

# PERFORMANCE INCENTIVE (PI) MECHANISM: CONSIDERATIONS FOR THE 2022-2024 PLAN

► August 18, 2021

# OUTLINE



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- ▶ **Summary of current performance incentive (PI) mechanism**
  - See the June 2020 presentation for more background and details on the current PI mechanism
- ▶ **Summary of goals for 2022-2024 Plan**
- ▶ **Considerations for a revised PI mechanism with adequate focus on the 2022-2024 goals**

# WHY PERFORMANCE INCENTIVES?



- ▶ **Performance incentives can be very effective in supporting achievement of goals and objectives**
- ▶ **Performance incentives have been effective in encouraging energy efficiency efforts in MA for decades**
  - However, those efforts haven't resulted in equitable service
- ▶ **Performance incentives are an extremely important part of the Plans; the design of the PI mechanism, the level of the incentive, and the focus on achieving the Plan goals are crucial**

# SUMMARY OF CURRENT (2019-2021 PLAN) PERFORMANCE INCENTIVE MECHANISM

- ▶ **Current performance incentives in MA are focused primarily on achieving two main goals:**
  1. Achieving higher savings and benefits (\$), in line with achieving all cost-effective energy efficiency
    - Electric energy, capacity, natural gas, oil, propane, water, non-energy impacts – all rolled up into benefits in \$
  2. Achieving the savings and benefits *cost-efficiently*, to maximize net benefits
    - Benefits minus the cost to achieve the benefits
- ▶ **Performance incentives are planned and earned at the portfolio level to achieve overall goals**
- ▶ **As a municipal aggregator, Cape Light Compact does not earn a performance incentive**

# CURRENT MA PERFORMANCE INCENTIVE: THREE COMPONENTS

## EE & Passive Demand Savings Component

Goal: Maximize savings and benefits from EE & passive demand (total EE & passive demand benefits in \$)

Rewards PAs for acquiring additional lifetime energy and demand savings and project-associated other energy and non-energy benefits

ELEC PAs: 58.7% of design level performance incentive  
GAS PAs: 61.5% of design level performance incentive

## Active Demand Savings Component

Goal: Maximize savings and benefits from active demand reduction (total active demand reduction benefits in \$)

Rewards PAs for acquiring additional demand savings through active demand reduction benefits

ELEC PAs: 4.5% of design level performance  
GAS PAs: 0%

## Value Component

Goal: Maximize value and *net* benefits (total benefits minus total costs)

Rewards PAs for seeking additional cost-effective savings and non-energy benefits, and doing so cost-efficiently

ELEC PAs: 36.8% of design level performance incentive  
GAS PAs: 38.5% of design level performance incentive

# PERFORMANCE INCENTIVES *PROPOSED IN THE 2019-2021 PLAN*

Electric Performance Incentive Totals		
Value Component (Energy Efficiency, Passive Demand, and Active Demand)	\$41.195 million	\$107 million (38.5% Value and 61.5% Savings)
Savings Component (Energy Efficiency and Passive Demand)	\$65.805 million	
Savings Component (Active Demand)	\$5 million	
Renter Component	\$2 million	
Total	\$114 million	

Gas Performance Incentive Totals		
Value Component	\$8.47 million	\$22 million (38.5% Value and 61.5% Savings)
Savings Component	\$13.53 million	
Renter Component	\$1 million	
Total	\$23 million	

\*The MA DPU did not approve the renter component.

# LOOKING FORWARD: SUMMARY OF GOALS FOR THE 2022-2024 PLAN

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- ▶ **Achieve benefits**
- ▶ **Ensure program equity**
- ▶ **Reduce greenhouse gas emissions**
  - Maximize long term greenhouse gas emissions reductions in alignment with the Secretary's GHG reduction goal as required by the Climate Act

# THE CURRENT PI MECHANISM IS NOT ADEQUATELY FOCUSED ON 2022-2024 GOALS

- ▶ **The current PI mechanism is based on one pool of benefits at the portfolio level, which does not provide adequate focus on two of the priority goals for 2022-2024.**
- ▶ **The PI mechanism should be designed in such a way to best achieve all three of the goals.**
  - Ensure equity. The PI mechanism should directly incentivize equitable investment levels in historically underserved communities. Performance incentives should be earned for achieving equitable benefits.
  - Reduce greenhouse gases. The PI mechanism should encourage program designs to *maximize* greenhouse gas reductions *in alignment with Climate Act & GWSA*.



# SUGGESTED PI CONCEPT FOR THE 2022-2024 PLAN (ELECTRIC)

- ▶ **Continue to focus on achieving benefits**
- ▶ **But going forward, use three components based on benefits to focus directly on the 2022-2024 Plan goals**
  1. Equity Benefits (benefits achieved in specific EJ communities, including from electrification)
  2. Climate Act/Electrification Benefits (benefits from heat pumps for heating, deep energy retrofits with electrification, and all-electric new construction)
  3. Remaining Portfolio Benefits (benefits achieved in the rest of the service territories that are not counted in the two benefits components above)

Gas PI mechanism would have equity and remaining portfolio components

# PI MECHANISM WITH THREE COMPONENTS WOULD BEST ACHIEVE THE THREE GOALS

- ▶ **Clear and distinct goal for each priority**
- ▶ **Separate and distinct performance incentive for each goal**
- ▶ **Threshold for each goal and PI component; incentive for each component would not begin to be earned until performance threshold is met**
- ▶ **Focus PAs on achieving all three goals, not just overall benefits wherever they could be achieved**
- ▶ **Tracking and reporting of all three goals and all three performance incentive components**

# CONSIDER REMOVING THE VALUE COMPONENT FROM THE PI MECHANISM

- ▶ **The value component disincentivizes GHG/electrification benefits and equity outcomes.**
- ▶ **The priorities for the 2022-2024 Plan will require increased investment in EJ communities and underserved customer groups, as well as in promoting/incentivizing 2050 Climate Act compliant measures such as heat pumps.**
- ▶ **These efforts may come at a higher cost per claimable benefit. Do not want to penalize PAs for prioritizing benefits that come at a higher cost, and want to reward PAs for additional benefits in these priority areas instead.**

# COMPARISON OF SUGGESTED PI CONCEPT FOR 2022-2024 PLAN VS CURRENT PI MECHANISM

## Electric PI Mechanism and Components, Current and Proposed for 2022-2024

Current PI Mechanism (Electric)		Suggested PI Mechanism for 2022-2024	
58.7%	EE & Passive Demand Benefits	Equity Benefits (EJ Community)	X%
		Climate Act/Electrification Benefits	Y%
		Remaining Portfolio Benefits	Z%
36.8%	Net Benefits		0%
4.5%	Active Demand Management		0%

} 100%

# COMPARISON OF SUGGESTED PI CONCEPT FOR GAS PROGRAMS VS CURRENT PI MECHANISM

## Gas PI Mechanism and Components, Current and Proposed for 2022-2024

Current PI Mechanism (Gas)		Suggested PI Mechanism for 2022-2024	
61.5%	EE & Passive Demand Benefits	Equity Benefits (EJ Community)	X%
		Remaining Portfolio Benefits	Z%
38.5%	Net Benefits		0%

} 100%

# THANK YOU

## Questions?

▶ August 18, 2021

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# APPENDIX

# STATUTORY GUIDANCE



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- ▶ **The Green Communities Act, in its directives on the three year statewide plans, states in Section 21 (b)(2):**  
“A plan shall include...(v) a proposed mechanism which provides performance incentives to the companies based on their success in meeting or exceeding the goals in the plan;...”



# REGULATORY GUIDANCE ON PERFORMANCE INCENTIVE DESIGN

The DPU, in its order in DPU 08-50-A, states that in reviewing the performance incentive mechanism included in an energy efficiency plan, the Department will rely on the following principles:

- ▶ Performance incentive mechanisms should be designed to encourage distribution companies to pursue all available cost-effective energy efficiency.
- ▶ The amount of funds available for performance incentive mechanisms should be kept as low as possible, in consideration of the other principles adopted herein, in order to minimize the costs to electricity and gas customers.
- ▶ Performance incentive mechanisms should be designed in such a way as to encourage energy efficiency program designs that will best achieve the Commonwealth's energy goals, particularly with regard to the goals stated in the Green Communities Act.
- ▶ Performance incentives should be based on clearly-defined goals and activities that can be sufficiently monitored, quantified and verified after the fact.
- ▶ Performance incentives should be available only for activities where the distribution company plays a distinct and clear role in bringing about the desired outcome.
- ▶ Performance incentive mechanisms should be as consistent as possible across all electric and gas distribution companies. Any deviations across distribution companies should be clearly justified.
- ▶ Performance incentive mechanisms should be created in such a way to avoid any perverse incentives.
- ▶ Any modifications to a previously approved performance incentive mechanism should be fully justified at the time they are proposed to the Department.

# THE MA PERFORMANCE INCENTIVE: DESIGN OF THE MECHANISM

## PI Pool

- The statewide design level PI pool is determined during the planning process
- 2016-2018: PI was 6.5% and 2.9% of total electric & gas PA costs, respectively
- These amounts are pre-tax

## PA allocation

- The pool is divided by planned statewide 1) EE and passive demand benefits, 2) active demand benefits (elec only) and 3) net benefits to calculate payout rates
- PI allocated to each individual PA based on its proportion of planned benefits and net benefits

## Potential PI

- Earned at the portfolio level
- Threshold – Minimum amount of benefits/net benefits needed to earn PI for each component (75% of design)
- Design – Equal to the PI pool at 100% of Plan, included in each PA's budget
- Exemplary – Maximum amount of PI, set as percentage of design (125%)

# THE MA PERFORMANCE INCENTIVE EXAMPLE: 2019-2021 ELECTRIC PI

PI Pool for electric PAs set at \$112 million: \$107m base pool and additional \$5m for active demand savings component

58.7% pool allocated to EE & passive demand savings component (\$65.8 million)

4.5% allocated to active demand savings component

36.8% allocated to value component (\$41.2 million)

Payout rate = \$65.8m / total planned EE & passive demand benefits

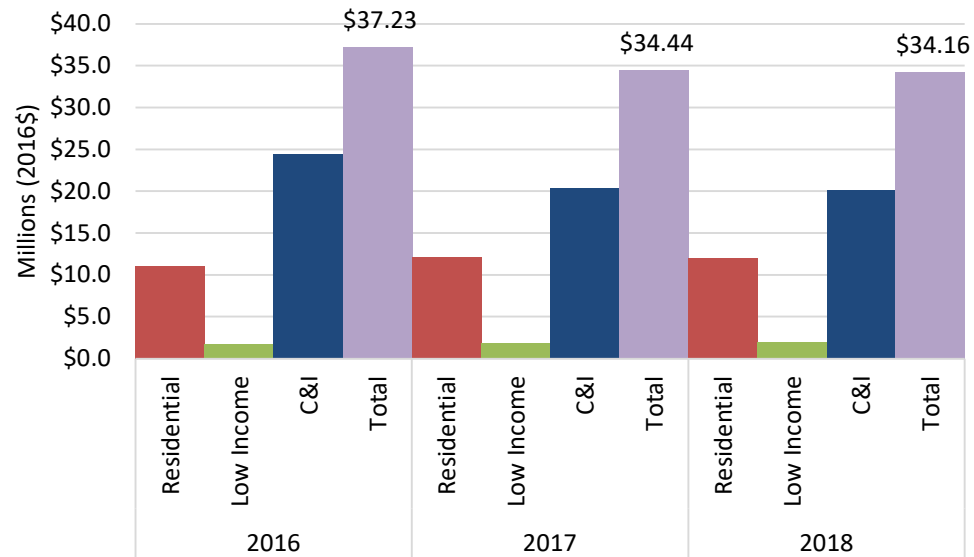
Payout rate = \$5m / total planned active demand benefits

Payout rate = \$30.7m / total planned net benefits

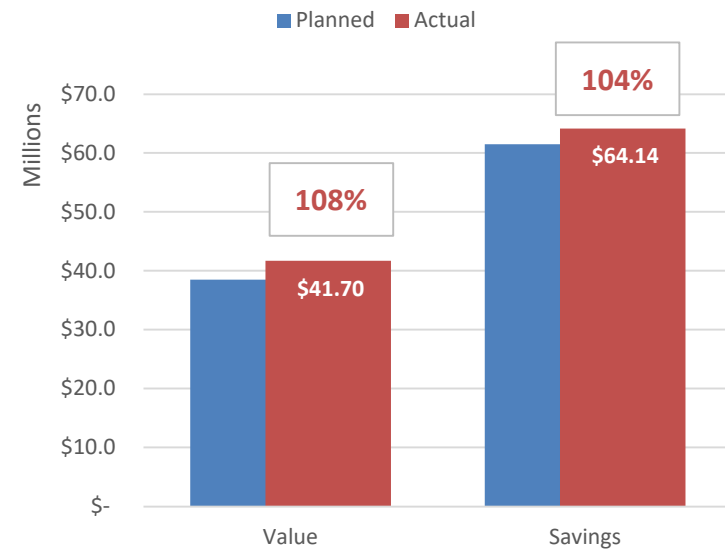
2019-2021 Energy Efficiency Performance Incentives Derivation of Electric Targets 2019-2021				
	Residential	Low Income	C&I	Total
Statewide Electric EE & Passive Demand Benefits	\$ 1,556,545,808	\$ 454,978,035	\$ 4,303,321,352	\$ 6,314,845,195
Electric EE & Passive Demand Benefits Payout Rate 2019-2021	\$ 0.0104	\$ 0.0104	\$ 0.0104	\$ 0.0104
<i>Forecasted Electric EE &amp; Passive Demand Savings Incentives</i>	\$ 16,220,270	\$ 4,741,182	\$ 44,843,548	\$ <b>65,805,000</b>
Statewide Electric Active Demand Reduction Benefits	\$ 15,188,881	\$ -	\$ 164,848,148	\$ 180,037,029
Electric Active Demand Reduction Payout Rates 2019-2021	\$ 0.0278	\$ 0.0278	\$ 0.0278	\$ 0.0278
<i>Forecasted Electric Active Demand Reduction Savings Incentives</i>	\$ 421,827	\$ -	\$ 4,578,173	\$ <b>5,000,000</b>
<b>Total Forecasted Savings Incentives</b>	\$ <b>16,642,097</b>	\$ <b>4,741,182</b>	\$ <b>49,421,721</b>	\$ <b>70,805,000</b>
Forecasted Net Benefits	\$ 899,495,649.00	\$ 261,573,172.00	\$ 3,567,154,000.00	\$ 4,728,222,821.00
Value Payout Rate 2019-2021	\$ 0.0087	\$ 0.0087	\$ 0.0087	\$ 0.0087
<b>Forecasted Value Incentives</b>	\$ <b>7,836,924</b>	\$ <b>2,278,976</b>	\$ <b>31,079,100</b>	\$ <b>41,195,000</b>
Statewide Electric Standard Savings and Portfolio Value Component	\$ 24,057,195	\$ 7,020,158	\$ 75,922,648	\$ 107,000,000
Statewide Electric Active Demand Reduction Savings Component	\$ 421,827	\$ -	\$ 4,578,173	\$ 5,000,000
<b>Statewide Design Level Performance Incentives</b>	\$ <b>24,479,021</b>	\$ <b>7,020,158</b>	\$ <b>80,500,821</b>	\$ <b>112,000,000</b>

# 2016-2018 ACHIEVED PI - ELECTRIC

Statewide Electric Earned Performance Incentive by Year & Sector

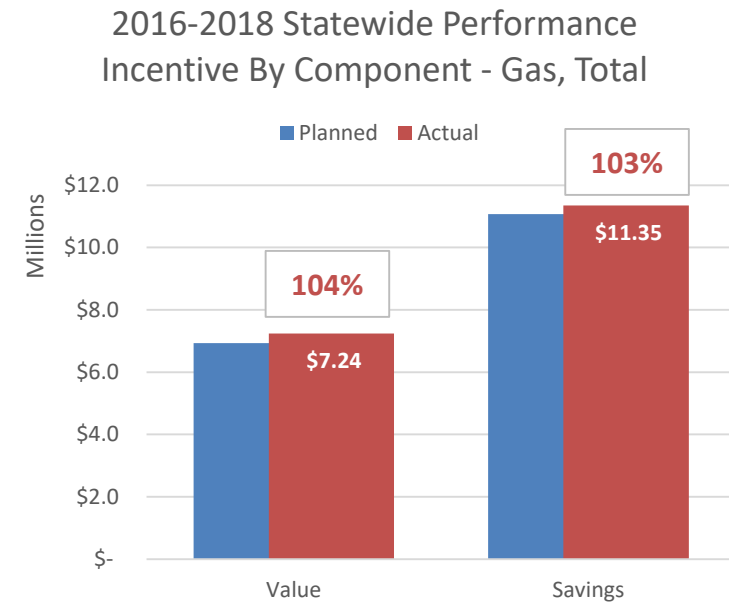
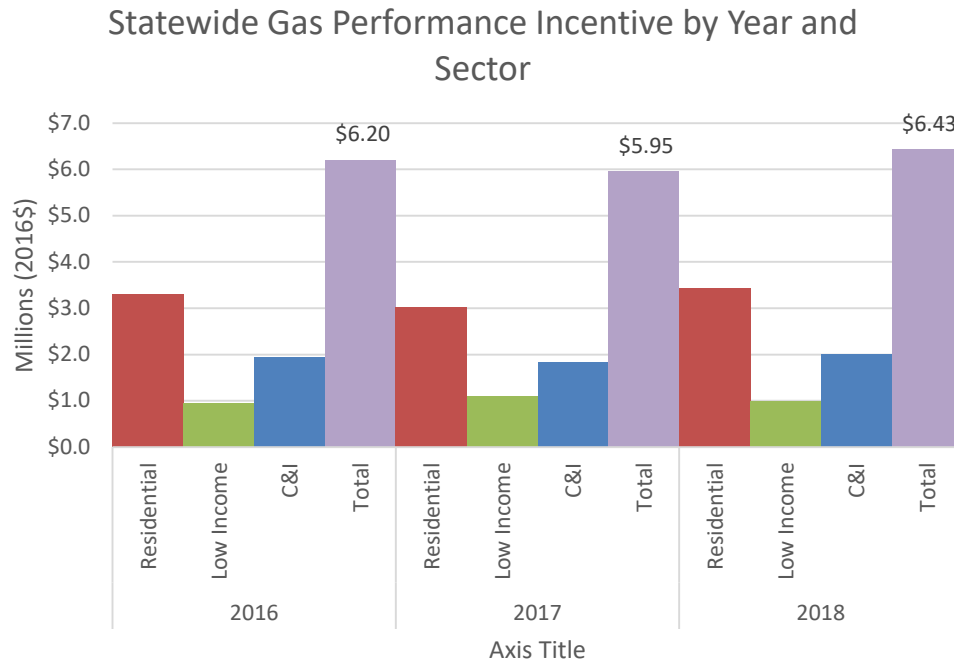


2016-2018 Statewide Performance Incentive By Component - Electric, Total



- ▶ Statewide, electric PAs earned 106% of planned performance incentive
- ▶ C&I achievements yielded 61.41% of total PI, Residential yielded 33.32% and Low Income yielded 5.28%

# 2016-2018 ACHIEVED PI - GAS



- ▶ **Statewide, gas PAs earned 103% of planned performance incentive**
- ▶ **Residential achievements yielded 52.5% of total PI, C&I yielded 31.1% and Low Income yielded 16.4%**