verification in accordance with the protocol verifies that the savings will be achieved." The commission concludes that this provision requires sufficient verification of energy savings prior to affording the utilities cost recovery. The commission has adequate means to review the utilities' programs and

take action if a utility reports savings that have not been achieved or adequately verified. The commission does not agree that deemed savings should be used only when it is not cost-effective to use standard measurement and verification procedures. One of the reasons for using deemed savings is that they are more cost-effective for use in situations in which the same measures are being installed at numerous locations, such as in residential retrofit situations. There may be other circumstances in which the development and use of deemed savings may be appropriate, and the commission does not believe that it is appropriate to foreclose this possibility in the rule.

As is noted above, the commission concludes that non-traditional programs that depend on technology coupled with customer behavior have a place in the energy efficiency program. Accordingly, the measurement and verification procedures need to be able to assess the validity of savings reported by such non-traditional programs. The commission concludes, however, that the rule as proposed is sufficiently broad that it would address such programs and that a specific reference to non-traditional programs is not necessary.

The commission agrees with Reliant's recommendation that the commission should allow "other means" to obtain customer approval for particular projects prior to final payment being made to any ESCO. The commission believes that no such project or measure can be performed without a customer's direct and express agreement to participate, however.

§25.181(p): Weatherization program

Texas ROSE and TLSC recommended that this subsection be renamed "targeted energy efficiency" to distinguish it from other weatherization programs that are not coordinated with the federally funded program.

Commission response

The commission agrees with Texas ROSE and TLSC's recommendation to modify the title of subsection (q) to include the phrase "targeted energy efficiency."

§25.181(q): Energy Efficiency Implementation Project - EEIP

Cities, TXU Energy, OPC, EUMMOT, Texas ROSE and (TLSC), and EPE agreed with the concept of an EEIP. OPC agreed that a commission review process would be needed to review programs, but the Cities were not supportive of any limited review of energy efficiency programs. Cities contended that it is good for the public to have a voice, and the commission should never forget that they are paying for the program. Cities, Texas ROSE and TLSC, and TXU Energy proposed modifying this subsection to be mandatory rather than permissive. Cities recommended inclusion of "savings and measurement and verification methods" within the scope of the EEIP.

EUMMOT proposed that the process described in §25.181(q) be the forum to discuss proposed new programs, which would allow the language relating to the failure of the utility to implement a program to be removed from §25.181(n).

TXU Energy expressed concern for inclusion of a process to allow commission staff and utilities to review proposals that contain confidential or sensitive competitive information. TXU Energy urged the commission to provide guidelines and consider alternative processes to approve programs that are competitively sensitive. TXU Energy stated that the market will continue to evolve and develop, while innovations in energy efficiency technologies, products, and services will continue to occur at a rapid pace. TXU Energy noted that, given these changes and the expectations placed on utilities, REPs, and EESPs, the rule should recognize these new roles and expectations, and not place unnecessary limitations on these entities that are trying to achieve demand and energy reductions. TXU Energy suggested the rule should also allow for new technologies and innovations to help reduce future demand. TXU Energy stated new programs and services offered by REPs in particular should be allowed to participate so long as they can demonstrate a verifiable reduction.

TXU Energy stated that the commission should be clear as to what authority it is granting this EEIP, and whether commission approval is necessary regarding EEIP decisions. TXU Energy believed that the commission should retain approval responsibility, which may be accomplished through updates from staff memos and discussions at commission Open Meetings. TXU Energy concluded that, just as HB 3693 recognized a new and expanded role for REPs in the delivery of energy efficiency programs, the EEIP must also include adequate and appropriate representation of REPs' interests. While it may be true that some REPs have participated in the past, it is important that the commission provide a mechanism to ensure that REPs participate.

Texas ROSE and TLSC recommended that the commission establish two time frames per year for EEIP review of new proposals and amendments, which Texas ROSE and TLSC described as

a process for utilities to submit new proposals and amendments. Texas ROSE and TLSC suggested, at a minimum, that the process include notice in the "In Addition" section of the *Texas Register* and notice using the commission's energy efficiency list-serve, a facsimile, or the U.S. mail; a timeline for parties requesting the change to provide information on the proposal to interested parties allowing not less than 15 days for review; and, if requested, a workshop to be held to explain substantive proposed changes. Texas ROSE and TLSC noted that, if within 30 days of the workshop, no party appeals the proposed change, the commission staff would request approval of the changes by the commission. Texas ROSE and TLSC suggested that if the proposal is appealed, the staff would establish a procedural schedule for hearing the appeal. Texas ROSE and TLSC suggested that approved changes be filed in a permanent docket established for the purpose of retaining the decisions in one location. Texas ROSE and TLSC proposed that parties be provided access to the deemed savings estimates and program templates on an on-line website. EPE and EUMMOT agreed that a streamlined process for introducing new energy efficiency programs and for changing existing programs would enable the utility program managers to make appropriate and necessary changes to their programs in a timely manner.

Texas ROSE and TLSC argued that provisions have been made to avoid, rather than encourage, review and evaluation of programs and plans, which is contrary to PURA §39.905(d). Texas ROSE and TLSC noted that the EEIP process is time consuming, but it served the energy efficiency effort well in designing programs that are by no means perfect but allow the industry to meet the energy savings goals established by the statute.

Texas ROSE and TLSC expressed disappointment in the ability of the consumers interested in energy efficiency to access the programs and the lack of information about how consumers are benefiting from the incentives being paid to contractors. Texas ROSE and TLSC suggested that using a public process with full participation by interested parties is the most effective strategy for making improvements that will remove barriers to consumers being more informed and aware of energy efficiency program options.

Commission response

The commission disagrees with Cities, Texas ROSE and TLSC, and TXU Energy's proposal to make the EEIP mandatory. The commission envisions using the EEIP as it is needed to address issues within its scope, but progress in modifying the energy efficiency program should not be dependent on whether the EEIP meets, as commission resource issues may at times make it difficult for the commission to manage the EEIP.

The commission agrees with EUMMOT's suggestion that EEIP is the forum to discuss proposed new programs, but the commission is not modifying the utilities' discretion to determine which programs to implement in order to meet their statutory obligations and goals.

The commission does not agree with TXU Energy's inclusion of a process to limit the review if proposals that contain confidential or competitively sensitive information to commission staff and the utilities. The commission believes that most discussions in the EEIP can be open, and that confidentiality issues, if they arise, can be resolved on a case-

by-case basis. The commission disagrees with TXU Energy's comments that EEIP decisions should be made through Open Meetings discussion, because such a procedure would not provide finality to matters under dispute. Where the informal discussion process in the EEIP is unable to resolve issues that arise concerning the energy efficiency program, and decision-making is not within a utility's discretion under this section, the commission may use the review process under subsection (n) to resolve issues.

The commission does not agree with TXU Energy's proposal to include a specific mechanism for retail electric providers to participate in EEIP. REPs clearly have an interest in the energy efficiency program and would have an opportunity to participate in the EEIP. The commission disagrees with Texas ROSE and TLSC's suggestion to establish two timeframes per year for EEIP review of new proposals, but it believes that notice of the EEIP should be provided and it has included notice provisions in the rule that is being adopted. The commission concludes that the EEIP is also an appropriate forum to address Texas ROSE and TLSC's suggestion to improve the information available to consumers interested in energy efficiency regarding the benefits, incentives and program options.

§25.181(r): Retail providers

ARM stated that the market has matured and become fully competitive and REPs are beginning to look beyond providing basic commodity service to their customers, and one of the areas of great interest to many of them is the area of energy efficiency. ARM contended that, in view of HB 3693, §25.181 should reflect the larger role that the legislature envisioned that REPs will and

should play in the provision of energy efficiency services; therefore ARM believed that the rule should be provided with more "teeth" in recognition of this expanded REP role.

Good Company expressed concern about the cost associated with utilities outside of ERCOT providing energy efficiency education materials to their customers. Good Company stated that detailed requirements and utility responsibilities should be provided regarding this material.

Texas ROSE and TLSC suggested mandating that REPs and electric utilities outside of ERCOT provide customers energy efficiency information by April 1, 2008, conduct a program every year in April and September, and, at a minimum, establish a voluntary REP program to provide rebates to consumers for purchase of energy efficient appliances. Texas ROSE and TLSC recommended a requirement that a REP that provides information and access to energy efficiency plans provide access on a non-discriminatory basis to its residential customers regardless of the customer's selected rate plan. Reliant opposed Texas ROSE and TLSC's proposed timelines for REPs to provide customers energy efficiency information. Reliant stated that REPs already provide education and concluded that a timeline was not needed.

TXU Energy stated that HB 3693 expressed the legislature's desire to shift some of the traditional utilities' energy efficiency role to REPs. Specifically, the legislature required the REPs to provide customers with energy efficiency educational materials, and imposed new requirements on the TDUs, and allowed the commission to encourage the REPs to provide individualized energy reports. TXU Energy also noted that §20 of HB 3693 plainly states "it is the intent of the legislature that net metering and advanced meter information networks be

deployed as rapidly as possible to allow customers to better manage energy use and control costs, and to facilitate demand response initiative." TXU Energy claimed this rulemaking was an important step to ensure that legislative intent was achieved.

TXU Energy argued that the proposed rule included only one of the two requirements imposed on the utilities' relationships with REPs, and that the inclusion of only one of the two requirements could cause confusion. TXU Energy suggested the addition of reference to the requirement that utilities provide "incentives sufficient for retail electric providers and competitive energy service providers to acquire additional cost-effective energy efficiency for residential and commercial customers" sufficient to achieve the annual targets.

Commission response

The commission agrees with ARM's comments that the market has matured and retail electric providers will have a significant impact and involvement in energy efficiency. However, the commission believes that PURA §39.905(a)(4) simply mandates that each electric utility in ERCOT use its best efforts to encourage and facilitate retail electric provider involvement.

The commission understands Good Company's concerns regarding the costs associated with providing energy efficiency education materials, but it concludes that the reporting requirements established in the rule should provide the commission adequate tools to monitor education expenses and programs, so that additional requirements are not necessary. In particular, the commission agrees with Reliant, and disagrees with Texas

ROSE and TLSC's comments relating to an April 1, 2008 deadline for providing customers energy efficiency information. The commission concludes that adopting a specific deadline is unnecessary and impractical. To balance workload and meet other program goals, utilities may want to time their information delivery and project delivery in ways that would be impractical under the Texas ROSE and TLSC proposal.

The commission also disagrees with Texas ROSE and TLSC's proposal to require rebates to customers for purchases of energy efficiency appliances. While utilities may choose to use such programs, the commission believes that the utilities that are responsible for the costs and success of the program should have the latitude to select programs that will best achieve the goals of the program. In addition, while the commission concludes that Texas ROSE and TLSC's comments regarding access to plans and information on a non-discriminatory basis reflect objectives, the parties participating in this rulemaking proceeding have not had an adequate opportunity to comment on the proposal. There are likely to be valid reasons for offering different energy efficiency programs to different customers. In particular, REPs may not see an economic benefit in offering high-cost programs to customers who have not committed to a term of service with the REP. If the commission is to encourage REP participation in the energy efficiency program, it must avoid adopting onerous restrictions on the REPs.

The commission recognizes that net metering and advanced meter information networks are important topics addressed in HB 3693, and the commission has specifically opened separate projects to address these crucial projects. These technologies should also foster

opportunities for REPs in providing energy efficiency and distributed generation options to their customers. The commission has not made any specific changes in the rule in response to these comments, because these topics are being addressed in other projects.

Finally, the commission disagrees with TXU Energy's suggestion to add a reference to the requirement that utilities provide "incentives sufficient for retail electric providers and competitive energy service providers to acquire additional cost-effective energy efficiency for residential and commercial customers." Language to this effect is included in subsection (a)(3) and does not need to be repeated in subsection (r).

§25.181(s): Customer protection

Public Citizen, Environmental Defense and SEED recommended that the final arrangement between the EESP and customer, include an estimate of energy cost savings and an approximate payback period based on that estimate. Public Citizen, Environmental Defense and SEED agreed with, and TXU Energy opposed, the inclusion of a provision stating that an EESP is not part of or endorsed by the commission or the utility. TXU Energy expressed concern that it may be necessary to explain the program to the participating customer and suggested an additional provision that "the energy efficiency service provider must not imply or infer that they are endorsed by the commission or the utility."

TXU Energy supported efforts to protect customers and suggested this section track PUC Substantive Rule §25.471 in providing the disclosures and to include the contractual provisions for residential and small commercial customers. TXU Energy suggested that for clarity the

customer's rights under subsection (s)(1)(A) should track PUC Substantive Rule §25.474(j), which would allow the customer to "rescind the agreement to receive the energy efficiency service or product without penalty or fee of any kind for a period of three federal business days." TXU Energy suggested that tracking §25.471 would support efforts to protect customers in ways that are similar to the protection for customers who select or switch REPs.

OPC urged inclusion of the Office of Attorney General's Consumer Protection hotline in this subsection, and TXU Energy proposed exclusion of the Office of Attorney General's Consumer Protection hotline. TXU Energy believed that the commission has primary jurisdiction over these programs and should be the entity the REP is required to mention. OPC argued that providing the customer as many resources as available would be beneficial to the customer.

TXU Energy, Good Company and EUMMOT proposed deletion of subsection (s)(1)(C), which requires disclosure of the fact that incentives are made available to the EESP through a program funded by utility customers, manufacturers or other entities and the amount of any incentives provided by the utility. TXU Energy stated that this should be removed due to the confusion it may cause, because the participant may not understand this refers to the statute, and the amount provided by the utility may or may not be included in the offering from the REP to the customer. Good Company stated that the disclosure provision might prove especially burdensome to EESPs, and that specific utility incentive amounts to be awarded may be unknown until after the measurement and verification of savings. EUMMOT noted that, for rented dwelling units, it is not clear whether the landlord or tenant should be provided with this information. EUMMOT concluded that the Host Customer Agreement presented to the program participant already

contains a disclosure that an incentive will be provided to the EESP or project sponsor, and it therefore would not be beneficial to the customer benefiting from the program to know that the amount of customer incentive oftentimes would be zero. According to Texas ROSE and TLSC, a contractor should be required to disclose the total amount of incentives being provided and the amount that will be provided to the customer. Texas ROSE and TLSC suggested that a form be developed and approved by the commission that may be used to satisfy the requirements of this subsection.

TXU Energy suggested that subsection (s)(1)(H) be clarified so that disclosure to the customer regarding the liability insurance to cover property damage carried by the EESP and any subcontractor be required only if applicable. TXU Energy and Good Company suggested that subsection (s)(2)(B) be clarified so that the energy efficiency service provider's contract with the customer could include a waiver of customer protections for commercial customers with a peak load exceeding 50kW, to be consistent with the allowance of this waiver for commercial customers at the beginning of subsection (s). TXU Energy recommended that the requirement under subsection (s)(3) for an "All Bills Paid" affidavit to be provided by an EESP to a customer following the installation of energy efficiency measures be permissive rather than mandatory.

Texas ROSE and TLSC noted that language was added to the proposed rule as §25.181(s)(1)(F), requiring the EESP to disclose "any adverse environmental or health effects associated with the energy efficiency measures to be installed." They argued that this provision directly contradicts §25.181(e)(3)(B)(iii), stating that a project that results in negative environmental or health effects

is not eligible for incentive payments. According to Texas ROSE and TLSC, the provision in subsection (e) is correct and should remain, and the provision in subsection (s) should be deleted.

Commission response

The commission does not agree with TXU Energy's proposed exclusion of a reference to the Office of Attorney General's Consumer Protection hotline in subsection (s) and agrees with OPC that having more resources will be beneficial to the customer. The commission does not adopt Public Citizen's recommendation that the final arrangement between an EESP and a customer should include an estimate of energy cost savings and approximate payback period based on that estimate. In the deregulated market, an energy service company or REP may market energy efficiency on a number of different grounds, including energy savings potential, and the commission does not believe that it should mandate a particular marketing representation.

The commission disagrees with TXU Energy and agrees with Public Citizen, Environmental Defense and SEED that the EESP should not represent itself as part of or endorsed by the commission or the utility. It would be misleading to customers to permit EESPs to suggest a tie to the commission as a means of inducing customers to use their services.

The commission does not agree with TXU Energy that the customer service protection provisions should track P.U.C. Substantive Rule §25.471, which protects customers who choose or switch retail electric providers, in providing disclosures and providing

contractual provisions for residential and small commercial customers. The services provided by EESPs are not necessarily identical or analogous in all instances to services provided by retail electric providers, and, therefore, rules specific to retail electric providers are not apposite to the proposed rule.

The commission disagrees with TXU Energy, Good Company and EUMMOT's recommendation to delete subsection (s)(1)(C), but it does not agree that disclosing the actual amount of incentive to the customer should be required. It is beneficial to the program to have customers understand that it is supported by the utility, but providing information on the amount of the incentive could in many instances be confusing or impracticable. PURA §39.905(b)(5) simply encourages that the "value" of the incentives to be passed on to the end-use customer, which does not require the amount of incentive, even if known or ascertainable, be disclosed to the end-use customer. The commission does not agree with Texas ROSE and TLSC's recommendation that a form be developed for the purpose of disclosing to the customer the "value" of the incentives. The commission believes that the disclosure discussed above will be sufficient to inform the customer and having a standard form would not materially further the program's objectives.

The commission does not agree with TXU Energy and Good Company's suggestion to amend subsection (s)(2)(B) to explicitly permit the waiver of customer protections for commercial customers with a peak load exceeding 50kW. This modification to subsection (s)(2)(B) is not necessary, because subsection (s) permits the waiver of disclosures and certain contractual provisions for commercial customers with a peak load exceeding 50kW.

The commission does not agree with TXU Energy's suggestion to make the "All Bills Paid" affidavit in subsection (s)(3) permissive rather than mandatory. The commission believes that this affidavit is an important customer protection. The commission agrees with Texas ROSE and TLSC's proposed deletion of subsection (s)(1)(F), which requires an EESP to disclose potential adverse health or environmental affects.

§25.181(t): Grandfathered programs

Cities recommended limiting grandfathered programs to industrial customers that have been cost-effective with net economic benefits to the participating customers. Nucor and EUMMOT recommended expansion and increased participation in existing load management programs because the legislature intended funding and participation at 2007 levels to be a floor, not a cap. EUMMOT noted that, because the current program requires a ten-year contract, the industrial participants need the ability to sign up new load for participation in the 2008 program and subsequent years. EUMMOT urged that, in order to protect the long-term viability of this program, it was necessary to enable utilities to increase participation in these existing programs. Nucor stated that the legislature clearly recognized the benefits of such programs and sought to ensure their continuation, in light of the concentration on residential and commercial energy efficiency in the new legislation. Nucor concluded that this in no way impacts the goals set for residential and commercial customers, which are specifically set forth in the statute and proposed rule and thus, will not be affected by industrial load management programs.

Commission response

The commission does not agree with Cities' recommendation to limiting grandfathered programs to industrial customers that have been cost-effective with net economic benefits to the participating customers. The statute specifically allows "any load management standard offer programs developed for industrial customers and implemented prior to May 1, 2007," and this language is included verbatim in the rule. The overall structure of the rule, including the bonus provisions, should provide an incentive to the utilities to focus their efforts on programs and participants that provide cost effective savings.

The commission does not entirely agree with Nucor and EUMMOT's proposal to increase participation in existing load management programs. The amended statute is not entirely clear, but it now defines the demand goals in terms of reducing the growth in demand for residential and commercial customers. The statute also includes a provision that directs electric utilities to "continue to make available, at 2007 funding and participation levels, any load management standard offer programs developed for industrial customers" that was implemented prior to May 2007. The commission believes that these provisions are inconsistent with treating the 2007 levels of funding and participation as a floor. The commission concludes that the utilities should have the latitude to sign up customers for the program to replace existing customers, if they leave the program, but that the levels of funding and participation should remain roughly what they were in 2007. The commission has made a minor modification to the proposed rule to reflect this understanding.

§25.181(u): Administrative penalty

EUMMOT, CenterPoint and EPE argued that the proposed provision relating to penalties is unnecessary. EUMMOT, CenterPoint and EPE stated that the commission already has ample authority to assess administrative penalties, and consequently the inclusion of such potentially harsh language is duplicative and unnecessary. EUMMOT suggested that the proposed penalty was contrary to the intent and spirit of the legislation which was intended to provide protection to utilities that have difficulty meeting the mandated goals because of conditions and circumstances totally out of their control in their service territories. CenterPoint questioned the need to have a provision under which an electric utility theoretically could incur an administrative penalty for not achieving, even to a minor degree, a "goal" set out in the rule. EPE rejected the proposed penalty language, and was concerned that the addition of specific penalty language created the appearance of an adversarial relationship between the commission and utilities with regard to meeting the energy efficiency goals instead of a cooperative one. EPE expressed concern because it serves far west Texas, where average energy use is approximately one-third to one-half of the statewide average. EPE stated that virtually all energy efficiency measures that provide significant peak demand and energy reduction savings in most other areas of Texas (*e.g.*, air infiltration reduction, the sealing of ducts, and the replacement of existing air conditioners with higher-efficiency equipment) provide little, if any, energy savings in El Paso. EPE argued this is a market condition over which EPE has almost no influence or control.

In summary EPE noted a commission discussion of this issue, as recorded in the Open Meeting transcript of February 24, 2000, in which the commission noted that the actual implementation of energy efficiency projects is in the hands of EESPs and concluded that penalizing the utility

would not be appropriate or productive. Texas ROSE and TLSC recommended that in determining the size of a penalty the commission consider the actions previously taken by the utility to promptly identify underperformance or the potential for underperformance and the steps that were taken to correct performance issues. They concluded, however, that these provisions should not be interpreted as a free pass for utilities that fail to anticipate change and fail to upgrade their programs to assure their success.

The Sierra Club believed that the proposed penalty provision was reasonable and that the proposed rule should state factors that could be used to impose a sanction and to make it clear that the commission can exempt a utility from a penalty, lessen the penalty, but not forgive it completely. The Sierra Club recommended factors to consider in determining whether to impose a sanction such as the utility's effectiveness in administering its energy efficiency program, and the actions taken by the utility to promptly identify underperformance in meeting the goal and the total amount of money spent on administration.

Commission response

The energy efficiency program has been successful, but not all of the utilities have consistently met their goals, and the commission believes that both administrative penalties and bonuses are appropriate tools to use in appropriate circumstances, to ensure compliance with the rule. The commission agrees with EUMMOT, CenterPoint and EPE that the commission already has authority to assess administrative penalties, but concludes that providing guidance on the factors that the commission would consider in assessing a penalty is useful for the commission and the utilities. Accordingly, the commission adopts the rule with a provision that deals explicitly with penalties. The commission agrees with

Texas ROSE and TLSC's comments that the rule should include the factors that are relevant in determining the amount of sanctions and the actions taken by a utility to identify and correct any underperformance. Finally, the commission declines to adopt the Sierra Club's recommendation to include additional factors to be used in assessing a sanction or penalty. The commission has a separate rule that addresses the factors to be considered in assessing penalties in general, and it concludes that these sections provide sufficient guidance for the commission and the utilities that may be subject to sanctions.

Other Issues:

OPC suggested that the rule as published may violate the "content of notice" provisions of the rulemaking section of the Administrative Procedure and Practice Act ("APA") under APA §2001.024. OPC concluded that the proposed rule should be republished for comment consistent with the APA. Texas ROSE and TLSC stated that, unlike the processes followed in other rule publications, this publication provides no redline or other comparison of the existing rules with the proposed rule. Texas ROSE and TLSC requested prior to the adoption of a rule, the commission provide such a comparison for the benefit of the interested parties commenting on the rule.

Commission response

The commission believes that the "notice" provisions of the Administrative Procedure and Practice Act were properly followed and that there is no need to republish the rule, as suggested by OPC, Texas ROSE and TLSC.

Reliant noted that its Smart Energy initiative is offered as context for its comments on the proposed rule. Reliant submitted that Smart Energy puts power in the hands of customers through the four basic concepts: (1) Transparency--knowing how much electricity you use as you use it. (2) Disaggregation--knowing how much each load, *i.e.*, individual appliance, contributes to overall power consumption. (3) Control-- the ability to make specific choices about how to use electricity. (4) Differential pricing--the ability to see how the cost of electricity varies over time. Reliant, at the public hearing, stated that OPC and Texas ROSE's comments were misguided regarding pricing programs. Reliant stated that the rule should not discriminate against moving peak usage to off-peak time and stated that pricing structures can align with new technology. Reliant also stated new retail offers for In-Home equipment may appropriately be used to offset cost.

GAP stated that the opportunities for public benefit from cooperation between utilities and local government entities, especially cities and counties, justify some recognition in the rule and some flexibility for cooperatively planning mutually supporting policies and programs. GAP noted that this is especially true in light of the role that HB 3693 envisions for school districts, higher education, municipalities and other government entities. GAP stated the legislature has recognized that these entities have a special role in preparing for our state's energy security. GAP noted that these entities can not only reduce demand and usage, but they can also save tax dollars through these efforts. GAP stated that, in addition to improving the efficient use of electricity in publicly-owned facilities, they can serve as examples and facilitate actions in other sectors of the economy. GAP suggested that this could include set-asides for delivering

weatherization or other standard offer programs to target neighborhoods, market transformation programs to improve compliance and enforcement of existing codes and standards.

Commission response

The commission agrees with GAP's suggestion that set-asides for government entities may be appropriate. Proposed subsection (i)(3), which the commission is adopting without change, provides, "A utility may establish funding set-asides or other program rules to foster participation in energy efficiency programs by municipalities and other governmental entities."

OPC noted that the commission has an Advanced Meter Systems Project (Number 34610) in progress and the market participants in that project have expressed an eagerness to deploy the advanced meters in order to offer new products with pricing and rate options. OPC noted that market participants need no incentive to offer new pricing or rate option plans that should result in energy efficiency as they already have a pent-up desire to offer these programs. OPC cited a February 11, 2005 article that lists one of the top three advanced metering benefits for investor-owned utilities to be the ability to have rate choice options. OPC submitted a document in which Reliant suggested the first order of business for the implementation project should be to set priorities for implementation items that must be accomplished in time for summer 2008 product offerings, so that REPs can plan accordingly and the ERCOT system and end-use customers can receive the benefits of mass market demand response. Reliant commented that the commissioners have been clear that they expect one of the benefits of advanced metering deployment to be new retail product offerings for end-use customers. Reliant noted that this goal

can not be achieved until a sufficient number of meters are deployed and the necessary data is available to support the products (both at a TDSP portal and locally at the home of the customer).

Texas ROSE and TLSC stated that they have been participating in Project Number 34610 on advanced metering in addition to this project to amend the energy efficiency rule. Texas ROSE and TLSC were uncertain as to how advanced meters may be applied to the implementation of energy efficiency programs, as is frequently implied in the discussion of advanced meters. Texas ROSE and TLSC noted that some proponents of advanced meters claim they will be able to provide better quality information on customer energy usage and will allow REPs to offer rate packages that vary by time. Texas ROSE and TLSC stated that the rule should be written to define the relationship between these activities and the proposed energy efficiency rule.

Commission response

The commission appreciates Reliant, OPC, Texas ROSE and TLSC's comments regarding advanced metering technology. However, advanced metering issues are being addressed in a separate proceeding.

Texas ROSE and TLSC stated that new issues that are not addressed by the Preamble to the proposed rule should be added to the discussion of the rule that is adopted by the commission, including the following topics:

- How to moderate the impacts of allowing projects that only reduce demand to be funded through rates along with programs that reduce both energy and demand, which, because they reduce emissions, provide greater value.

- The cost impact on residential and low-income consumers resulting from the exclusion of industrial customers from full participation in energy efficiency programs.
- How the rule can be structured to assure that residential and commercial customers benefit from the programs they pay for in their rates.

Commission response

This rulemaking proceeding has given parties an opportunity to raise a number of issues, including the ones specifically noted by Texas ROSE and TLSC, and the commission appreciates the comments of all of the parties that participated in the proceeding. In addition, the issues that Texas ROSE and TLSC have identified as important have been addressed by the commission in this order. The rule that the commission proposed and is adopting stresses the importance of both energy and demand reduction, and provides a greater emphasis on energy savings than the version of the rule that is being repealed. The commission believes that the rule that is being adopted is structured so that residential and low-income customers will derive value from the programs that are implemented by the utilities. The commission has disagreed with the approach that Texas ROSE and TLSC propose on customer impact issues, but it believes that the rule reflects the changes in the statute that resulted from the enactment of HB 3693 and that the incentives for utilities in the rule should result in cost-effective programs that benefit all customers. In addition, the higher goals in the statute and rule should result in opportunities for more residential and low-income customers to benefit directly from energy efficiency improvements to their homes. Finally, the rule requires the utilities to report on under-served areas, which

should lead to additional opportunities for customers in areas where the programs have not been widely deployed.

Free Lighting Corporation (FLC) stated that it is a small EESP with approximately twenty-five employees and that during the 2007 program year FLC delivered approximately 3.7 megawatts of demand savings to three utilities in southeast Texas by installing weatherization measures in single family residences. FLC noted that since 2005, it has performed these installations in more than 15,000 homes. FLC was concerned that as a small business that faces the real possibility of being adversely affected economically by the repeal of the current rule, the small, independent EESP can still play a significant role in the program if given the opportunity. At the public hearing, H and L Energy Company, on behalf of FLC, commented that it was a problem for the commission to allow TDUs to alter the current success of programs, and that it is the commission's duty is to ensure those programs that have been successful continue.

Commission response

The commission appreciates FLC's comments regarding the participation of smaller businesses as independent EESPs. One of the objectives of the statute is to develop energy efficiency expertise in Texas, so that customers have reliable sources of information, products and services in a competitive market, whether customers take advantage of the utility programs or not. The main objectives of the new rule are to implement the amendments to PURA §39.905, improve the energy efficiency program, and facilitate the utilities' efforts to meet their higher energy efficiency goals. These changes do not imply

that there is no longer a place for small EESPs. In fact, the new subsection (i)(2), which permits set-asides for small projects, may enhance the opportunities for small EESPs.

All comments, including any not specifically referenced herein, were fully considered by the commission. In adopting this section, the commission makes other minor modifications for the purpose of clarifying its intent.

These repeals and new section are adopted under the Public Utility Regulatory Act, Texas Utilities Code Annotated §14.002 and §39.905 (Vernon 2007 and Supp. 2007) (PURA), which provide the commission with the authority to make and enforce rules reasonably required in the exercise of its powers and jurisdiction and requires the commission to provide oversight and adopt rules and procedures to ensure that the utilities can meet energy efficiency goals, including a cost recovery factor, an incentive mechanism, the recovery of costs from the customer classes that receive services, and encouraging the value of incentives to be passed on to customers.

Cross Reference to Statutes: Public Utility Regulatory Act §14.002 and §39.905.

§25.181. Energy Efficiency Goal. (REPEAL)

§25.184. Energy Efficiency Implementation Project. (REPEAL)

§25.181. Energy Efficiency Goal.

(a) **Purpose**. The purpose of this section is to ensure that:

(1) electric utilities administer energy efficiency incentive programs in a market-neutral, nondiscriminatory manner and do not offer competitive services, except as permitted in §25.343 of this title (relating to Competitive Energy Services) or this section;

(2) all customers, in all eligible customer classes and all areas of an electric utility's service area, have a choice of and access to energy efficiency alternatives that allow each customer to reduce energy consumption, peak demand, or energy costs;

(3) each electric utility provides, through market-based standard offer programs or limited, targeted, market-transformation programs, incentives sufficient for retail electric providers and competitive energy service providers to acquire additional cost-effective energy efficiency for residential and commercial customers equivalent to at least:

(A) 10% of the electric utility's annual growth in demand of residential and commercial customers by December 31, 2007;

(B) 15% of the electric utility's annual growth in demand of residential and commercial customers by December 31, 2008; and

(C) 20% of the electric utility's annual growth in demand of residential and commercial customers by December 31, 2009.

(b) **Application.** This section applies to electric utilities.

(c) **Definitions.** The following terms, when used in this section, shall have the following meanings unless the context indicates otherwise:

(1) **Affiliate** --

(A) a person who directly or indirectly owns or holds at least 5.0% of the voting securities of an energy efficiency service provider;

(B) a person in a chain of successive ownership of at least 5.0% of the voting securities of an energy efficiency service provider;

(C) a corporation that has at least 5.0% of its voting securities owned or controlled, directly or indirectly, by an energy efficiency service provider;

(D) a corporation that has at least 5.0% of its voting securities owned or controlled, directly or indirectly, by:

(i) a person who directly or indirectly owns or controls at least 5.0% of the voting securities of an energy efficiency service provider; or

(ii) a person in a chain of successive ownership of at least 5.0% of the voting securities of an energy efficiency service provider; or

(E) a person who is an officer or director of an energy efficiency service provider or of a corporation in a chain of successive ownership of at least 5.0% of the voting securities of an energy efficiency service provider;

(F) a person who actually exercises substantial influence or control over the policies and actions of an energy efficiency service provider;

(G) a person over which the energy efficiency service provider exercises the control described in subparagraph (F) of this paragraph;

(H) a person who exercises common control over an energy efficiency service provider, where "exercising common control over an energy efficiency service provider" means having the power, either directly or indirectly, to direct or cause the direction of the management or policies of an energy efficiency service provider, without regard to whether that power is established through ownership or voting of securities or any other direct or indirect means; or

(I) a person who, together with one or more persons with whom the person is related by ownership, marriage or blood relationship, or by action in concert, actually exercises substantial influence over the policies and actions of an energy efficiency service provider even though neither person may qualify as an affiliate individually.

(2) **Capacity factor -** The ratio of the annual energy savings goal, in kWh, to the peak demand goal for the year, measured in kW, multiplied by the number of hours in the year; or the ratio of the actual annual energy savings, in kWh, to the actual peak demand reduction for the year, measured in kW, multiplied by the number of hours in the year.

(3) **Commercial customer --** A non-residential customer taking service at a metered point of delivery at a distribution voltage under an electric utility's tariff during the prior calendar year and a non-profit customer or government entity, including

an educational institution. For purposes of this section, each metered point of delivery shall be considered a separate customer.

(4) **Competitive energy efficiency services** -- Energy efficiency services that are defined as competitive under §25.341 of this title (relating to Definitions).

(5) **Deemed savings** -- A pre-determined, validated estimate of energy and peak demand savings attributable to an energy efficiency measure in a particular type of application that an electric utility may use instead of energy and peak demand savings determined through measurement and verification activities.

(6) **Demand** -- The rate at which electric energy is used at a given instant, or averaged over a designated period, usually expressed in kilowatts (kW) or megawatts (MW).

(7) **Demand savings** -- A quantifiable reduction in demand.

(8) **Eligible customers** -- Residential and commercial customers. In addition, to the extent that they meet the criteria for participation in load management standard offer programs developed for industrial customers and implemented prior to May 1, 2007, industrial customers are eligible customers solely for the purpose of participating in such programs.

(9) **Energy efficiency** -- Improvements in the use of electricity that are achieved through facility or equipment improvements, devices, or processes that produce reductions in demand or energy consumption with the same or higher level of end-use service and that do not materially degrade existing levels of comfort, convenience, and productivity.

(10) **Energy efficiency measures** -- Equipment, materials, and practices at a customer's site that result in a reduction in electric energy consumption, measured in kilowatt-hours (kWh), or peak demand, measured in kilowatts (kWs), or both. These measures may include thermal energy storage and removal of an inefficient appliance so long as the customer need satisfied by the appliance is still met.

(11) **Energy efficiency program** -- The aggregate of the energy efficiency activities carried out by an electric utility under this section or a set of energy efficiency projects carried out by an electric utility under the same name and operating rules.

(12) **Energy efficiency project** -- An energy efficiency measure or combination of measures undertaken in accordance with a standard offer or market transformation program.

(13) **Energy efficiency service provider** -- A person who installs energy efficiency measures or performs other energy efficiency services under this section. An energy efficiency service provider may be a retail electric provider or commercial customer, provided that the commercial customer has a peak load equal to or greater than 50kW.

(14) **Energy savings** -- A quantifiable reduction in a customer's consumption of energy that is attributable to energy efficiency measures.

(15) **Growth in demand** -- The annual increase in demand in the Texas portion of an electric utility's service area at time of peak demand, as measured in accordance with this section.

(16) **Hard-to-reach customers** -- Residential customers with an annual household income at or below 200% of the federal poverty guidelines.

(17) **Incentive payment** -- Payment made by a utility to an energy efficiency service provider under an energy-efficiency program.

(18) **Inspection** -- Examination of a project to verify that an energy efficiency measure has been installed, is capable of performing its intended function, and is producing an energy saving or demand reduction.

(19) **Load control** -- Activities that place the operation of electricity-consuming equipment under the control or dispatch of an energy efficiency service provider, an independent system operator or other transmission organization or that are controlled by the customer, with the objective of producing energy or demand savings.

(20) **Load management** -- Load control activities that result in a reduction in peak demand on an electric utility system or a shifting of energy usage from a peak to an off-peak period or from high-price periods to lower price periods.

(21) **Market transformation program** -- Strategic programs intended to induce lasting structural or behavioral changes in the market that result in increased adoption of energy efficient technologies, services, and practices, as described in this section.

(22) **Measurement and verification** -- Activities intended to determine the actual energy and demand savings resulting from energy efficiency projects as described in this section.

(23) **Off-peak period** -- Period during which the demand on an electric utility system is not at or near its maximum. For the purpose of this section, the off-peak period includes all hours that are not in the peak period.

(24) **Peak demand** -- Electrical demand at the times of highest annual demand on the utility's system.

(25) **Peak demand reduction** -- Reduction in demand on the utility system throughout the utility system's peak period.

(26) **Peak period** -- For the purpose of this section, the peak period consists of the hours from one p.m. to seven p.m., during the months of June, July, August, and September, excluding weekends and Federal holidays.

(27) **Renewable demand side management (DSM) technologies** -- Equipment that uses a renewable energy resource (renewable resource), as defined in §25.173(c) of this title (relating to Goal for Renewable Energy) that, when installed at a customer site, reduces the customer's net purchases of energy, demand, or both.

(28) **Standard offer contract** -- A contract between an energy efficiency service provider and a participating utility specifying standard payments based upon the amount of energy and peak demand savings achieved through energy efficiency measures, the measurement and verification protocols, and other terms and conditions, consistent with this section.

(29) **Standard offer program** -- A program under which a utility administers standard offer contracts between the utility and energy efficiency service providers.

(d) **Cost-effectiveness standard.** An energy efficiency program is deemed to be cost-effective if the cost of the program to the utility is less than or equal to the benefits of the program.

(1) The cost of a program includes the cost of incentives, measurement and verification, and actual or allocated research and development and administrative

costs. The benefits of the program consist of the value of the demand reductions and energy savings, measured in accordance with the avoided costs prescribed in this subsection. The present value of the program benefits shall be calculated over the projected life of the measures installed under the program.

(2) The avoided capacity cost shall be based on the estimated capital cost of a new gas turbine, and the avoided energy costs shall be based on wholesale energy costs.

(A) The initial avoided cost of capacity is $80/kW per year. The avoided cost of capacity shall be adjusted annually based on the annual capacity costs of a new simple-cycle gas turbine, using a recognized industry source of information, adjusted for line losses.

(B) The initial avoided cost of energy is $0.055/kWh. The avoided cost of energy shall be adjusted annually to the simple average of the market clearing price in ERCOT for balancing energy for all hours during the peak period for the previous calendar year. When ERCOT nodal prices are available, the avoided energy price shall be adjusted to the zonal average of nodal prices for all hours during the peak period. For areas outside of ERCOT with a regional transmission organization that has been approved by the Federal Energy Commission and operates a balancing market and publicly reports prices in the market, the avoided energy cost may be adjusted to the simple average of the market clearing price in the region for balancing service for peak hours. For areas that do not have such a regional transmission organization, the ERCOT avoided energy cost shall

be used unless the commission determines a different avoided cost for an area.

(e) **Annual energy efficiency goals.** Electric utilities shall administer energy efficiency programs to achieve at least a 15% reduction in the electric utility's annual growth in demand of residential and commercial customers by December 31, 2008; and 20% of the electric utility's annual growth in demand of residential and commercial customers by December 31, 2009.

(1) A utility may carry over any reduction in growth in residential and commercial demand that is achieved in 2007 in excess of 10% of its growth in demand to apply to the required savings in 2008, to the extent that the reduction is consistent with the definition of demand reduction in this section. Each utility's demand-reduction goal shall be calculated as follows:

(A) Each year's historical demand for residential and commercial customers shall be adjusted for weather fluctuations, using weather data for the most recent ten years. The utility's growth in residential and commercial demand is based on the average growth in retail load in the Texas portion of the utility's service area, measured at the utility's annual system peak. The utility shall calculate the average growth rate for the prior five years.

(B) The demand goal for energy-efficiency savings for a year is calculated by applying the percentage goal, prescribed in this subsection, to the average growth in demand, calculated in accordance with subparagraph (A) of this paragraph.

(C) A utility may submit for commission approval an alternative method to calculate its growth in demand, for good cause.

(D) Beginning in 2009 a utility's demand reduction goal in megawatts for any year shall not be less than the previous year's goal.

(E) Savings achieved through programs for hard-to-reach customers shall be no less than 5.0% of the utility's total demand reduction goal.

(2) Beginning in 2008, an electric utility shall administer an energy efficiency program designed to meet an energy savings goal calculated from its demand savings goal, using a 20% capacity factor.

(3) Electric utilities shall administer energy efficiency programs to effectively and efficiently achieve the goals set out in this section.

(A) Incentive payments may be made under standard offer contracts or market transformation contracts, for energy savings and demand reductions. Each electric utility shall establish standard incentive payments to achieve the objectives of this section.

(B) Projects or measures under either the standard offer or market transformation programs are not eligible for incentive payments or compensation if:

(i) A project would achieve demand or energy reduction by eliminating an existing function, shutting down a facility or operation, or would result in building vacancies or the re-location of existing operations to a location outside of the area served by

the utility conducting the program, except for an appliance recycling program consistent with this section.

(ii) A measure would be adopted even in the absence of the energy efficiency service provider's proposed energy efficiency project, except in special cases, such as hard-to-reach and weatherization programs, or where free riders are accounted for using a net to gross adjustment of the avoided costs, or another method that achieves the same result.

(iii) A project results in negative environmental or health effects, including effects that result from improper disposal of equipment and materials.

(f) **Cost recovery**. An Energy Efficiency Cost Recovery Factor (EECRF) rate schedule shall be included in the utility's tariff to permit the utility to timely recover the reasonable costs of providing energy efficiency programs. The forecast of the energy efficiency program costs shall reflect the spending necessary to meet the utility's goals under this section, subject to the limitations established in this section.

(1) A utility may request that an EECRF be established to recover all of the utility's forecasted annual energy efficiency program costs, if the commission order establishing the utility's base rates does not expressly include an amount for energy efficiency program costs. If a utility's existing base rate order expressly includes an amount for energy efficiency program costs, the utility may request that an EECRF be established to recover forecasted annual energy efficiency program costs in excess of the costs recovered through base rates.

(2) In any base rate case that is filed after December 31, 2007 or is pending on that date, base rates shall not be set to recover energy efficiency costs.

(3) The EECRF shall be calculated to recover the costs associated with each program from the customer classes that receive services under each program.

(4) Each year, a utility with an EECRF shall apply to adjust the EECRF in order to reflect changes in costs and bonuses and minimize any over- or under-collection of energy efficiency costs resulting from the use of the EECRF. The EECRF shall be designed to permit the utility to recover any under-recovery of energy efficiency program costs or return any over-recovery of costs. An application to change an EECRF that will take effect in January of the following year shall be filed not later than May 1.

(5) The EECRF may be changed in a general rate proceeding or, if a general rate proceeding has not been conducted in the preceding year, an electric utility may petition to adjust its EECRF on an annual basis.

(6) The commission may approve an energy charge or a monthly customer charge for the EECRF. The EECRF shall be set at a rate that will give the utility the opportunity to earn revenues equal to the sum of the utility's forecasted energy efficiency costs, net of energy efficiency costs included in base rates, the energy efficiency performance bonus amount that it earned for the prior year under subsection (h) of this section and any adjustment for past over- or under-recovery of energy efficiency revenues.

(7) A utility that is unable to establish an EECRF due to a rate freeze may defer the costs of complying with this section and recover the deferred costs through an

energy efficiency cost recovery factor on the expiration of the rate freeze period. Any deferral of costs that are not being recovered in rates shall bear interest at the utility's commission approved cost of capital from the time the costs are incurred until the commission approves an EECRF for the recovery of the costs. A utility that seeks to defer its costs shall file an application for approval of the deferral.

(8) A utility's program expenditures for 2008 shall not exceed 175% of its program budget for 2007 for residential and commercial customers, as included in its April 1, 2006, filing. A utility's program expenditures for 2009 shall not exceed 250% of its program budget for 2007 for residential and commercial customers, as included in the April 1, 2006, filing.

(9) A utility's application to establish or change an EECRF shall include the information and schedules in any commission approved EECRF filing package, but at a minimum shall include testimony and schedules showing the utility's forecasted energy efficiency costs, energy efficiency costs included in base rates, the Energy Efficiency Performance Bonus amount that it earned for the prior year, any adjustment for past over- or under-recovery of energy efficiency revenues, information concerning the calculation of billing determinants, information from its last base rate case concerning the allocation of energy efficiency costs to customer classes, and the following:

(A) the incentive payments by the utility, by program; the utility's administrative costs for its energy efficiency programs for the most recent year and for the year in which the EECRF is expected to be in effect,

including costs for the dissemination of information and outreach; and other major administrative costs, and the basis for the projection;

(B) billing determinants for the most recent year and for the year in which the EECRF is expected to be in effect;

(C) the actual revenues attributable to the EECRF for any period for which the utility seeks to adjust the EECRF for an under- or over-recovery of EECRF revenues; and

(D) any other information that supports the determination of the EECRF.

(10) Upon a utility's filing of an application to establish or change an EECRF, the presiding officer shall set a procedural schedule that will enable the commission to issue a final order in the proceeding as follows, except where good cause supports a different procedural schedule:

(A) within 60 days after a sufficient application was filed if no hearing is requested within 30 days of the filing of the application; or

(B) within 120 days after a sufficient application was filed, if a timely request for a hearing is made. If a hearing is requested, the hearing will be held no earlier than the first working day after the 45th day after a sufficient application is filed.

(11) In any proceeding to establish or change an EECRF, the utility must show that:

(A) the costs to be recovered through the EECRF are reasonable estimates of the costs necessary to provide energy efficiency programs and to meet the utility's goals under this section;

(B) calculations of any under- or over-recovery of EECRF revenues is consistent with this section;

(C) any energy efficiency performance bonus for which recovery is being sought is consistent with this section;

(D) the costs assigned or allocated to customer classes are reasonable and consistent with this section;

(E) the estimate of billing determinants for the period for which the EECRF is to be in effect is reasonable; and

(F) any calculations or estimates of system losses and line losses used in calculating the charges are reasonable.

(12) The scope of a proceeding to establish or adjust an EECRF is limited to the issues of whether the utility's cost estimates are reasonable, calculations of under- or over-recoveries are consistent with this section, the calculation of any energy efficiency performance bonus is consistent with this section, the assignments and allocations to the classes are appropriate, and the calculation of the EECRF is in accordance with this subsection. The commission shall make a final determination of the reasonableness of the costs and performance bonuses that the utility recovered through the EECRF.

(13) A utility shall file an application at least every three calendar years to reconcile costs recovered through its EECRF. The commission may establish a schedule and form for such applications.

(g) **Incentive payments.** The incentive payments for each customer class shall not exceed 100% of avoided cost, as determined in accordance with this section. The incentive payments shall be set by each utility with the objective of achieving its energy and demand savings goals at the lowest reasonable cost per program. Different incentive levels may be established for areas that have historically been underserved by the utility's energy efficiency program or for other appropriate reasons. Utilities may adjust incentive payments during the program year, but such adjustments must be clearly publicized in the materials used by the utility to set out the program rules and describe the program to participating energy efficiency service providers.

(h) **Energy efficiency performance bonus**. A utility that exceeds its demand reduction goal established in this section at a cost that does not exceed the limit established in this section shall be awarded a performance bonus. The performance bonus shall be based on the utility's energy efficiency achievements for the previous calendar year. The bonus calculation shall not include demand or energy savings that result from programs other than programs implemented under this section.

(1) The performance bonus shall entitle the utility to receive a share of the net benefits realized in meeting its demand reduction goal established in this section.

(2) Net benefits shall be calculated as the sum of total avoided cost associated with the eligible programs administered by the utility minus the sum of all program costs. Total avoided costs shall be calculated in accordance with this section.

(3) A utility that exceeds 100% of its demand reduction goal (DRG) shall receive a bonus equal to 1% of the net benefits for every 2% that the demand reduction goal has been exceeded, with a maximum of a 20% of the utility's program costs.

(4) A utility that meets at least 120% of its demand reduction goal with at least 10% of its savings achieved through Hard-to-Reach programs shall receive an additional bonus equal to 10% of the bonus calculated under paragraph (3) of this subsection.

(5) Any energy or demand savings achieved in 2007 that are applied to a utility's goal in 2008 are not eligible for a performance bonus.

(6) A bonus earned under this section shall not be included in the utility's revenues or net income for the purpose of establishing a utility's rates or commission assessment of its earnings.

(i) **Utility administration.** The cost of administration may not exceed 10% of a utility's total program costs. Research and development costs shall not exceed 10% of a utility's total program costs. Any bonus awarded by the commission shall not be included in program costs for the purpose of applying these limits.

(1) Administrative costs include all reasonable and necessary costs incurred by a utility in carrying out its responsibilities under this section, including:

(A) conducting informational activities designed to explain the standard offer programs and market transformation programs to energy efficiency service providers, retail electric providers, and vendors;

(B) for utilities outside of ERCOT, providing informational programs to improve customer awareness of energy efficiency programs and measures;

(C) reviewing and selecting energy efficiency programs in accordance with this section;

(D) providing regular and special reports to the commission, including reports of energy and demand savings; and

(E) any other activities that are necessary and appropriate for successful program implementation.

(2) A utility shall adopt measures to foster competition among energy service providers, such as limiting the number of projects or level of incentives that a single energy service provider and its affiliates is eligible for and establishing funding set-asides for small projects.

(3) A utility may establish funding set-asides or other program rules to foster participation in energy efficiency programs by municipalities and other governmental entities.

(4) Electric utilities shall use standardized forms, procedures, deemed savings estimates and program templates. The electric utility shall file any standardized materials, or any change to it, with the commission at least 60 days prior to its use. In filing such materials, the utility shall provide an explanation of changes from the version of the materials that was previously used. The utility shall provide relevant documents to REPs and EESPs and work collaboratively with them when it changes program documents, to the extent that such changes are not considered

in the Energy Efficiency Implementation Project described in subsection (q) of this section.

(j) **Standard offer programs.** A utility's standard offer program shall be implemented through programs rules and standard offer contracts that are consistent with this section. Standard offer contracts will be available to any energy efficiency service provider that satisfies the contract requirements prescribed by the utility under this section and demonstrates that it is capable of managing energy efficiency projects under an electric utility's energy efficiency program.

(k) **Market transformation programs**. Market transformation programs are strategic efforts, including, but not limited to, incentives and education designed to reduce market barriers for energy efficient technologies and practices. Market transformation programs may be designed to obtain energy savings or peak demand reductions beyond savings that would be achieved through compliance with existing building codes and equipment efficiency standards or standard offer programs. Utilities should cooperate with the REPs, and, where possible, leverage existing industry-recognized programs that have the potential to reduce demand and energy consumption in Texas and consider statewide administration where appropriate. Market transformation programs may operate over a period of more than one year and may demonstrate cost-effectiveness over a period longer than one year.

(l) **Requirements for standard offer and market transformation programs.** A utility's standard offer and market transformation programs shall meet the requirements of this subsection.

(1) Standard offer and market transformation programs:

(A) shall describe the eligible customer classes and allocate funding among the classes on an equitable basis;

(B) may offer standard incentive payments and specify a schedule of payments that are sufficient to meet the goals of the program, which shall be consistent with this section, or any revised payment formula adopted by the commission. The incentive payments may include both payments for energy and demand savings, as appropriate;

(C) shall not permit the provision of any product, service, pricing benefit, or alternative terms or conditions to be conditioned upon the purchase of any other good or service from the utility, except that only customers taking transmission and distribution services from a utility can participate in its energy efficiency programs;

(D) shall provide for a complaint process that allows:

(i) an energy efficiency service provider to file a complaint with the commission against a utility; and

(ii) a customer to file a complaint with the utility against an energy efficiency service provider;

(E) may permit the use of renewable DSM and combined heat and power technologies, involving installations of ten megawatts or less; and

(F) may require energy efficiency service providers to provide the following:

(i) a description of how the value of any incentive will be passed on to customers;

(ii) evidence of experience and good credit rating;

(iii) a list of references;

(iv) all applicable licenses required under state law and local building codes;

(v) evidence of all building permits required by governing jurisdictions; and

(vi) evidence of all necessary insurance.

(2) Standard offer programs:

(A) shall require energy efficiency service providers to identify peak demand and energy savings for each project in the proposals they submit to the utility;

(B) shall be neutral with respect to specific technologies, equipment, or fuels. Energy efficiency projects may lead to switching from electricity to another energy source, provided that the energy efficiency project results in overall lower energy costs, lower energy consumption, and the installation of high efficiency equipment. Utilities may not pay incentives for a customer to switch from gas appliances to electric appliances except in connection with the installation of high efficiency combined heating and air conditioning systems;

(C) shall require that all projects result in a reduction in purchased energy consumption, or peak demand, or a reduction in energy costs for the end-use customer;

(D) shall encourage comprehensive projects incorporating more than one energy efficiency measure;

(E) shall be limited to projects that result in consistent and predictable energy or peak demand savings over an appropriate period of time based on the life of the measure; and

(F) may permit a utility to use poor performance, including customer complaints, as a criterion to limit or disqualify an energy efficiency service provider or its affiliate from participating in a program.

(3) A market transformation program shall identify:

(A) program goals;

(B) market barriers the program is designed to overcome;

(C) key intervention strategies for overcoming those barriers;

(D) estimated costs and projected energy and capacity savings;

(E) a baseline study that is appropriate in time and geographic region. In establishing a baseline, the study shall consider the level of regional implementation and enforcement of any applicable energy code;

(F) program implementation timeline and milestones;

(G) a description of how the program will achieve the transition from extensive market intervention activities toward a largely self-sustaining market;

(H) a method for measuring and verifying savings; and

(I) the period over which savings shall be considered to accrue, including a projected date by which the market will be sufficiently transformed so that the program should be discontinued.

(4) A market transformation program shall be designed to achieve energy or peak demand savings, or both, and lasting changes in the way energy efficient goods or services are distributed, purchased, installed, or used over a defined period of time.

(5) A load-control standard-offer program shall not permit an energy efficiency service provider to receive incentives under the utility program for the same demand reduction for which it is compensated under a demand response program conducted by an independent organization, independent system operator, or regional transmission operator.

(m) **Energy efficiency plans and reports.** Each electric utility shall file by April 1 of each year an energy efficiency plan and report, as described in this subsection. The plan and report shall be filed as a single document.

(1) Each electric utility's energy efficiency plan and report shall describe how the utility intends to achieve the goals set forth in this section and comply with the other requirements of this section. The plan and report shall be based on calendar years. The plan and report shall propose an annual budget sufficient to reach the goals specified in this section.

(2) Each electric utility's plan and report shall include:

(A) the utility's total actual and weather-adjusted peak demand and actual and weather-adjusted peak demand for residential and commercial customers for the previous five years;

(B) the demand goal calculated in accordance with this section for the current year and the following year, including documentation of the demand, weather adjustments, and the calculation of the goal;

(C) the utility's customers' total actual and weather-adjusted energy consumption and actual and weather-adjusted energy consumption for residential and commercial customers for the previous five years;

(D) the energy goal calculated in accordance with this section, including documentation of the energy consumption, weather adjustments, and the calculation of the goal;

(E) a description of existing energy efficiency programs and an explanation of the extent to which these programs will be used to meet the utility's energy efficiency goals;

(F) a description of each of the utility's energy efficiency programs that were not included in the previous year's plan, including measurement and verification plans if appropriate, and any baseline studies and research reports or analyses supporting the value of the new programs;

(G) an estimate of the energy and peak demand savings to be obtained through each separate energy efficiency program;

(H) a description of the customer classes targeted by the utility's energy efficiency programs, specifying the size of the hard-to-reach, residential,

and commercial classes, and the methodology used for estimating the size of each customer class;

(I) the proposed annual budget required to implement the utility's energy efficiency programs, broken out by program for each customer class, including hard-to-reach customers, and any set-asides or budget restrictions adopted or proposed in accordance with this section. The proposed budget shall detail the incentive payments and utility administrative costs, including specific items for research and information and outreach to energy efficiency service providers, and other major administrative costs, and the basis for estimating the proposed expenditures;

(J) a discussion of the types of informational activities the utility plans to use to encourage participation by energy efficiency service providers and retail electric providers to participate in energy efficiency programs, including the manner in which the utility will provide notice of energy efficiency programs, and any other facts that may be considered when evaluating a program;

(K) the utility's energy goal and demand goal for the prior five years, as reported in annual energy efficiency reports filed in accordance with this section;

(L) a comparison of projected savings (energy and demand), reported savings, and verified savings for each of the utility's energy efficiency programs for the prior two years;

(M) a description of the results of any market transformation program, including a comparison of the baseline and actual results and any adjustments to the milestones for a market transformation program;

(N) expenditures for the prior five years for energy and demand incentive payments and program administration, by program and customer class;

(O) funds that were committed but not spent during the prior year, by program;

(P) a comparison of actual and budgeted program costs, including an explanation of any increase or decreases of more than 10% in the cost of a program;

(Q) information relating to energy and demand savings achieved and the number of customers served by each program by customer class;

(R) the utility's most recent EECRF, the revenue collected through the EECRF, energy efficiency revenue collected through base rates, and the control number under which the most recent EECRF was established;

(S) the amount of any over- or under-recovery energy efficiency program costs whether collected through base rates or the EECRF;

(T) beginning with the report filed in 2009, a list of any counties that in the prior year were under-served by the energy efficiency program; and

(U) a calculation showing whether the utility qualifies for a performance bonus and the amount of any bonus.

(n) **Review of programs.** An electric utility's energy efficiency program is subject to review, which may be initiated by the commission staff or informal review through the EEIP process. The review under this section may relate to an existing program, proposed new programs, or the failure of the utility to implement a program. The initiation of a formal review of a utility's energy efficiency plan does not preclude the utility from carrying out existing or planned programs, unless a presiding officer or the commission issues an order requiring it to make a change in a program.

(o) **Inspection, measurement and verification.** Each standard offer program shall include an industry-accepted measurement and verification protocol, such as the International Performance Measurement and Verification Protocol, to measure and verify energy and peak demand savings to ensure that the goals of this section are achieved. An energy efficiency service provider shall not receive final compensation until it establishes that the work is complete and measurement and verification in accordance with the protocol verifies that the savings will be achieved. If inspection of one or more measures is a part of the protocol, an energy efficiency service provider shall not receive final compensation until the utility has conducted its inspection on the sample of measures and the inspections confirm that the work has been done.

(1) The energy efficiency service provider is responsible for the measurement of energy and peak demand savings using the approved measurement and verification protocol, and may utilize the services of an independent third party for such purposes.

(2) Commission-approved deemed energy and peak demand savings may be used in lieu of the energy efficiency service provider's measurement and verification,

where applicable. The deemed savings approved by the commission before December 31, 2007 are continued in effect, unless superseded by commission action.

(3) An energy efficiency service provider shall verify that the measures contracted for were installed before final payment is made to the energy efficiency service provider, by obtaining the customer's signature certifying that the measures were installed, or by other reasonably reliable means approved by the utility.

(4) For projects involving over 30 installations, a statistically significant sample of installations will be subject to on-site inspection in accordance with the protocol for the project to verify that measures are installed and capable of performing their intended function. Inspection shall occur within 30 days of notification of measure installation.

(5) Projects of less than 30 installations may be aggregated and a statistically significant sample of the aggregate installations will be subject to on-site inspection in accordance with the protocol for the projects to ensure that measures are installed and capable of performing their intended function. Inspection shall occur within 30 days of notification of measure installation.

(6) The sample size for on-site inspections may be adjusted for an energy efficiency service provider under a particular contract, based on the results of prior inspections.

(p) **Targeted energy efficiency program.** Unless funding is provided under PURA §39.903, each unbundled transmission and distribution utility shall include in its energy efficiency

plan a targeted low-income energy efficiency program as described by PURA §39.903(f)(2). Savings achieved by the program shall count toward the transmission and distribution utility's energy efficiency goal. Each utility shall include a proposed funding level for the weatherization program in its energy efficiency plan.

(q) **Energy Efficiency Implementation Project - EEIP.** The commission may use an implementation project involving input by interested persons to make recommendations to the commission with regard to best practices in standard offer programs and market transformation programs, modifications to programs, standardized forms and procedures, deemed savings estimates, program templates, and the overall direction of the energy efficiency program established by this section. The following functions may also be undertaken in the energy efficiency implementation project:

(1) development, discussion, and review of new statewide standard offer programs;

(2) identification, discussion, design, and review of new market transformation programs;

(3) determination of measures for which deemed savings are appropriate and participation in the development of deemed savings estimates for those measures;

(4) review of and recommendations on an independent measurement and verification expert's report;

(5) review of and recommendations on incentive payment levels and their adequacy to induce the desired level of participation by energy efficiency service providers and customers;

(6) review of and recommendations on the utility annual energy efficiency plans and reports;

(7) periodic reviews of the cost effectiveness methodology; and

(8) other activities as requested by the commission.

(r) **Retail providers**. Each electric utility in the ERCOT region shall conduct outreach and information programs and otherwise use its best efforts to encourage and facilitate the involvement of retail electric providers as energy efficiency service companies in the delivery of efficiency and demand response programs. Electric utilities outside of the ERCOT region shall provide customers with energy efficiency education materials.

(s) **Customer protection.** Each energy efficiency service provider that provides energy efficiency services to end-use customers under this section shall provide the disclosures and include the contractual provisions required by this subsection, except for commercial customers with a peak load exceeding 50 kW.

(1) Clear disclosure to the customer shall be made of the following:

(A) the customer's right to a cooling-off period of three business days, in which the contract may be canceled, if applicable under law;

(B) the name, telephone number, and street address of the energy efficiency services provider and any subcontractor that will be performing services at the customer's home or business;

(C) the fact that incentives are made available to the energy efficiency services provider through a program funded by utility customers, manufacturers or other entities and the amount of any incentives provided by the utility;

(D) the amount of any incentives that will be provided to the customer;

(E) notice of provisions that will be included in the customer's contract, including warranties;

(F) the fact that the energy efficiency service provider must measure and report to the utility the energy and peak demand savings from installed energy efficiency measures;

(G) the liability insurance to cover property damage carried by the energy efficiency service provider and any subcontractor;

(H) the financial arrangement between the energy efficiency service provider and customer, including an explanation of the total customer payments, the total expected interest charged, all possible penalties for non-payment, and whether the customer's installment sales agreement may be sold;

(I) the fact that the energy efficiency service provider is not part of or endorsed by the commission or the utility; and

(J) a description of the complaint procedure established by the utility under this section, and toll free numbers for the Office of Customer Protection of the Public Utility Commission of Texas, and the Office of Attorney General's Consumer Protection Hotline.

(2) The energy efficiency service provider's contract with the customer shall include:

(A) work activities, completion dates, and the terms and conditions that protect residential customers in the event of non-performance by the energy efficiency service provider;

(B) provisions prohibiting the waiver of consumer protection statutes, performance warranties, false claims of energy savings and reductions in energy costs; and

(C) a complaint procedure to address performance issues by the energy efficiency service provider or a subcontractor.

(3) When an energy efficiency service provider completes the installation of measures for a customer, it shall provide the customer an "All Bills Paid" affidavit to protect against claims of subcontractors.

(t) **Grandfathered programs.** An electric utility that offered a load management standard offer programs for industrial customers prior to May 1, 2007 shall continue to make the program available, at 2007 funding and participation levels, and may include additional customers in the program to maintain these funding and participation levels. Notwithstanding subsection (c)(7), an industrial customer may be considered an eligible customer for programs that will be completed no later than December 31, 2008.

(u) **Administrative penalty.** The commission may impose an administrative penalty or other sanction if the utility fails to meet a goal for energy efficiency under this section. Factors that may be considered in determining whether to impose a sanction for the utility's failure to meet the goal include:

(1) the level of demand by retail electric providers and competitive energy service providers for program incentives made available by the utility through its programs;

(2) changes in building energy codes;

(3) changes in national or state appliance or equipment efficiency standards;

(4) any actions taken by the utility to identify and correct any deficiencies in its energy efficiency program; and

(5) the utility's effectiveness in administering its energy efficiency program.

This agency hereby certifies that the adoption has been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority. It is therefore ordered by the Public Utility Commission of Texas that §25.181 and §25.184 are repealed and new §25.181, relating to Energy Efficiency Goal is hereby adopted with changes to the text as proposed.

SIGNED AT AUSTIN, TEXAS the _____ day of April 2008.

PUBLIC UTILITY COMMISSION OF TEXAS

_____
BARRY T. SMITHERMAN, CHAIRMAN

_____
JULIE CARUTHERS PARSLEY, COMMISSIONER

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PAUL HUDSON, COMMISSIONER

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