

Energy and Clean Technology Alert: Massachusetts Orders Revenue Decoupling by Distribution Companies

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On July 16, 2008, the Massachusetts Department of Public Utilities (“DPU” or “Department”) issued an Order calling for revenue “decoupling” by distribution companies in Massachusetts. The Department’s Order, which results from a year-long investigation, follows closely on the heels of the “Green Communities Act,” the Commonwealth’s comprehensive energy reform bill.

See our Client Alert on the Green Communities Act from July 2, 2008.

The Order’s goal is to remove the disincentives that distribution companies face in fostering energy efficiency and demand-reduction programs. Currently, distribution companies’ revenues are tied to sales: the more electricity or gas customers use, the more revenues the companies earn. The Department’s new decoupling mechanism will separate (hence, “decouple”) electric and gas distribution company revenues from changes in consumption, *i.e.*, commodity sales, regardless of the underlying cause of the changes. Decoupling will align distribution companies’ financial interests with state policy objectives by promoting the deployment of demand-reducing resources, according to the Department. At the same time, it will ensure that companies are not harmed by decreases in sales associated with those deployments.

In its Order, the Department notes that decoupling is a first step in the Commonwealth to “implement the ground breaking provisions of the Green Communities Act” and “paves the way for aggressive expansion of demand resources (*i.e.*, energy efficiency, demand response, combined heat and power, and renewable generation).” The Order, in conjunction with the Commonwealth’s overall policy to support the development of demand resources, creates a significant opportunity for distribution companies to implement such programs. It also encourages third parties to create effective mechanisms to promote energy efficiency, conservation and wise use of energy resources.

The Order also establishes specific ratemaking filing procedures and requirements that allow distribution companies to capture revenues that would otherwise be unrecovered due to the implementation of energy efficiency/demand reduction programs. Distribution companies will implement decoupling plans through a base rate proceeding consistent with the Department’s well-established precedents regarding cost of service, cost allocation, and rate design. Each distribution company is required to notify the Department, which anticipates numerous filings, within 45 days of the Order regarding its intention to file a rate case.

As part of any filing, distribution companies will be required to reconcile actual revenues derived from the number of customers served, with consideration of the revenue impacts of capital spending and inflation as compared to a revenue target. The Department would no longer consider growth in usage per customer as a criterion for determining total utility allowed revenue.

Other significant requirements include:

- Reconciliation of target revenues to actual revenues on a company-wide basis (to ensure that customers in one rate class do not see a disproportionate change in rates compared to customers in other rate classes);
- Annual reconciliations through adjustments of distribution charges (to provide customers with greater incentive to reduce their energy consumption, furthering the goal of deployment of demand resources);
- Interim rate adjustments (when the difference between actual and target revenues exceeds ten percent); and
- Recovery of “lost base revenues” resulting from implementation of energy efficiency activities (electric companies will be required to petition the Department as part of filing three-year efficiency plans required by the Green Communities Act).

In addition to these requirements, in each decoupling proceeding, the Department will evaluate the distribution company’s risk profile (“decoupling should reduce risks to company shareholders”); investigate issues related to cost allocation, rate design and cost reconciling mechanisms; and address issues that were not fully explored in this proceeding (*e.g.*, cost drivers, shifting risk profiles). Because distribution companies are operating under rate plans approved by the Department through litigated proceedings, the Department will allow those plans to run their course and not require full decoupling until the end of 2012.

This Order has several important implications for distribution companies, efficiency and demand response providers, and consumers. First, it places significant, new responsibilities on distribution companies to pursue efficiency and demand response programs for the benefit of Massachusetts ratepayers. Second, the Department specifically identifies the resources and capabilities of the distribution companies as critical to achieving its policy goals: to support expansion of energy efficiency, demand response, combined heat and power, and renewable generation. Finally, the Order assumes that efficiency and demand response providers be given a substantial opportunity to flourish through expanded utility-sponsored efficiency programs.

Each rate case, particularly the first cases resulting from the Order, will establish important precedents and mechanisms to realize the Department’s goal of promoting demand response through decoupling. All stakeholders, including demand response providers, distributed generators, energy and grid efficiency companies and consumers, have a unique opportunity to participate in these proceedings. These stakeholders should seize the opportunity to ensure that an appropriate balance is struck between the Department’s goals of reducing energy use, adjusting distribution company rates, and expanding efficiency and demand response industries.

To read the full text of the Department of Public Utilities Order [Click here](#).

If you wish to discuss the contents of this alert, or for assistance with issues raised by the legal or regulatory developments that are the subject of this alert, please contact any of the Mintz Levin service professionals listed below.

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