BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

------ In the Matter of ------

PUBLIC UTILITIES COMMISSION

Instituting a Proceeding
To Investigate Performance-
Based Regulation.

DOCKET NO. 2018-0088

DECISION AND ORDER NO. 36326

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DECISION AND ORDER

By this Decision and Order,[1] the commission establishes the regulatory principles, goals, and outcomes to guide Phase 2,

[1]The Parties to this proceeding are HAWAIIAN ELECTRIC COMPANY, INC. ("HECO"), HAWAII ELECTRIC LIGHT COMPANY, INC. ("HELCO"), MAUI ELECTRIC COMPANY, LIMITED ("MECO")(collectively HECO, HELCO, and MECO are referred to as the "HECO Companies" or the "Companies") and the DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS, DIVISION OF CONSUMER ADVOCACY ("Consumer Advocate"), an ex officio party, pursuant to Hawaii Revised Statutes ("HRS") § 269-51 and Hawaii Administrative Rules § 16-601-62(a). Additionally, the commission has granted the following entities intervenor status: CITY AND COUNTY OF HONOLULU ("C&CH"), COUNTY OF HAWAII ("COH"), BLUE PLANET FOUNDATION ("Blue Planet"), HAWAII PV COALITION ("HPVC"), HAWAII SOLAR ENERGY ASSOCIATION ("HSEA"), LIFE OF THE LAND ("LOL"), ULUPONO INITIATIVE, LLC ("Ulupono"), and DER COUNCIL OF HAWAII ("DERC"). See Order No. 35542, "Admitting Intervenors and Participant and Establishing a Schedule of Proceedings," filed June 20, 2018 ("Order No. 35542"). The commission has also granted participant status to ADVANCED ENERGY ECONOMY INSTITUTE ("AEEI"). Id.

and identifies a portfolio of specific PBR mechanisms for prioritized examination and development. In so doing, the commission outlines its vision of a comprehensive PBR framework, the details of which will be informed throughout Phase 2 by Party feedback, proposals, and positions. Consistent with the guiding principles established by this Decision and Order, the regulatory framework described herein will provide for better alignment of the HECO Companies' financial incentives with customer needs and the State's policy goals, such that customers will benefit from lower costs and greater access to renewable energy, while the HECO Companies will be rewarded for exemplary performance and high-quality service.

I.

EXECUTIVE SUMMARY

In April 2018, the commission issued Order No. 35411, initiating this proceeding to evaluate opportunities for updating the regulatory framework for the HECO Companies, in light of a transforming electric power system.[2]

The COUNTY OF MAUI was formerly an intervenor, but has since withdrawn from this proceeding. See Order No. 36252, "Granting the County of Maui's Motion to Withdraw," filed April 3, 2019.

[2]See Order No. 35411, "Instituting a Proceeding to Investigate Performance-Based Regulation," filed April 18, 2018 ("Order No. 35411").

As the commission has observed, Hawaii's electricity sector is undergoing a period of dramatic transformation. The State of Hawaii has established a 100% Renewable Portfolio Standard by 2045. In addition, thousands of customers across the State are investing in renewable energy, energy storage, and demand management technologies. The scope and scale of this transformation necessitates Hawaii's regulatory framework also evolve and adapt to the changing system.

While the State's clean energy policies are ambitious, there are several challenges with the current regulatory framework that will be addressed by the PBR mechanisms prioritized for examination and development in Phase 2 of this proceeding. In particular, under the current regulatory framework the HECO Companies lack strong incentives to control costs. Hawaii has the highest electricity prices in the nation, which exacerbates the cost of living and imposes a substantial burden on residents and businesses.

Nevertheless, there are ample opportunities to accelerate progress toward the State's goals while reducing costs to customers. Increasing the efficiency of utility operations and investments can reduce costs, while acquiring additional renewable energy (both customer-sited and grid-scale) can provide significant savings while delivering essential grid services. PBR mechanisms including the multi-year rate plan, annual revenue adjustments, and performance incentives described herein are designed to re-align the utilities' financial incentives with customer needs and focus utilities on improving performance with respect to highly valued societal goals.

In addition, the PBR mechanisms prioritized for Phase 2 are intended to streamline regulatory requirements and reduce risk for utilities and their customers. By automatically adjusting utility revenues based on an annual revenue formula and employing an "upside" and "downside" earnings sharing mechanism, utilities will have greater certainty and more timely recognition of revenues. These provisions will provide a corresponding reduction in risk for the HECO Companies' bondholders and shareholders, which will reduce the HECO Companies' cost of capital, benefiting all customers.

In sum, updating the regulatory framework will better align the HECO Companies' financial incentives with customer needs and the State's policy goals. As a result, customers will benefit from lower costs and greater access to renewable energy, while the HECO Companies will be rewarded for exemplary performance and high-quality service.

Through Phase 1 of the proceeding, the commission conducted a collaborative stakeholder process according to a three-step conceptual framework: (1) identify priority goals and outcomes to guide PBR development, (2) characterize and assess the existing regulatory framework, and (3) identify changes to regulatory components and measures necessary to attain identified goals and outcomes. This Decision & Order concludes Phase 1, identifying core elements of an updated PBR framework for the HECO Companies, and directing further development of key details in the upcoming Phase 2. As discussed herein, this framework incorporates many of the proposals presented by the Parties in Phase 1.

Phase 2 of this proceeding will focus on design and implementation of updated regulatory mechanisms to achieve the priority outcomes established herein. The PBR mechanisms to be examined and developed in Phase 2 will set a target revenue amount that encourages near-term cost savings for customers. The utility will have the opportunity to earn additional performance revenue if it achieves identified objectives, including improved customer engagement and DER performance. Earnings will be shared with utility customers in a way intended to maintain the utility's financial health, while passing cost savings on to customers.

Building on the February 2019 Staff Proposal ("Staff Proposal"),[3] the commission establishes the following

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[3]See Letter From: Commission To: Service List Re: Staff Proposal for Updated Performance-Based Regulations - Docket No. 2018-0088, In re Public Utilities Commission, Instituting a Proceeding to Investigate Performance-Based Regulation, filed February 7, 2019.

guiding principles ("Principles") suggested in the Staff Proposal to inform the development of PBR mechanisms in Phase 2:

1. **A customer-centric approach.** A PBR framework should encourage the expanding opportunities for customer choice and participation in all appropriate aspects of utility system functions, including verifiable "day-one" savings for customers.

2. **Administrative efficiency.** PBR offers an opportunity to simplify the regulatory framework and enhance overall administrative efficiency.

3. **Utility financial integrity.** The financial integrity of the utility is essential to its basic obligation to provide safe and reliable electric service for its customers and a PBR framework is intended to preserve the utility's opportunity to earn a fair return on its business and investments, while maintaining attractive utility features, such as access to low-cost capital.[4]

Likewise, the commission adopts the three regulatory goals ("Goals") and the twelve prioritized outcomes ("Outcomes") suggested in the Staff Proposal and organized as follows:

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[4]Staff Proposal at 21.

Goal	Regulatory Outcome[5]	
Enhance Customer Experience	*Traditional*	Affordability
		Reliability
	Emergent	Interconnection Experience
		Customer Engagement
Improve Utility Performance	*Traditional*	Cost Control
	Emergent	DER Asset Effectiveness
		Grid Investment Efficiency
Advance Societal Outcomes	*Traditional*	Capital Formation
		Customer Equity
	Emergent	Greenhouse Gas ("GHG") Reduction
		Electrification of Transportation
		Resilience

Consistent with these Principles, Goals, and Outcomes, Phase 2 will focus on the development of certain Revenue Adjustment Mechanisms, which determine the level of allowed utility revenues during a multi-year rate period, and Performance Mechanisms,

[5]As described in the Staff Proposal, regulatory outcomes can be distinguished between "traditional" and "emergent." "Traditional outcomes have been ingrained in utility regulations for many years and, while not immutably achieved or secured in current regulations, they are at least partially addressed." Conversely, "[e]mergent outcomes include those that need attention as Hawaii progresses towards a 100% RPS, as the electricity system becomes more renewable and distributed, and as the HECO Companies pursue opportunities for non-traditional asset investments and services." Staff Proposal at 16.

which provide for the reporting, tracking, and incentivization of utility progress towards achieving specific benchmarks or targets. Specifically, the commission prioritizes the following for Phase 2:

(A) Development of Multi-Year Rate Plan with Index-Driven Revenue Adjustment Formula

Phase 2 will focus on the development of requirements for a five-year multi-year rate plan ("MRP"), rather than maintaining the status quo triennial rate case cycle, in order to amplify cost containment incentives. The MRP will feature an attrition relief mechanism, in the form of an index-driven annual revenue adjustment ("ARA"), to provide revenue adjustments during the five-year MRP. The determination of the specific factors included in the ARA formula, set out below, will be the subject of examination and discussion in Phase 2:[6]

Annual Revenue Adjustment = (Inflation Factor) - (X-Factor) + (Z-Factor) - Customer Dividend[7]

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[6]Allowed revenues in the years of the MRP period would be adjusted by an externally-indexed revenue formula, rather than by adjustments determined by the utility's actual costs. As discussed below, the "Revenue Cap Index" referenced in the Staff Proposal and some of the Parties' filings is more appropriately characterized as a "formula" rather than a "cap," and will be referred to as a "formula," below.

[7]Where Annual Revenue Adjustment: Annual adjustment to allowed annual revenues;

Inflation Factor: Annual change according to a published inflation index;

(B) **Development of an Earnings Sharing Mechanism ("ESM")**

In order to maintain a reasonable range of utility earnings, Phase 2 will prioritize examination of an ESM that provides both "upside" and "downside" sharing of earnings between the utility and customers when earnings fall outside a commission-approved non-adjustment range or "deadband." The quantification of earnings subject to adjustment by the ESM will be comprehensive, including the contributions of target revenues, performance incentive revenues, cost trackers, and other components of overall utility revenues. An ESM, along with other mechanisms that account for exceptional circumstances, will help ensure that utility earnings do not excessively benefit or suffer from external factors outside of utility control or from unforeseen results of regulatory mechanisms. The impacts of an ESM on utility incentives for cost control and the potential effects of providing both upward and downward adjustments to maintain a range of utility earnings will be a subject of discussion in Phase 2.

X-Factor: Predetermined annual productivity factor;

Z-Factor: Factor applied (ex post) to account for exceptional circumstances not in the utility's direct control (e.g., tax law changes); and

Consumer Dividend Factor: A "stretch factor" or reduction in allowed revenues. See Section IV.B.2.

(C) Development of off-ramp provisions. Consideration shall be given to examining "off-ramp" mechanisms to provide for review of approved PBR mechanisms, pursuant to specified exceptional circumstances or conditions.

(D) Continuation of the Major Project Interim Recovery ("MPIR") Adjustment Mechanism

The commission will preserve a mechanism for interim cost recovery for exceptional projects, to the extent that it may not be feasible to appropriately provide cost recovery for all such investments during the MRP exclusively through the ARA. At this time, the commission envisions that extraordinary relief for eligible projects will continue to be governed according to the MPIR Guidelines;[8] however, the commission may consider revisions to the MPIR Guidelines in Phase 2, in order to remain consistent with the principles, goals, and outcomes of the PBR framework described herein, as well as the specific PBR Mechanisms under consideration.

(E) Development of a Portfolio of Performance Mechanisms

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[8]The MPIR Guidelines are implemented and provided as Attachment A to Order No. 34514. See In re Public Util. Comm'n, Docket No. 2013-0141, Order No. 34514, "Establishing Performance Incentive Measures and Addressing Outstanding Schedule B Issues," filed April 27, 2017 ("Order No. 34514").

In addition to incentives for cost reductions, updates to the State's regulatory framework are designed to support new utility earnings opportunities as an incentive to achieve exemplary performance and business innovation expected of the State's electric utilities. Phase 2 will prioritize development of a portfolio approach to performance mechanisms, which will include Performance Incentive Mechanisms ("PIMs"),[9] Scorecards and Reported Metrics, and Shared Savings Mechanisms ("SSMs").

(1) Performance Incentive Mechanisms ("PIMs")

Regarding PIMs, which provide financial incentives tied to identified benchmarks or targets, the commission will prioritize the development of between three to six new PIMs, addressing the Outcomes of *Interconnection Experience*, *Customer Engagement*, and *DER Asset Effectiveness*. For PIMs addressing *Customer Engagement* and *DER Asset Effectiveness*, the commission will explore PIMs with only "upside" elements; for PIMs addressing *Interconnection Experience*, the commission will explore PIMs with both "upside" and "downside" elements.

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[9]The use of the term "Performance Incentive Mechanism" in this Decision and Order refers specifically to "a metric paired with a performance benchmark/target and a financial incentive[,]" by which to "provide financial motivation for utilities to improve performance toward established outcomes, or to discourage underperformance." See Staff Proposal at 33.

(2) Scorecards and Reported Metrics

Phase 2 will prioritize the design and development of: (1) new Scorecards to track progress against targeted performance levels, addressing the Outcomes of *Interconnection Experience, Customer Engagement, Cost Control,* and *GHG Reduction;* and (2) new Reported Metrics to measure and track relevant utility performance data, addressing the Outcomes of *Affordability, Customer Equity, Electrification of Transportation, Capital Formation,* and *Resilience*, as set forth in the Staff Proposal.

While commission staff characterized SSMs as part of the "Other Regulatory Mechanisms" in the Staff Proposal, the commission will include SSMs as part of its examination of Performance Mechanisms to address the Outcomes of *Grid Investment Efficiency* and *Cost Control.*

In addition to the portfolio of PBR mechanisms described above, the commission intends for the following regulatory mechanisms to continue:

(A) Revenue Balancing Account ("RBA")

The commission will continue to utilize revenue decoupling (i.e., the RBA) to "true up" appropriately adjusted recorded revenues to an approved revenue target, thus ensuring that the utility recovers its approved target revenue, regardless of increases or decreases in energy sales or other revenue determinants. Revisions to the RBA may be considered to reduce lag and streamline the existing accrual, recovery, and reconciliation process, and to accommodate other potential regulatory changes discussed in Phase 2.[10]

(B) Continuation of Existing Tracking and Pass-Through Mechanisms

Existing cost trackers and pass-through mechanisms will continue to operate (e.g., Energy Cost Recovery Clause ("ECRC"), Purchased Power Adjustment Clause ("PPAC"), pension and other post-employment benefits tracking mechanisms, Renewable Energy Infrastructure Program ("REIP") surcharge, Demand-Side Management surcharge ("DSM Surcharge"), etc.), unless otherwise ordered by the commission.

Regarding "Other Regulatory Mechanisms," the third category of regulatory mechanisms identified in the Staff Proposal, the commission will not focus on these mechanisms at this time, though they may be addressed in the future, either later in the instant proceeding, or in other current or future dockets.

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[10]That being said, the commission retains the authority to examine and modify the RBA in other proceedings as may be appropriate under the circumstances. See In re Public Util. Comm'n, Docket No. 2008-0274, Final Decision and Order; and Dissenting Opinion of Leslie H. Kondo, Commissioner, filed August 31, 2010, at 115-116 ("the commission may review the decoupling mechanism at any time if it determines that the mechanism is not operating in the interests of the ratepayers.").

In sum, upon reviewing the record, the commission has selected for prioritized focus those PBR mechanisms that have garnered significant interest from the Parties and which appear to be mature enough for practical development during Phase 2. Recognizing the need to focus on mechanisms that are effective and can be implemented in a reasonable timeframe, the commission intends to establish a process in Phase 2 that focuses on examination of the specific Revenue Adjustment Mechanisms and Performance Mechanisms identified above. The commission will issue a subsequent Order convening Phase 2, which will contain further details about the Phase 2 process and procedural schedule. At this time, the commission intends to utilize a collaborative process that will rely upon significant party participation, and will involve working groups and periodic workshops, followed by a more formal briefing and evidentiary hearing process.

The comprehensive PBR framework to be further developed in Phase 2 is summarized in the table below:

Revenue Adjustment Mechanisms	
MRP with Indexed Revenue Adjustment	**5-Year Control Period** with **Externally-indexed Revenue Adjustment** allowing interim revenue changes pursuant to an indexed formula: **Annual Revenue Adjustment = (Inflation) - (X-Factor) + (Z-Factor) - Customer Dividend**
Earnings Sharing Mechanism (ESM)	Apply an **ESM** that provides both "upside" and "downside" sharing of earnings between the utility and customers when earnings fall outside a Commission-approved range
Major Project Interim Recovery (MPIR)	Examine the **MPIR adjustment mechanism** to determine how it can continue to provide relief for appropriate projects during the MRP consistent with other approved PBR objectives and mechanisms
Revenue Decoupling and Existing Cost Trackers	Continue to utilize **revenue decoupling** (i.e., the Revenue Balancing Account), to true up revenues to an annual revenue target and existing **cost tracking mechanisms** (e.g. PPAC, ECRC, etc.) to track and recover certain approved costs
Off-Ramps	Develop **off-ramp** mechanisms to provide for review of approved PBR mechanisms, pursuant to specified circumstances or conditions
Performance Mechanisms	
Performance Incentive Mechanisms (PIMs)	Implement a set of **PIMs** designed to help drive achievement of the following priority outcomes: *Interconnection Experience*; *Customer Engagement*; and *DER Asset Effectiveness*
Shared Savings Mechanisms	Develop **shared savings mechanisms** to address priority outcomes including *Grid Investment Efficiency* and *Cost Control*, mitigate capex bias, and reward pursuit of cost effective solutions to meet customer needs
Scorecards and Reported Metrics	Publish **Scorecards** with targeted performance levels to track progress against the priority outcomes of *Interconnection Experience, Customer Engagement, Cost Control*, and *GHG Reduction* and utilize **Reported Metrics** to highlight performance on the priority outcomes of *Affordability, Customer Equity, Electrification of Transportation, Capital Formation*, and *Resilience*

II.

PROCEDURAL HISTORY

A summary of the relevant procedural history of this proceeding is provided in Appendix A.

III.

PARTIES AND POSITIONS

A summary of the Parties' positions regarding the Staff Proposal is provided in Appendix B.

IV.

DISCUSSION

A.

Phase 1

Pursuant to HRS § 269-6 and -7, the commission has general supervision and broad investigative authority over the Companies. On April 18, 2018, the commission issued Order No. 35411 instituting this proceeding "to investigate the economic and policy issues associated with [PBR] for the [HECO] Companies."[11]

In Order No. 35411, the commission described its intent to use this proceeding "to set the foundation for a continued

[11]Order No. 35411 at 1.

successful relationship between the HECO Companies and its customers by holistically assessing and evaluating the current regulatory framework to ensure that the various regulatory mechanisms in place today are working efficiently, in concert, and as intended."[12] More specifically, the commission stated that it "seeks to examine revenue and incentive mechanisms that encourage exemplary utility performance as well as PBR elements that may, over time, result in more fundamental changes to the regulatory framework[,]" including: (A) greater cost control and reduced rate volatility; (B) efficient investment and allocation of resources regardless of classification as capital or operating expense; (C) fair distribution of risks between utilities and customers; and (D) fulfillment of State policy goals.[13]

Given the scope of this undertaking, the commission bifurcated this proceeding into two phases, in which Phase 1 would "comprehensively evaluate and assess the current regulatory framework in Hawaii to examine which incentive mechanisms and regulatory components may not be functioning as intended and to identify specific areas of utility performance that should be targeted for improvement[;]" and Phase 2 would involve "work[ing] collaboratively with stakeholders to: streamline and/or refine

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[12]Order No. 35411 at 4-5.

[13]Order No. 35411 at 5.

elements of the existing regulatory framework; develop incentive mechanisms to better address specific objectives or areas of utility performance; and explore regulatory frameworks that result in more incentive-neutral utility investment decisions between capital- and service-based solutions."[14]

Phase 1 included a significant focus on identifying priority outcomes that can guide regulatory design in Hawaii. Staff identified nearly thirty proposed outcomes at the beginning of Phase 1, which were supplemented by additional outcomes and refinements suggested by the Parties, which reflect the far-reaching importance of utility regulations, as well as associated expectations attached to utility ratemaking.[15]

After reviewing the record, staff concluded in the Staff Proposal that the Companies' financial incentives

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[14]Order No. 35411 at 5-6.

[15]See Letter From: Commission To: Service List Re: Staff Report #1 ("Goals and Outcomes for Performance-Based Regulation in Hawaii"), filed July 10, 2018, at 14-16; "County of Hawaii's Brief on Proposed Goals and Outcomes for Performance-Based Regulation in Hawaii," filed August 22, 2018, at 8-12; "Ulupono Initiative LLC's Brief on Goals and Outcomes; and Certificate of Service," filed August 27, 2018, at 25-30; "Blue Planet Foundation's Goals-Outcomes Brief; and Certificate of Service," filed August 27, 2018, at 14-21; "Division of Consumer Advocacy's Goals-Outcomes Brief," filed August 31, 2018, at 13-17; "City and County of Honolulu's Goals-Outcomes Brief; Affidavit of Georgette T. Deemer; and Certificate of Service," filed August 31, 2018, at 14-16; and "Goals-Outcomes Brief of the Hawaiian Electric Companies; Exhibits 1-4; and Certificate of Service," filed August 31, 2018, Exhibit 1 at 6-37.

are not sufficiently aligned with achieving the State's clean energy goals, increasing customer choice, and reducing the cost of energy services.[16] Building on the efforts and contributions of the Parties from Phase 1, the Staff Proposal "outlines a suggested portfolio of PBR elements . . . to effectively and holistically drive achievement of twelve priority outcomes identified for continued attention."[17] Specifically, as noted above, the Staff Proposal suggests a focused set of twelve priority Outcomes organized according to three overarching regulatory Goals to "guide the development of changes to utility regulations[:]"[18]

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[16]Staff Proposal at 2.

[17]Staff Proposal at 9.

[18]Staff Proposal at 10.

Regulatory Goal	Regulatory Outcome[19]	
Enhance Customer Experience	Traditional	Affordability
		Reliability
	Emergent	Interconnection Experience
		Customer Engagement
Improve Utility Performance	Traditional	Cost Control
	Emergent	DER Asset Effectiveness
		Grid Investment Efficiency
Advance Societal Outcomes	Traditional	Capital Formation
		Customer Equity
	Emergent	GHG Reduction
		Electrification of Transportation
		Resilience

[19]As noted above, "traditional" outcomes refer to those which have been ingrained in utility regulation for many years, while "emergent" outcomes refer to those which have been more recently developed in response to the changes in Hawaii's electric industry, including the State's 100% RPS, increasing amounts of renewable and distributed generation, and new opportunities for non-traditional asset investments and services. See Staff Proposal at 16.

In addition, the Staff Proposal suggests three guiding Principles to inform continued development of PBR regulations:

1. **A customer-centric approach.** A PBR framework should encourage the expanding opportunities for customer choice and participation in all appropriate aspects of utility system functions, including verifiable "day-one" savings for customers.

2. **Administrative efficiency.** PBR offers an opportunity to simplify the regulatory framework and enhance overall administrative efficiency.

3. **Utility financial integrity.** The financial integrity of the utility is essential to its basic obligation to provide safe and reliable electric service for its customers. A PBR framework is intended to preserve the utility's opportunity to earn a fair return on its business and investments, while maintaining attractive utility features, such as access to low-cost capital.[20]

Consistent with these Principles, Goals, and Outcomes, the Staff Proposal recommends the following portfolio of PBR mechanisms:

Revenue Adjustment Mechanisms, including a five-year MRP with an externally-indexed revenue adjustment formula, combined with an ESM, as well as continued operation of revenue decoupling, the MPIR adjustment mechanism, and other existing cost-tracking/recovery mechanisms.

[20]Staff Proposal at 21.

Performance Mechanisms, including a combination of PIMs that provide financial incentives tied to meeting specific performance benchmarks/targets, Scorecards to track progress towards identified performance benchmarks/targets, and Reported Metrics to measure and track relevant utility performance data.

Other Regulatory Mechanisms, including approaches to equalize treatment of capital expenditures and O&M expenditures ("Capex/Opex equalization"), support third-party and utility innovation, and examine platform service revenues.[21]

Together with the record developed by the Parties and staff during Phase 1, the Staff Proposal provides a strong starting point for continued development of PBR in Hawaii.

Pursuant to Order No. 35542, the commission solicited briefing from the Parties on the Staff Proposal.[22] In response, the Parties have expressed broad support for the progress made thus far in this proceeding, as well as for the suggested guiding Principles, Goals, and regulatory Outcomes in the Staff Proposal. Additionally, the Parties have indicated general interest in exploring the portfolio of PBR mechanisms set forth in the Staff Proposal.

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[21] Staff Proposal at 11-12.

[22] See Order No. 35542 at 57 and Staff Proposal.

The Parties devoted significant attention in their briefing to the specific components of the staff's proposed Revenue Adjustment Mechanisms. The Parties also expressed broad support for the Staff Proposal's suggested Performance Mechanisms, particularly development of PIMs. Regarding the proposed "Other Regulatory Mechanisms," while most of the Parties expressed general interest in discussing these further, several suggested that discussion of these mechanisms should be deferred for now, and that Phase 2 should focus on addressing Revenue Adjustment Mechanisms and Performance Mechanisms.

As this proceeding transitions from Phase 1 to Phase 2, the commission would like to express its appreciation to all of the Parties who have participated in Phase 1. Significant progress has been made and the commission acknowledges the time and resources expended by the Parties in furthering the PBR discussion to this point. As Phase 1 draws to a close, the commission is pleased with the progress made thus far, as reflected in the collaborative spirit of the discussions and the Parties' briefing. While much work remains to be done in Phase 2, the progress achieved by the Parties is commendable.

With that being said, the commission provides the following discussion to guide further efforts in Phase 2.

B.

Priority Issues For Phase 2

Upon review of the record, including the workshops, staff concept papers, Staff Proposal, and Parties' briefings, the commission will begin Phase 2 by focusing on the development of a portfolio of Revenue Adjustment Mechanisms and Performance Mechanisms, as discussed below. Other Regulatory Mechanisms, as identified in the Staff Proposal, will not be a priority focus at this time, with the exception of SSMs, which the commission will consider as part of the examination of Performance Mechanisms.

Discussion of Revenue Adjustment Mechanisms in Phase 2 will prioritize the examination and development of a five-year MRP with an ARA, presented as an externally-indexed revenue formula, and an ESM featuring both upside and downside earnings sharing and a non-adjustment deadband, as well as appropriate adjustments to the MPIR adjustment mechanism. Based on the record and expressed interest of the Parties, the commission will not focus on an Efficiency Carryover Mechanism ("ECM") in Phase 2.

Performance Mechanisms will include development of Reported Metrics, Scorecards, new PIMs to complement the existing PIMs for Reliability and Customer Service, and SSMs. Each of the above-identified categories of Performance Mechanisms will be tied to achieving specific Outcomes, as suggested in the Staff Proposal. Development of SSMs will be focused on addressing the Outcomes of

Grid Investment Efficiency and *Cost Control*. The commission intends to focus its examination of PIMs on addressing the specific Outcomes of *Interconnection Experience*, *Customer Engagement*, and *DER Asset Effectiveness*.

In addition to the mechanisms discussed above, commission envisions that the RBA and existing cost tracking and pass-through mechanisms will continue to operate, unless otherwise ordered by the commission, with potential modifications as necessitated by potential changes as a result of Phase 2.

1.

Goals, Outcomes, and Guiding Principles

The Staff Proposal identifies a set of Outcomes intended to achieve certain regulatory Goals to help guide discussion of PBR in Phase 2. The commission concurs with the proposed Goals, as well as the twelve specific Outcomes, recommended for priority consideration in the Staff Proposal. These Goals and Outcomes will provide a practical framework for examination of specific PBR mechanisms in Phase 2.

Likewise, the commission concurs with the guiding Principles of utilizing a customer-centric approach, promoting administrative efficiency, and preserving utility financial integrity, as proposed in the Staff Proposal,[23] and believes these guiding Principles are fundamental to the discussions, development, and eventual adoption of PBR mechanisms. These principles serve to remind all Parties of important characteristics and considerations to apply in the design and evaluation of each candidate PBR mechanism, so that the resulting mechanisms are practical, feasible, and effectively address the identified Goals and Outcomes. The commission notes, however, that the guiding Principles are not an exclusive list of criteria by which proposed mechanisms may ultimately be evaluated; all identified aspects and impacts of proposed mechanisms will be considered carefully by the commission in making determinations in this proceeding.

2.

Revenue Adjustment Mechanisms

Phase 2 will focus on the following Revenue Adjustment Mechanisms and/or features, consistent with the discussion below:

Development of a MRP with an index-driven revenue formula. Phase 2 will examine an extended five-year period between general rate cases during which the Companies' revenues will be

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[23] See Staff Proposal at 21.

determined by a combination of an ARA (in the form of an indexed revenue formula), PIMs, and cost trackers.[24]

As noted in the Staff Proposal, "a 5-year rate plan represents a balanced approach"[25] that is largely consistent with the Parties' positions. While Blue Planet proposed an eight-year MRP and the Consumer Advocate proposed an automatically-renewing "evergreen" provision for the MRP, both proposals incorporated various more-frequent review periods consistent in duration with the Staff Proposal's five-year timeline.[26] Only the HECO Companies stated explicitly that they do not support a five-year MRP;[27] however, it should be noted, the Companies have also stated that, at this time, they do not support any MRP duration beyond the current three-year interim period provided by the decoupling triennial rate case cycle.[28]

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[24]See Staff Proposal at 25.

[25]Staff Proposal at 25.

[26]See Blue Planet SOP at 6-8 and RSOP at 12; and CA SOP at 21-22 and RSOP at 20-21.

[27]More specifically, the HECO Companies state they "do **not** support extending the period between rate cases (i.e., the control period) beyond three years at this time[,]" but provide a bulleted list of circumstances under which the Companies "agree that consideration can be given to extending the control period for the [MRP] to four years[.]" HECO RSOP at 49 (emphasis in bold in original; underlining added).

[28]Initially, the Companies indicated that they would be open to considering a four-year MRP, provided that certain conditions applied. See HECO SOP at 18-19. However, in their Reply Statement of Position, the Companies state that they do not support extending

The commission believes that the MRP period should be extended beyond three-years. Three years is the current "stay out" period between general rate cases for the HECO Companies. As the electric utility industry in Hawaii transitions to include additional PBR elements, it is anticipated that periods in between "rate cases" will increase, in line with the development of additional PBR mechanisms that provide appropriate incentives to manage costs. The development of a five-year MRP represents a reasonable step towards transitioning to a longer control period between rate cases, providing the utility with an operational environment similar to a competitive market structure. This structure can provide incentives to manage costs over a longer period of time; if the Companies can lower costs during the control period, they will increase their earnings.

The commission will utilize the existing or pending "rate cases," respectively, in setting their target revenues for the initial MRP. This is staff's recommended position[29] and is supported by the Consumer Advocate and Blue Planet.[30] The commission agrees that, on the whole, this is the most straightforward and efficient means of setting initial target

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the period between rate cases beyond three years at this time. HECO RSOP at 49.

[29]Staff Proposal at 27.

[30]See CA SOP at 25; and Blue Planet SOP at 10.

revenues and rates, and would conserve the significant resources that would otherwise be expended by the commission, the Companies, the Consumer Advocate, and any intervenors or participants in an alternative consolidated "target revenue-setting proceeding," as proposed by the Companies.[31] As the Companies are currently on a triennial rate case cycle, their rates are frequently "refreshed," such that the rates in effect for any of the given Companies at the time the initial MRP is placed into effect will reflect a reasonable baseline upon which to establish the MRP target revenues (which will be subsequently adjusted by the ARA).

During the MRP, utility revenues will be subject to an ARA in which revenues will be adjusted by the following index-driven revenue formula:

Annual Revenue Adjustment = (Inflation Factor) - (X-Factor) + (Z-Factor) - Customer Dividend[32]

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[31]See HECO SOP at 18.

[32]Where: Annual Revenue Adjustment: Annual adjustment to allowed annual revenues;

Inflation Factor: Annual change according to a published inflation index;

X-Factor: Predetermined annual productivity factor;

Z-Factor: Factor applied (ex post) to account for exceptional circumstances not in the utility's direct control (e.g., tax law changes); and,

Consumer Dividend Factor: A "stretch factor" or reduction in allowed revenues.

The determination of the specific factors of the indexed revenue formula will be the subject of discussion in Phase 2.

The commission notes that the indexed revenue formula presented in this Decision and Order differs slightly in appearance from the formula in the Staff Proposal. Specifically, the commission's formula establishes an "Annual Revenue Adjustment," rather than a "Revenue Cap Index."[33] This difference is intended to clarify that the ARA is not a "cap," but an index-driven formula for determining revenues. The concept of a revenue "cap" is derived from the existing decoupling RAM and RAM Cap, which the MRP and ARA will replace. As currently contemplated, the ARA would be used to establish the target revenues during the MRP period, rather than "capping" revenues determined by some other means. This distinction is informative in shifting thinking away from the existing "RAM-plus-RAM Cap" interim relief structure and towards the ARA formula.

The commission observes that the Parties have generally expressed support for a MRP with an indexed revenue formula. In many respects, the Staff Proposal represents the ongoing evolution of the decoupling mechanisms first initiated in Docket No. 2008-0274,[34] with many of the salient features updated

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[33]Staff Proposal at 26.

[34]See In re Public Util. Comm'n, Docket No. 2008-0274 (commission investigation into establishing decoupling mechanisms

to reflect the Parties' and commission's experiences and developments in regulatory and energy policy. In this sense, the MRP can be seen as a more sophisticated regulatory mechanism that seeks to consolidate and streamline existing mechanisms.

While various Parties have expressed concerns with the revenue formula, much of this concern pertains to the specific components in the formula, rather than whether a formula should be used. While the Companies have opposed the inclusion of a Customer Dividend,[35] the commission is not persuaded that it should be excluded from the revenue formula. Consistent with the Principle of adopting a customer-centric approach, including a Customer Dividend will help ensure that "day-one" savings for utility customers are realized (in this regard, the Companies have acknowledged that their proposals "would not result in immediate savings to customers").[36]

Likewise, consistent with the Principle of ensuring utility financial integrity, in addition to other considerations in the design and examination of the ARA, the commission will consider measures to reduce lag in implementing the accrual and/or

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for the HECO Companies); and In re Public Util. Comm'n, Docket No. 2013-0141 (commission re-examination of Companies' decoupling mechanisms).

[35]See HECO SOP at 29 and HECO RSOP at 30-31.

[36]HECO RSOP at 30.

collection of approved revenues.[37] Regulatory lag has consistently been raised by the Companies as a concern for certain mechanisms (e.g., the RBA's approximately five-month lag between January and the June effective date). Establishing target revenues with an automatic annual adjustment formula will mitigate this concern.

Due to development of a MRP, as well as other revenue adjustment mechanisms under consideration, the commission recognizes that there will likely be a need to examine changes to the Companies' rate design structure during the MRP. Such rate design revisions are expected to be revenue neutral (i.e., not affecting the revenues set by the ARA) and will be addressed in a separate proceeding.

Development of an ESM. Consistent with the Staff Proposal, the ESM is intended to "share" amounts of utility earnings that deviate substantially from a predetermined reasonable amount. The ESM developed in Phase 2 should contemplate both "upside" and "downside" elements, though not necessarily "symmetrical" (i.e., mirror-image) amounts. In addition, the ESM should feature a "deadband" or "collar" around the baseline level of earnings in which the ESM would provide no adjustment.

Similar to the MRP with indexed revenue formula, the commission notes that there is general agreement of the Parties

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[37]See HECO SOP at 28 and HECO RSOP at 28-29.

regarding exploring an ESM in Phase 2.[38] In addition, the Companies have already developed and implemented the asymmetrical Earnings Sharing Revenue Credit Mechanism ("ESRCM") in the first decoupling proceeding, Docket No. 2008-0274, which provides experience upon which to build in Phase 2. Furthermore, a well-designed ESM will maintain the utility's financial integrity and reduce risk to the HECO Companies' bondholders and shareholders, which will have a corresponding reduction in the cost of capital, benefiting all customers.

Development of off-ramp provisions. Consideration shall be given to examining "off-ramp" mechanisms to provide for review of approved PBR mechanisms, pursuant to specified circumstances or conditions.

Revisions to the MPIR adjustment mechanism. The MPIR adjustment mechanism will continue to provide revenues for extraordinary projects as approved by the commission, above revenues established by the ARA.

The MPIR adjustment mechanism currently serves as a case-by-case revenue cap "relief" mechanism for major utility capital projects. Requests for MPIR relief are currently governed

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[38]See CA RSOP, Exhibit 1. As reflected in Exhibit 1 of the Consumer Advocate's RSOP, only Blue Planet opposes the development of an ESM. Notwithstanding Blue Planet's opposition, the commission is not persuaded that an ESM should be removed from consideration in Phase 2.

by the MPIR Guidelines, with application, review, and approval of an MPIR request provided in the context of review under General Order No. 7.[39]

Based on the Parties' briefing, continuation of the MPIR adjustment mechanism, in general, does not appear to be controversial[40] (although the commission notes that several Parties have advocated for modifications to its applicability and scope). The commission agrees that preserving the MPIR adjustment mechanism for extraordinary projects is appropriate, to the extent that it may not be feasible to effectively address all such investments during the MRP period exclusively through an externally-indexed revenue formula.[41] At this time, the commission envisions that MPIR relief will still be governed according to the MPIR Guidelines; however, it may be necessary to consider revisions to the MPIR Guidelines in Phase 2, in light of the PBR framework's Principles, Goals, and Outcomes, as well as the other PBR Revenue Adjustment Mechanisms and Performance Mechanisms under consideration. This also presents an opportunity to address capital bias that may be perpetuated through the current MPIR adjustment mechanism and explore how the MPIR may be used to

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[39]See Order No. 34514, Attachment A.

[40]See CA RSOP, Exhibit 1.

[41]See Staff Proposal at 30.

address incentives regarding capital expenditures and operational expenditures.

In reviewing the Parties' briefing, it appears that there may be some confusion as to the contemplated role of the MPIR adjustment mechanism within the Staff Proposal's suggested PBR Framework.[42] Accordingly, the commission clarifies that during Phase 2, the Parties should consider relief provided under the MPIR adjustment mechanism as distinct from potential relief under the "Z-Factor" component of the MRP indexed revenue formula. "Z-Factor" events are intended to address unforeseen events and are considered in determining the amount of allowed revenue in accordance with the ARA formula, whereas the MPIR Guidelines are used to prospectively seek relief for planned "eligible projects" in addition to revenue determined by the indexed revenue formula.

Although the commission does not prioritize the RBA or existing cost trackers and pass-through mechanisms for development in Phase 2, the commission's vision of a PBR framework does include continuation of these elements, as discussed below:

Continuation of the RBA. The RBA will continue to operate in its existing role, though revisions may be necessary to accommodate other changes (e.g., extension of an interim rate

[42]See CA RSOP at 27 (stating that "Blue Planet appears to conflate the Z-Factor with the MPIR Mechanism . . . .").

period beyond three years, timing and process for review of adjustments, and possible design changes given the development of Revenue Adjustment Mechanisms). Based on the Parties' briefing, this does not appear to be controversial.[43]

Continuation of existing cost tracking and pass-through mechanisms. Existing cost trackers and pass-through mechanisms will continue to operate (e.g., ECRC, PPAC, pension and other post-employment benefits tracking mechanisms, REIP surcharge, DSM Surcharge, Public Benefits Fee surcharge, etc.). The commission observes that the Parties are generally in agreement on this issue, or do not voice any opposition.[44] The commission has previously stated that such mechanisms may be subject to future revision,[45] and may explore revisions as the discussions regarding other PBR mechanisms develop in Phase 2.

Although the Staff Proposal proposes development of an ECM, the commission does not intend to prioritize development of an ECM during Phase 2. While the Staff Proposal suggests an ECM

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[43]See CA RSOP, Exhibit 1.

[44]See CA RSOP, Exhibit 1. In this regard, to the extent the C&CH raises concerns that "fossil fuel costs are passed through the [PPAC]," see C&CH SOP at 11, the commission notes that such pass through is done pursuant to HRS § 269-16.22.

[45]See e.g., In re Hawaiian Elec. Co., Inc., Docket No. 2016-0328, Decision and Order No. 35545, filed June 22, 2018, at 69 (stating that revisions to the ECRC's fuel-risk sharing mechanism may be subject to further examination and review in Docket No. 2018-0088).

to allow the utility to benefit from efficiency gains through multiple MRP periods, regardless of when those savings were actually made,[46] this issue was not actively addressed in the Parties' briefing and does not appear to be of immediate concern. Given the complexity of the issues already set for consideration in Phase 2, the commission does not believe it is necessary to expressly consider this issue, at this time.

3.

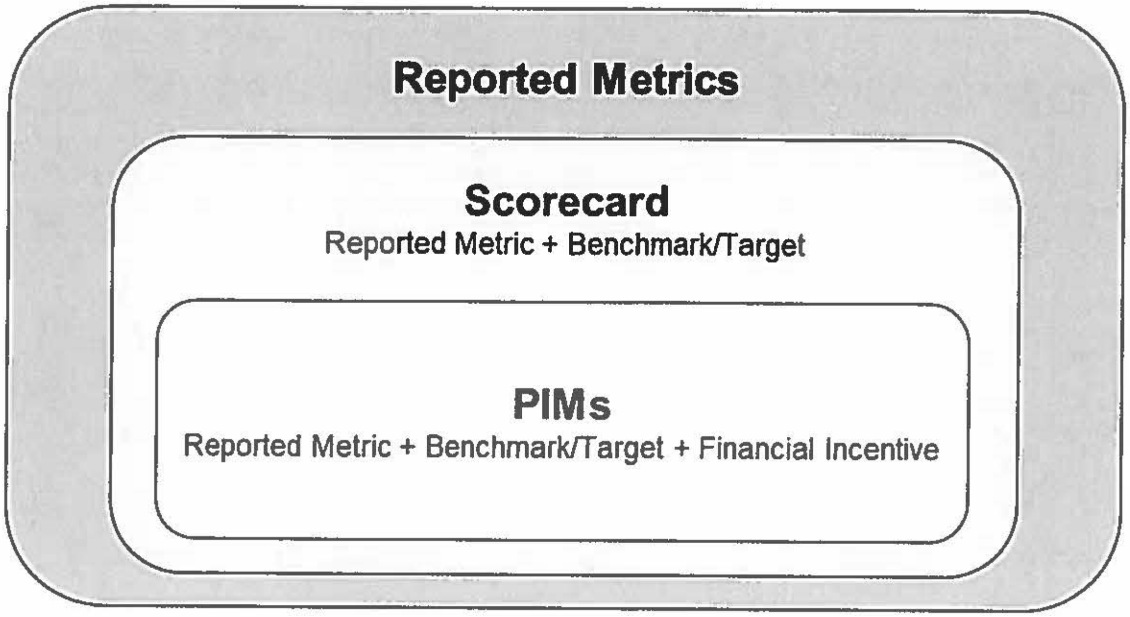
Performance Mechanisms

The commission will prioritize development of a portfolio of Performance Mechanisms in Phase 2 to provide more targeted incentives in support of particular Outcomes that may not be sufficiently addressed by Revenue Adjustment Mechanisms alone.

In the Staff Proposal, commission staff describe Performance Mechanisms using a hierarchical framework of Reported Metrics, Scorecards, and PIMs, summarized in the illustration reproduced below:[47]

[46]Staff Proposal at 24 and 29.

[47]Staff Proposal at 32, Figure 6.



As reflected in the illustration above, the three identified categories of Performance Mechanisms are organized in a hierarchical fashion, with each subsequent tier including additional components to track, evaluate, and, in the case of PIMs, reward and/or penalize achievement of benchmarks or targets, in order to incentivize performance. Determining whether a specific Outcome should be encouraged through development of a Reported Metric, Scorecard, or PIM depends on several considerations, including the nature of the underlying metric(s).

The Staff Proposal sets out a table with suggested Performance Mechanisms for each of the twelve Outcomes, along with proposed metrics for each Outcome.[48] The commission will pursue this approach as a guide for discussion of Performance Mechanisms

[48]Staff Proposal at 35-37.

in Phase 2. In addition, the commission adopts the descriptions for Reported Metrics, Scorecards, and PIMs set forth in the Staff Proposal to guide their development in Phase 2. Each of these Performance Mechanisms is discussed in greater detail below.

Reported Metrics. As stated in the Staff Proposal, metrics serve as a standard unit of measurement used to assess performance regarding identified Outcomes.[49] As further noted in the Staff Proposal:

> Metrics can be designed as activity-, program-, and outcome-based. Different types of metrics may be appropriate for a specific indicator or measurement, and a mix or blended portfolio of metric types may be warranted in the Hawaii context. . . .
>
> The simple act of tracking and reporting metrics can incent utilities toward stronger performance by using transparency as a regulatory tool. Reporting standalone metrics can also be useful to inform ongoing market evaluation and policy assessments, and serve as the foundation for developing Scorecards or PIMs . . . .
>
> Finally, Reported Metrics may help to inform the development of revenue adjustment mechanisms as well as to track the efficacy of all regulatory mechanisms over time.[50]

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[49]See Staff Proposal at 31.

[50]Staff Proposal at 32-33 (footnotes omitted).

The Staff Proposal also suggests "five principles for metric design," including that metrics should:

(1) reflect desired outcomes;

(2) be clearly defined;

(3) be quantifiable through reasonably available data;

(4) be easily interpreted; and

(5) be easily verified.[51]

The Staff Proposal further suggests developing Reported Metrics to measure the following Outcomes: *Affordability*, *Customer Equity*, *Electrification of Transportation*, *Capital Formation*, and *Resilience*.[52]

None of the Parties has objected to the development and use of Reported Metrics as part of developing Performance Mechanisms in Phase 2. The DER Intervenors[53] have suggested that the data collected through Scorecards and Reported Metrics should be translated into "dashboard tools that can be used to educate and inform the public and competitive service providers about system conditions and trends, and where appropriate, utilize the data and information gathered through

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[51]Staff Proposal at 38.

[52]See Staff Proposal at 35-37.

[53]Based on their decision to jointly file a Statement of Position and Reply Statement of Position, HPVC, HSEA, and DERC are referred to, collectively, as the "DER Intervenors" in this Decision and Order.

scorecards and reported metrics into new PIMs."[54] The Companies also support developing metrics so that appropriate data can be collected and assessed, but raise the issue of cost recovery, stating that "the cost and resource commitment necessary to accomplish reporting must be considered and addressed[,]"[55] and support Blue Planet's proposal of including such costs in base rates.[56]

Upon review, the commission finds the Staff Proposal's suggested development of Reported Metrics to be reasonable and will focus on development of activity-, outcome-, and program-based Reported Metrics aligned with the specific Outcomes as set forth in the Staff Proposal. The commission likewise adopts the Staff Proposal's "five principles for metric design" to further guide the Parties' discussions in Phase 2.

Scorecards. As described in the Staff Proposal, a Scorecard represents the next level in the Performance Mechanism hierarchy, effectively combining a Reported Metric with a specific benchmark or target, which may "encourage better achievement of regulatory outcomes than through Reported Metrics alone."[57]

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[54]DER Intervenors SOP at 20.

[55]HECO RSOP at 73.

[56]HECO RSOP at 75 (citing Blue Planet response to HECO/BP-16).

[57]See Staff Proposal at 33.

Staff proposed using Scorecards to measure and evaluate the Outcomes of: *Interconnection Experience*, *Customer Engagement*, *Cost Control*, and *GHG Reduction*.[58]

None of the Parties raised objections to Scorecards in their briefing. The Consumer Advocate affirmatively supports a "full, robust discussion of scorecards in Phase 2[,]" noting that they "provide more pressure to improve performance than reported metrics and do not impose the costs or risks to customers that PIMs impose."[59] Similarly, as noted above, the DER Intervenors support translating information gathered through Reported Metrics and Scorecards into dashboard tools.[60]

As with the Staff Proposal's Reported Metrics, the commission likewise finds that the suggested Scorecards represent a valuable opportunity to begin tracking and measuring the Companies' performance in certain areas and supports their development in Phase 2. Accordingly, the commission will focus development of Scorecards for the specific Outcomes set forth in the Staff Proposal.

PIMs. PIMs, as discussed in the Staff Proposal, represent the third level in the Performance Mechanism hierarchy,

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[58]See Staff Proposal at 35-37.

[59]CA RSOP at 45.

[60]DER Intervenors SOP at 20.

adding a financial incentive and/or penalty to the utility's achievement of a specific benchmark or target, as measured by a Reported Metric.[61] "Through the use of financial award or penalty, a PIM can more strongly promote achievement of a prioritized outcome than a performance target or reported metric."[62]

Concomitantly, the development of PIMs requires careful consideration and analysis of the underlying metrics and targets, to ensure that the expected performance, as well as the amount of financial incentives and/or penalties, are reasonable, and that the utility is not exposed to inappropriate financial gain or risk. Anticipating these concerns, the Staff Proposal proposes several "PIM-specific design considerations," as set forth below.[63]

> (1) Setting a quantitative standard for performance. The benchmarks/targets, and especially any associated financial incentives, should focus on promoting the achievement of only superior performance or penalizing poor performance.
>
> (2) Benefit-cost analyses should inform the development of PIMs. PIMs should be designed to reflect some sharing of net benefits. This assessment of net benefits sets an upper limit on the value of the PIM, with further

[61]See Staff Proposal at 33.

[62]Staff Proposal at 33-34.

[63]In contrast to the guiding Principles discussed above, which are intended to influence the development of PBR mechanisms in general, the "PIM-specific design considerations" are, as the title implies, intended to guide the development of PIMs, specifically, within the larger context of a PBR framework.

discussion about the appropriate sharing percentages between ratepayers and the utility shareholders.

(3) PIMs should shift an appropriate amount of performance risk to the utility in exchange for longer-term regulatory certainty and perhaps incentive compensation. Entrepreneuralism on the part of the utility should be rewarded, but PIMs should also ensure the risk and reward is comparable to that of firms in a free and competitive market.

(4) "Double recovery" of PIMs that achieve the same or similar outcome should be minimalized (for example, a program-based [Demand Response] PIM and an outcome-based PIM for improved system load factor or peak demand reduction). Care will need to be taken to ensure that the design of PIMs is coordinated so that multiple utility activities are not double-counting the same benefits and receiving reward for the same outcome(s).

(5) Consider designing individual PIMs so that "outstanding" performance on an individual PIM may be rewarded by additional earnings, while maintaining overall earnings caps for all PIMs.

(6) Consider the appropriate time frame for PIMs. PIMs can be designed to span multiple years to allow time for utility actions to take effect.[64]

[64]Staff Proposal at 38-39.

The commission agrees with the PIMs framework set forth in the Staff Proposal and summarized above. While details regarding the specific metrics, targets, and degree of financial exposure will require further discussion, the commission adopts the Staff Proposal's "PIM-specific design considerations" to assist the Parties in their discussion. Based on the commission's review of the Parties' briefing, it does not appear that any Party has any objections to the development of PIMs. Much of the Parties' briefing regarding Performance Mechanisms has been largely supportive of this approach, although the specific details of PIMs are expected to be the subject of robust discussion in Phase 2.

Consistent with the Staff Proposal, the commission will prioritize the development of three to six new PIMs addressing the specific Outcomes of *Customer Engagement*, *DER Asset Effectiveness*, and *Interconnection Experience*.[65] The existing backstop PIMs addressing *Reliability* (i.e., SAIDI and SAIFI) and *Customer*

[65]Staff Proposal at 34. Although the Staff Proposal also recommends exploring PIMs for *Reliability*, the commission notes that there are already existing "backstop" PIMs for this Outcome. While these PIMs, based on SAIDI and SAIFI metrics, may be further examined in Phase 2, the commission is not inclined to focus on developing new *Reliability* PIMs at this time.

Service (i.e., Call Center Performance), while continuing to operate, will not be counted toward this target.[66]

In light of the expected time and resources necessary to develop PIMs, which includes the development of appropriate Reported Metric(s), Benchmark(s)/Target(s), and financial incentives, the commission will prioritize development of PIMs to achieve the specific Outcomes of *Interconnection Experience*, *Customer Engagement*, and *DER Asset Effectiveness*, consistent with the Staff Proposal. The commission has elected to focus on developing PIMs for these specific Outcomes for the following reasons:

Interconnection Experience: as noted by staff, as the number of Distributed Energy Resources ("DER") and community-based renewable energy ("CBRE") projects increases, there is a corresponding need to "ensure interconnection is efficient and seamless."[67] In addition, interconnection has been challenging for grid-scale renewable energy projects, which are expected to continue to be essential for achieving the State's clean energy goals. As Hawaii relies more on increasing levels of DER and

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[66]C.f., HECO RSOP at 68 (requesting that their existing PIMs be included as part of the overall number of PIMs developed in Phase 2).

[67]Staff Report #3, "Prioritized Outcomes, Regulatory Options, and Metric Development for Performance-Based Regulation in Hawaii," filed November 14, 2018 ("Staff Report #3"), at 25.

grid-scale renewable energy projects, ensuring that there is a reliable and timely interconnection process to integrate these resources onto the Companies' grids is critical. Providing financial incentives for exemplary performance with respect to this Outcome is intended to facilitate the interconnection of renewable resources going forward.

Customer Engagement: the commission concurs with staff's assessment that "[u]tilities need to adequately and equitably facilitate a move toward an inclusive, customer-oriented electric grid, as customers evolve from passive consumers of a commodity (kWh) to active participants in a dynamic market for grid services."[68] This not only involves tracking customer participation in the Companies' new program offerings, such as DER, CBRE, and Demand Response, but also developing effective outreach tools to educate customers about their electricity consumption and how they can better manage it, whether it be through energy-saving practices, or taking on a more active role as a market participant or as an energy and grid services provider.

In a monopolistic market, customer engagement may be lower than in a competitive market. A PIM for the *Customer Engagement* Outcome will focus attention on interaction and experience with the customer, which should be a

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[68]Staff Report #3 at 26.

vital part of an electric utility's business model. A PIM should also incent the utility to leverage its relationship with its customers to collaboratively work towards increasing renewable energy in a manner that serves both utility and customer.

DER Asset Effectiveness: as discussed above, as well as in other commission proceedings, the HECO Companies have experienced an unprecedented level of DER adoption in recent years, offering an increasing number of evolving and sophisticated DER program options, including Net Energy Metering ("NEM") and NEM+, time-of-use ("TOU"), Customer Self Supply ("CSS"), Customer Grid Supply ("CGS") and CGS+, and Smart Export.[69] As observed by staff, "there is an emergent and increasing need to ensure that these resources play an integral role in the functioning and balancing of the network."[70] The commission agrees. As the suite of DER options becomes more robust and complex, it is critical that utilities manage these new resources in an efficient manner, such that these resources are maximized while also promoting safe, reliable, electrical service.

Similar to the *Interconnection* Outcome discussed above, developing a PIM(s) for this Outcome will incent greater and more meaningful utilization of DERs and other customer-sited assets.

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[69]See generally, Docket No. 2014-0192.

[70]Staff Proposal #3 at 26.

For PIMs addressing *Customer Engagement* and *DER Asset Effectiveness*, the commission will focus on developing "upside-only" PIMs, providing the HECO Companies with financial rewards based on exemplary performance. These are relatively new areas of analysis for the Companies, and this approach will ensure that any metrics and corresponding targets used in designing this initial set of PIMs are appropriate indicators of utility progress in achieving desired outcomes before exposing the utilities to financial penalties. However, regarding PIMs for *Interconnection Experience*, the commission will consider both rewards and penalties, given that this has been an area of ongoing concern for the commission and there is likely to be sufficient historical information available to establish reliable metrics and targets.

Regarding the financial exposure of potential PIMs to be discussed in Phase 2, although the Staff Proposal suggests a collective financial exposure of 150-200 basis points for new PIMs,[71] the commission will not decide on a range of financial exposure at this time and requests further discussion this issue in Phase 2.

SSMs. SSMs, as described in the Staff Proposal, "reward a utility for reducing expenditures from a baseline or

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[71]Staff Proposal at 34.

projection by allowing it to retain a portion of savings as profit while returning the remainder to ratepayers."[72]

The Parties' reaction to the proposed development of SSMs is mixed, with the Companies, Ulupono, and the DER Intervenors expressing support, and the Consumer Advocate and Blue Planet contending that SSMs would not be needed if other proposed Revenue Adjustment Mechanisms are adopted.[73]

The commission believes SSMs provide an opportunity to incent the Companies to improve performance with respect to the priority Outcomes of *Grid Investment Efficiency*, by addressing utility capital bias, and *Cost Control*, by rewarding the Companies for pursuit of cost effective solutions to meet customer needs. Furthermore, the commission observes that the Companies have recent experience with a similarly-structured PIM in their efforts to competitively procure grid-scale renewable energy generation,[74]

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[72]Staff Proposal at 40.

[73]See CA RSOP, Exhibit 1.

[74]See In re Hawaiian Elec. Co., Inc., Hawaii Elec. Light Co., Inc., and Maui Elec. Co. Ltd., Docket No. 2017-0352, Order No. 35405, "Establishing a Performance Incentive Mechanism for Procurement in Phase 1 of the Hawaiian Electric Companies' Final Variable Requests for Proposals," filed April 6, 2018 ("Order No. 35405") at 11 (establishing a "shared-savings performance incentive for Phase 1 of the Companies' procurement effort . . . . based on an 80% customer/20% utility split of the savings from each PPA, compared to benchmarks established by considering recent low-cost renewable energy projects, up to a cap of $3,500,000.").

which can inform discussions in Phase 2. Thus, although categorized as an "Other Regulatory Mechanism" in the Staff Proposal, the commission believes SSMs are ripe for consideration as part of the larger examination into Performance Mechanisms.

4.

Other Regulatory Mechanisms

While generally supported by most of the Parties, it does not appear that the "Other Regulatory Mechanisms" suggested in the Staff Proposal reflect similar levels of development and focus as the Revenue Adjustment Mechanisms and Performance Mechanisms in the Parties' briefings. This is not wholly unexpected, as the current regulatory framework already incorporates limited forms of Revenue Adjustment Mechanisms (e.g., triennial rate case cycle, RAM Cap, MPIR, asymmetrical ESRCM) and Performance Mechanisms (e.g. PIMs for SAIDI, SAIFI, and Call Center Performance).

Upon considering the record and circumstances, the commission will not focus on "Other Regulatory Mechanisms" at this time, and will begin Phase 2 by focusing on the development of Revenue Adjustment Mechanisms and Performance Mechanisms, as discussed above.

As noted by a number of Parties, Phase 2 will involve a difficult transition from discussing theoretical proposals to transforming them into viable, practical regulatory tools. As the Parties and commission work towards addressing these issues in an organized, comprehensive, and collaborative manner, it will be critical to narrow the focus of the proceeding to conserve resources and focus on developing those mechanisms which are most likely to be effective, feasible, and implemented within a reasonable timeframe, while deferring discussion on other proposals until a time when Party and commission resources are available to fairly and meaningfully consider them.[75]

Consequently, "Other Regulatory Mechanisms" may be addressed in the future, either later in the instant proceeding, or in other current or future dockets. In particular, the commission encourages the HECO Companies to work with stakeholders on developing a proposed framework for an expedited review process for innovative pilot projects. As suggested in the Staff Proposal, "[i]n the nearer term, . . . the development of an expedited pilot implementation process . . . could result in several leading-edge projects without the limitations of traditional program approval."[76] The commission agrees that

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[75]See e.g., CA RSOP at 2-3.

[76]Staff Proposal at 49.

exploring an expedited implementation process for pilots that test new technologies and programs is desirable. While time and resources preclude such exploration in the PBR proceeding at this time, the commission encourages the HECO Companies to work with stakeholders towards developing a proposed framework that can be reviewed and examined by the commission in a separate proceeding, in parallel with Phase 2.

C.

Phase 2

Following this Decision and Order, the commission will issue a convening order for Phase 2 discussing the processes and procedures to guide the Parties' discussions and development of the record for Phase 2. At this time, the commission envisions beginning discussion with focused working groups interspersed with workshops facilitated by third-parties, followed by a more formal briefing period and hearing.

V.

ORDERS

THE COMMISSION ORDERS:

1. The Principles, Goals, and Outcomes set forth in the Staff Proposal are established for use in Phase 2.

2. During Phase 2, the commission intends to focus discussion on the development of specific Revenue Adjustment Mechanisms and Performance Mechanisms, as set forth above.

3. The commission will subsequently issue an order providing details regarding Phase 2.

DONE at Honolulu, Hawaii MAY 23 2019.

PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

By ______________________
James P. Griffin, Chair

By ______________________
Jennifer M. Potter, Commissioner

By ______________________
Leodoloff R. Asuncion, Jr., Commissioner

APPROVED AS TO FORM:

____
Mark Kaetsu
Commission Counsel

2018-0088.ljk

APPENDIX A

PROCEDURAL HISTORY

On April 18, 2018, the commission issued Order No. 35411, initiating this proceeding to investigate PBR to explore new opportunities for evaluating and updating the State's utility regulatory framework in light of a transforming electric power system.[77]

In Order No. 35411, the commission set out a two-phase approach to guide the docket process, with Phase 1 intended to examine the current regulatory framework to identify specific areas of focus for PBR development, and Phase 2 intended to focus on refinement and/or modification to the existing regulatory framework in those specific areas identified in Phase 1.[78]

Pursuant to Order No. 35411, motions to intervene or participate without intervention were accepted through May 8, 2018.[79] On June 20, 2018, commission issued Order No. 35542, which addressed the motions and adopted a procedural schedule. The commission granted intervenor status to the C&CH, COH, COM, Blue Planet, HPVC, HSEA, LOL, Ulupono, and DERC, as well as participant status to AEEI. Order No. 35542 also set forth a

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[77]See Order No. 35411 at 1-6.

[78]See Order No. 35411 at 52-57.

[79]See Order No. 35411 at 57-58.

procedural schedule for Phase 1, which contemplated a series of three technical workshops, with accompanying briefing, as well as the filing of formal Statements of Position and information requests.[80]

On July 10, 2018, in preparation for Technical Workshop #1, commission staff submitted a concept paper, entitled "Goals and Outcomes for Performance-Based Regulation in Hawaii," to provide the Parties with an initial set of proposed goals and outcomes to which to respond. In addition, the concept paper provided Parties with a discrete proposal upon which to provide feedback, and to help facilitate a focused discussion around the appropriate set of goals and outcomes at the workshop.

On July 23 and 24, 2018, the commission held Technical Workshop #1, facilitated by Rocky Mountain Institute ("RMI"), to: (1) review PBR efforts in other jurisdictions, including tools and processes used; (2) build a shared understanding of the potential for PBR in Hawaii and a planned approach for the PBR proceeding; and (3) discuss potential regulatory goals and outcomes for PBR in Hawaii.

From August 22, 2018 through August 31, 2018, Party briefs on "Goals and Outcomes" were filed to provide specific

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[80]See Order No. 35542 at 57.

feedback on Staff-proposed regulatory goals and outcomes, as well as to propose alternatives.

On September 18, 2018, in advance of Technical Workshop #2, staff submitted a second concept paper, entitled "Assessing the Existing Regulatory Framework in Hawaii," to describe how current regulations function, and to offer a revised set of regulatory outcomes for the Parties' consideration.

On September 27, 2018, the commission held Technical Workshop #2, facilitated by RMI, which focused on: (1) deepening collective understanding of existing regulatory mechanisms; (2) exploring how existing structures are or are not supporting achievement of particular regulatory outcomes; and (3) strengthening Parties' and stakeholders' capacity to collaborate in this work.

On October 25, 2018, the Parties submitted their briefs on "Regulatory Assessment," informed by discussions at Technical Workshop #2, to provide insight on the effectiveness of the current regulatory framework by examining how individual regulatory mechanisms help, hinder, or have no impact on the achievement of identified outcomes.

On November 14, 2018, in advance of Technical Workshop #3, Staff submitted a third concept paper, entitled "Prioritized Outcomes, Regulatory Options, and Metric Development for Performance-Based Regulation in Hawaii," to:

(1) suggest a prioritized set of outcomes to guide the remainder of this proceeding; (2) review key issues and possible approaches for metric design; (3) illustrate certain considerations for mapping prioritized outcomes to corresponding categories of regulatory mechanisms; and (4) explore whether it may be appropriate and beneficial to tailor separate regulatory mechanisms for each individual segment of the power system value chain.

On November 28, 2018, the commission held Technical Workshop #3, facilitated by RMI, to: (1) identify refinements to existing mechanisms that support prioritized outcomes; (2) consider new regulatory approaches to support prioritized outcomes not well met by existing regulations; and (3) explore common approaches and principles for metric design.

On January 4, 2019, the Parties filed their briefs on "Metrics," providing suggestions for metrics to support tracking of progress made toward achieving future outcomes. Parties also suggested appropriate regulatory mechanisms to best address Staff's prioritized outcomes.

On February 7, 2019, Staff submitted its Staff Proposal, which proposed a suggested portfolio of PBR mechanisms for the Parties' consideration and comment.

On March 8, 2019, pursuant to Order No. 35542 and the specific deadlines set forth in the Staff Proposal, the Parties submitted their Statements of Position in response to the Staff Proposal.[81]

On March 18, 2019, the Parties exchanged information requests with respect to each other's Statements of Position. On March 22 and 25, 2019, the Parties filed their respective responses to information requests.

On April 3, 2019, the commission issued Order No. 36252, which granted the County of Maui's Motion to Withdraw, filed on March 6, 2019.

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[81]See "Life of the Land's Comments on Staff Proposal; and Certificate of Service," filed March 8, 2019 ("LOL SOP"); "City and County of Honolulu's Statement of Position; Affidavit of Roy K. Amemiya, Jr.; and Certificate of Service," filed March 8, 2019 ("C&CH SOP"); "County of Hawaii's Statement of Position on the Staff Proposal for Updated Performance-Based Regulations; and Certificate of Service," filed March 8, 2019 ("COH SOP"); "Ulupono Initiative LLC's Statement of Position; and Certificate of Service," filed March 8, 2019 ("Ulupono SOP"); "Hawaii PV Coalition, Hawaii Solar Energy Association and Distributed Energy Resource Council of Hawaii Statement of Position on Staff Proposal for Updated Performance Based Regulation; and Certificate of Service," filed March 8, 2019 ("DER Intervenors SOP"); "Statement of Position of the Hawaiian Electric Companies; Exhibits 'A' through 'H;' and Certificate of Service," filed March 8, 2019 ("HECO SOP"); "Division of Consumer Advocacy's Statement of Position on Staff Proposal for Updated Performance-Based Regulations," filed March 8, 2019 ("CA SOP"); and "Blue Planet Foundation's Statement of Position; and Certificate of Service," filed March 8, 2019 ("Blue Planet SOP"). AEEI did not file a Statement of Position.

On April 4 and 5, 2019, the Parties filed their respective Reply Statements of Position.[82]

Pursuant to the procedural schedule for Phase 1, as set forth in Order No. 35542 and the Staff Proposal, no further procedural steps are contemplated and Phase 1 is ready for decision making.

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[82]See "Life of the Land's Reply Statement of Position; and Certificate of Service," filed April 4, 2019 ("LOL RSOP"); "County of Hawaii's Reply Statement of Position on the Staff Proposal for Updated Performance-Based Regulations; and Certificate of Service," filed April 4, 2019 ("COH RSOP"); "Hawaii PV Coalition, Hawaii Solar Energy Association and Distributed Energy Resource Council of Hawaii Reply Statement of Position on Staff Proposal for Updated Performance Based Regulation; and Certificate of Service," filed April 5, 2019 ("DER Intervenors RSOP"); "Ulupono Initiative LLC's Reply Statement of Position; and Certificate of Service," filed April 5, 2019 ("Ulupono RSOP"); "Reply Statement of the Hawaiian Electric Companies; Exhibits 'A' through 'F;' and Certificate of Service," filed April 5, 2019 ("HECO RSOP"); "Blue Planet Foundation's Reply Statement of Position; and Certificate of Service," filed April 5, 2019 ("Blue Planet SOP"); and "Division of Consumer Advocacy's Reply Statement of Position on Staff Proposal for Updated Performance-Based Regulations," filed April 5, 2019 ("CA RSOP"). AEEI did not submit a Reply Statement of Position.

APPENDIX B

PARTIES AND POSITIONS

The summary of the Parties' positions in response to the Staff Proposal are organized around the specific PBR mechanisms suggested in the Staff Proposal.

A.

Revenue Adjustment Mechanisms

1.

MRP Length

The Consumer Advocate, the HECO Companies, Ulupono, Blue Planet, the DER Intervenors, the C&CH, and the COH all comment on the MRP suggested in the Staff Proposal and propose different approaches for designing and implementing a MRP.

Ulupono and the C&CH support staff's proposed five-year control period.[83]

Blue Planet proposes a longer control period with: "(1) a default duration of eight years; (2) a mid-period review or 'look in' provision for the Commission to check progress under the

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[83]*See* Ulupono SOP at 7; and C&CH SOP at 9.

PBR regime after four years; and (3) a mid-period 'off-ramp' or reset option at the end of five years."[84]

The Consumer Advocate does not support a "scheduled expiration" of the MRP after five years.[85] According to the Consumer Advocate, "any new MRP [should] be initiated as a complete suspension of traditional [cost of service regulation ('COSR')] rate cases for the indefinite future . . . until revised by future Commission Order."[86] The Consumer Advocate maintains that staff's proposed expiration of the MRP after five years "should not imply any expectation of a return to COSR" and argues that resuming COSR after the initial MRP term expires would be "inherently problematic" for several reasons.[87] Instead, the Consumer Advocate recommends an evergreen provision under which "an unstructured MRP Review Window" would occur "around year five[,]" which would involve a "comprehensive review of PBR and the [MRP]" and could result in "a variety of outcomes informed by actual utility performance, none of which require resumption of COSR rate cases[.]"[88]

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[84]Blue Planet SOP at 6-7. A table illustrating Blue Planet's MRP proposal is also reflected in pages 7-8 of its SOP.

[85]CA SOP at 17.

[86]CA SOP at 17-18.

[87]CA SOP at 18-20.

[88]CA SOP at 21.

The HECO Companies have concerns about extending the period between rate cases and recommend that only incremental changes to the existing multi-year rate plan be adopted.[89] Provided that a number of conditions are met, the Companies initially offered qualified support for a four-year control period,[90] but subsequently clarified that this pertains to an unspecified "reasonable time beyond Phase 2[.]"[91]

The COH does not take an explicit position regarding the length of a MRP control period, but supports increasing the period to a length greater than three years.[92]

The DER Intervenors do not oppose MRP as a regulatory mechanism, but emphasize the need for data and analysis before implementation.[93]

2.

Determination Of Initial MRP Target Revenues

The Consumer Advocate and Blue Planet support the Staff Proposal's recommended approach of utilizing existing base

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[89]See HECO SOP at 4.

[90]See HECO SOP at 16 and 18-19.

[91]HECO RSOP at 49.

[92]See COH SOP at 5.

[93]See DER Intervenors SOP at 14.

rates to set target revenues for the initial MRP.[94] Ulupono also supports this approach, but stresses that "[i]t is imperative that the initial rates take into account anticipated utility capital expenditures for grid modernization, resiliency measures and other similar expenditures."[95]

The HECO Companies recommend that the initial base rates for a modified MRP be set either in the next set of triennial rate cases (i.e., utilizing a 2019 test year for HELCO, 2020 test year for HECO, and 2021 test year for MECO) or in a consolidated proceeding for all three utilities.[96]

The DER Intervenors caution that "utilizing existing revenue requirements and rates could further hinder the potential effectiveness of these mechanisms for the initial five-year term by maintaining status quo assumptions about utility investment plans and revenue requirements."[97] While the DER Intervenors acknowledge that using existing revenue requirements provides a certain level of administrative efficiency, they contend that it could "further delay the opportunity to restructure return on

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[94]See CA SOP at 25; and Blue Planet SOP at 10.

[95]Ulupono SOP at 14.

[96]HECO SOP at 33.

[97]DER Intervenors SOP at 15.

equity regimes to better reflect risk."[98] In this regard, the DER Intervenors do not support implementing a MRP at this time, maintaining instead that "the near-term focus of PBR should be on achieving emergent outcomes[,]" such as developing a "PBR framework facilitating the emergence of sustainable competitive markets, particularly DER markets."[99]

3.

MRP Attrition Relief Mechanism (Indexed Revenue Formula)

The Consumer Advocate, Blue Planet, Ulupono and the C&CH support the replacement of the traditional RAM and RAM Cap mechanism with a simplified ARA and generally agree with the proposed formula set forth in the Staff Proposal:

Revenue Cap Index: (Inflation) - (X-Factor)+(Z-Factor) - Consumer Dividend Factor[100]

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[98]DER Intervenors SOP at 15.

[99]DER Intervenors SOP at 16; see also, DER Intervenors RSOP at 5-6 (recommending that the commission "[d]elay any extension of the existing 3-year [MRP] . . . until the Commission has high confidence, based on actual performance by the utilities under the new PBR regime, that the utilities will use the additional regulatory flexibility provided under an extended [MRP] to meet the goals and objectives that such flexibility is intended to facilitate.").

[100]See CA SOP at 23; Blue Planet SOP at 5; Ulupono SOP at 12-13; and C&CH SOP at 9-10.

That being said, there is disagreement among the Parties as to specific details for each of these formulaic elements. For example, some Parties favor using the Gross Domestic Product Price Index as an index for inflation,[101] while others suggest the Consumer Price Index,[102] and others[103] prefer a "Hawaii-specific" measure of inflation.

The Consumer Advocate, Ulupono, Blue Planet, and the C&CH support the inclusion of a productivity "X-Factor" in the new revenue cap formula, as well as the exogenous "Z-Factor."[104] Regarding the Consumer Dividend, the Consumer Advocate and Blue Planet voice support,[105] but Ulupono disagrees on the grounds that it is unnecessary in light of the proposed ESM, which can achieve similar customer benefits while utilizing more reliable metrics (i.e., ROE).[106]

In contrast, the HECO Companies maintain that the existing RAM Cap "already undercompensates the Companies" and that

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[101]See CA SOP at 23.

[102]See C&CH SOP at 10.

[103]See Ulupono SOP at 12-13.

[104]See CA SOP at 23-24, Ulupono SOP at 13, and Blue Planet SOP at 5.

[105]See CA SOP at 23; and Blue Planet SOP at 5.

[106]See Ulupono RSOP at 27. Blue Planet's countering arguments against the ESM are discussed below.

adopting an ARA that is "more conservative than the very conservative RAM Cap plus MPIR Mechanism currently in place would undercut the financial integrity guiding principle."[107] Instead, the Companies recommend simplifying the RAM calculation, eliminating the lag in the implementation of the annual RAM adjustment, and modifying the RAM Cap escalator "to better recognize the impact of needed baseline plant additions[,]" as well as clarifying the scope of the MPIR adjustment mechanism within this new ARA structure.[108]

The DER Intervenors suggest that "certain data, risk analysis, and other information necessary to develop a revenue cap index, productivity factor, and other elements of the MRP and revenue cap are not currently known or must be better understood before implementing these mechanisms as a main component of PBR at this stage."[109] Accordingly, the DER Intervenors do not agree that the MRP with ARA is "the best means to accomplish Hawaii's policy goals at this early stage of PBR[,]" and will "create unnecessary regulatory risk due to uncertainty over how the utilities would exercise the high degree

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[107]HECO SOP at 4-5.

[108]HECO SOP at 5.

[109]DER Intervenors SOP at 14.

of regulatory flexibility that would likely be granted to them under this structure."[110]

4.

Earnings Sharing Mechanism

The Consumer Advocate, the HECO Companies, Ulupono, and the C&CH support the development of an ESM with upside and downside financial risk/reward.[111]

The Consumer Advocate asserts that the ESM incents financial performance while providing any needed support for the utilities' financial integrity.[112] The Consumer Advocate maintains that to avoid complicated revenue and cost classification disagreements, the ESM "should be calculated to include all PIM related rewards, penalties and the related costs incurred by the utilities to achieve performance, so that ESM goals are not undermined by selectively excluded incentives, penalties, or new platform revenues."[113] The Consumer Advocate also recommends a commission-defined non-sharing deadband around the ESM.[114]

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[110]DER Intervenors RSOP at 9.

[111]See CA SOP at 33; HECO SOP at 32; Ulupono SOP at 17; and C&CH SOP at 11.

[112]See CA SOP at 33.

[113]CA SOP at 27 (emphasis in original).

[114]CA SOP at 28.

Ulupono also supports Staff's proposed ESM and observes that it appears "substantially similar" to the "ESM-X" suggested by Ulupono earlier in this proceeding, which also includes upside and downside elements and a non-sharing deadband around the target ROE.[115] Additionally, like the Consumer Advocate, Ulupono recommends that the ESM be inclusive of all PIM financial incentives and penalties.[116]

The HECO Companies note that they already have what represents an asymmetric ESM (i.e., the ESRCM) and support the development of a symmetrical ESM (i.e., featuring both an upside and a downside) with a non-sharing deadband, but caution that the cost sharing must remain within an acceptable ROE level.[117] Additionally, the Companies note that a number of Parties have relied on the ESM to support a MRP with ARA and argue that this over-emphasizes the impact of the ESM, which, the Companies contend, would still be insufficient to make up for lost revenues expected under an inflation indexed revenue cap.[118]

The DER Intervenors support the Staff Proposal's recommendation for an ESM, "but believe that ESMs should be viewed

[115]See Ulupono SOP at 15-16.

[116]Ulupono SOP at 17.

[117]See HECO SOP at 31-32.

[118]See HECO RSOP at 62-63.

as a transition mechanism toward revenue models based purely on performance[.]"[119] According to the DER Intervenors, "[w]hile ESMs mitigate the uncertainty associated with early-stage PBR implementation, they are not a desirable end-point for market development[,]" and, if used, "should be narrowly structured to measure earnings associated with specific, trackable, and well-understood functions[,]" to address uncertainty and "gaming risks."[120]

Conversely, Blue Planet does not support a long-term ESM.[121] Blue Planet expresses concern that an ESM "will seriously handicap the PBR regime" and suggests that "ROE would pose particular problems as a metric for an ESM."[122] In particular, Blue Planet notes that the "sharing" element of the ESM may dull the utility's incentives to cut costs, since a portion of their savings will be shared with ratepayers.[123] Furthermore, Blue Planet states that earnings sharing inherently requires a comparison between actual and "allowed" earnings, "a classic artifact of traditional COSR," and, thus, an ESM in the context of a

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[119]DER Intervenors SOP at 18.

[120]DER Intervenors SOP at 18.

[121]See Blue Planet SOP at 14-16.

[122]Blue Planet SOP at 14-15.

[123]Blue Planet SOP at 14.

PBR framework "will work to anchor or pull regulation back to COSR."[124] As noted above, Blue Planet prefers using the "Consumer Dividend" element of the revenue cap formula to provide customer savings, which, Blue Planet maintains, achieves a similar result while "avoid[ing] bringing COSR back into the picture and relinking investment and revenues."[125] Similarly, Blue Planet contends that the ESM's use of ROE as a metric "reconnects the link between earning calculations and rate base, rate-of-return that PBR is supposed to break[,]" thereby perpetuating the "capital bias under COSR by another name."[126]

The Staff Proposal also suggests an Efficiency Carryover Mechanism ("ECM") to allow utilities to benefit from efficiency gains throughout and across various MRP periods and thus avoid the potential "loss" of savings made near the end of a given MRP period.[127] None of the Parties appear to have responded to this favorably, either by observing that this issue should be addressed

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[124]Blue Planet SOP at 14-15.

[125]Blue Planet SOP at 16.

[126]Blue Planet SOP at 15. In this regard, Blue Planet recommends that financial metrics other than ROE, such as changes in depreciation, earnings per share, or earnings yield, should be used to inform adjustments to the revenue cap formula. Id. at 17.

[127]Staff Proposal at 24.

through the proper operation of other PBR elements, or ignoring the issue completely.

5.

Off-Ramp Mechanisms

The Parties appear to be in general agreement that it is reasonable to develop "off-ramps" to review and possibly adjust the PBR framework ahead of schedule. That being said, each Party has a different opinion as to what circumstances should be required.

The Companies provide general support for the development of off-ramp provisions "reflecting the need for appropriate provisions to provide relief or adjustments to the specific provisions of PBR elements."[128] Similarly, the COH offers general support for developing off-ramp provisions, but with a "two to three year check-in examination . . . to understand the interplay between PBR mechanisms in addition to the individual impact of the mechanisms."[129]

The Consumer Advocate supports development of off-ramps, but states that it "does not support Phase 2 determination of

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[128]HECO SOP at 12, 19, and 33.

[129]COH SOP at 9.

Off-Ramp Provisions that would trigger a COSR rate case."[130] According to the Consumer Advocate, the ESM should serve as the primary means to backstop the Companies' financial performance and, in the event the ESM proves unable to support the utility's financial integrity, "alternative forms of relief other than reversion to COSR rate cases" should be considered.[131]

Ulupono concurs with the need to develop "off-ramp mechanisms," but supports limiting them to "significant changes to the utility's financial health, including its credit rating[,]" and proposes a tiered approach, under which modifications to the PBR framework are considered, such as PIMs and Revenue Adjustment Mechanisms, before terminating the MRP and ARA in favor of a general rate case.[132]

Blue Planet states that "[a]ny 'off-ramp' provisions . . . should be limited to circumstances so extraordinary that they must necessarily override the performance-based principles of PBR."[133] According to Blue Planet, such "extraordinary circumstances" would exclude poor utility performance as well as excess profits, to allow the PBR Framework to provide necessary

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[130]CA SOP at 33.

[131]CA SOP at 33-34.

[132]See Ulupono SOP at 22-23.

[133]Blue Planet SOP at 18.

"upside" and "downside" flexibility, absent evidence of "grave miscalculation or misconduct unrelated to performance."[134]

The C&CH supports the development of off-ramps, but states that "the inclusion of off-ramp provisions should also be matched by a willingness and ability to implement more innovative, comprehensive reforms such as a GHG Reduction PIM."[135]

6.

Decoupling

The Consumer Advocate, the HECO Companies, Blue Planet, and Ulupono support the continuation of the Companies' revenue decoupling (i.e., the RBA).[136] In addition, to incent the *Electrification of Transportation* Outcome, Ulupono suggests that "a small fraction of utility revenues that are generated from the sale of electricity at [non-utility owned] [Electric Vehicle] charging stations could be excluded from the existing decoupling RBA."[137]

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[134]Blue Planet SOP at 18.

[135]C&CH SOP at 12.

[136]See CA SOP at 26; HECO SOP at 6; Blue Planet SOP at 11; and Ulupono SOP at 14-15.

[137]Ulupono SOP at 30.

The DER Intervenors state that while decoupling may "mitigate[] some utility bias or *disincentive* against energy efficiency, DER adoption, or other customer-based actions that reduce utility kWh sales and/or slow load growth[,] . . . . it does not provide an *incentive* for utilities to, for instance, invest in energy efficiency or facilitate greater DER adoption."[138] Ultimately, the DER Intervenors maintain, the revenue requirement to which the decoupling target revenues are tied "is a creature of cost-of-service regulation[,]" and thus, while "revenue decoupling may be an appropriate revenue adjustment mechanism to include in a near-term PBR framework[,] . . . . the mechanism should be replaced with PIMs, capex/opex equalization mechanisms, innovation incentives, and other mechanisms once revenue requirement and revenue earning opportunity assumptions are determined according to PBR framework assumptions."[139]

7.

The MPIR Adjustment Mechanism

As noted above, the MPIR Guidelines and associated MPIR adjustment mechanism is a relatively recent development and

[138]DER Intervenors SOP at 17 (emphasis in original).

[139]DER Intervenors SOP at 17.

provides the Companies with the ability to seek interim cost recovery for approved projects above the current RAM Cap.

The Consumer Advocate, Ulupono, Blue Planet, and the COH contend that the MPIR Guidelines should be modified to ensure that the MPIR adjustment mechanism does not perpetuate capital bias.[140] The Consumer Advocate recommends considering "clarifying modifications to the MPIR Guidelines . . . in order to eliminate the possible appearance that the capital bias may be perpetuated through the MPIR."[141] For example, the Consumer Advocate suggests modifications to explicitly clarify that the MPIR adjustment mechanism may be used to recover both capitalized and expenses costs, but may not be used to recover "routine replacements of existing plant assets or expenses that would have been incurred but for the Major Project[.]"[142]

Blue Planet recognizes that the revenue cap regime must accommodate potential contingencies of large expenditures (such as storm damage or major infrastructure projects), but expresses concern that the MPIR adjustment mechanism could become an "overused exception or backdoor that can defeat the cost-control

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[140]CA SOP at 31; Ulupono SOP at 9; Blue Planet SOP at 12; and COH SOP at 9.

[141]CA SOP at 32.

[142]CA SOP at 32.

function of the revenue cap regime."[143] Blue Planet suggests that an effective Integrated Grid Planning ("IGP") process "would help establish or update the foundation for the PBR revenue cap regime, which would in turn help ensure that resort to the MPIR would truly be limited to unexpected capital expenditures arising from exogenous events."[144] In this regard, it appears that Blue Planet considers the role of the MPIR adjustment mechanism to exclusively address unforeseen events, and not planned or pre-approved major projects.

Ulupono also suggests using an IGP process to coordinate MPIR projects, but recommends limiting MPIR recovery during the MRP to only those projects included in an approved IGP plan "to the extent possible."[145] However, Ulupono acknowledges that "an exception to this requirement could involve use of the MPIR mechanism in conjunction [with] the Z-Factor to address 'uncontrolled exogenous events' that affect the utility's cost."[146] Additionally, Ulupono recommends that any relief afforded by the

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[143]Blue Planet SOP at 12.

[144]Blue Planet SOP at 12.

[145]Ulupono RSOP at 13.

[146]Ulupono SOP at 9 n.14.

MPIR not be authorized above the revenue cap "to the extent reasonably possible[.]"[147]

The COH states that it would "prefer to see the phase-out of the MPIR altogether," but "recommends that the Commission only allow capex projects that show clear cost-benefit results, closely monitor HECO's usage of the MPIR over the next five years, and *ex post facto* compare the costs of MPIR projects with the results of the HECO Companies' future non-wires alternatives solicitations."[148]

The HECO Companies support continuation of the MPIR adjustment mechanism within the new PBR Framework, but request further clarification as to its scope.[149] In particular, the Companies seek confirmation that "new (as opposed to replacement, relocated or restored) facilities, such as substations, transmission lines and structures, and distribution facilities in new developments" would be eligible for MPIR recovery, maintaining that such inclusion "would be necessary to properly design a multi-year rate plan."[150] The Companies further state that the MPIR is necessary to accommodate "lumpy" major

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[147]Ulupono SOP at 11.

[148]COH SOP at 9.

[149]HECO SOP at 30-31.

[150]HECO SOP, Exhibit G at 7.

capital projects that do not otherwise easily comport with an indexed revenue cap rate plan.[151] The Companies reiterate their argument that the existing regulatory cost recovery framework that utilizes a RAM Cap with an MPIR adjustment mechanism is inadequate to meet the Companies' financial needs and maintain that if either the MPIR adjustment mechanism or revenue cap is made more restrictive, this will require a corresponding increase to the other to preserve the Companies' financial health.[152] Finally, in response to Ulupono's proposal to limit MPIR recovery to projects pre-approved through the IGP process, the Companies counter that this "is unnecessary, since the Commission can decide in the [General Order No.] 7/MPIR proceeding, whether the major project in question is consistent with any rate plan or integrated grid plan in effect."[153] The Companies also disagree with Ulupono's proposal to implement the MPIR adjustment mechanism in a way that "severely limits or prevents excursions above the revenue cap."[154]

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[151]See HECO RSOP at 34.

[152]See HECO RSOP at 35 and Exhibit C at 3-4.

[153]HECO RSOP at 37.

[154]HECO RSOP, Exhibit C at 6.

8.

Existing Cost Tracking Mechanisms

The Companies currently have a number of cost tracking mechanisms in place that provide for the recording and recovery of actual costs incurred for various utility expenses. The most significant are the PPAC, under which the utility recovers its purchased power expenses, and the ECRC, under which the utility recovers its fuel expenses, subject to a limited amount of risk sharing.[155] In addition, the Companies have cost tracking mechanisms for their pension and other post-employment benefits (collectively, "pension and OPEB trackers"), the Renewable Energy Infrastructure Projects Surcharge, the Demand Response Adjustment Clause, the Public Benefit Fund surcharge, and the Integrated Resource Planning/Demand-Side Management program ("IRP/DSM Surcharge").

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[155]The ECRC was preceded by the Energy Cost Adjustment Clause ("ECAC"). In HECO's last general rate case, Docket No. 2016-0328, the commission, among other things, effectively transformed the ECAC into the ECRC and included a risk-sharing component under which HECO and its ratepayers share 2% of the financial risk associated with fossil fuel prices, up to ±$2.5 million annually. See In re Hawaiian Elec. Co., Inc., Docket No. 2016-0328, Decision & Order No. 35545, filed June 22, 2018. A similar mechanism was implemented for MECO in its last general rate case as well, Docket No. 2017-0150 (2% fuel price risk, up to ±$500,000 annually). See In re Maui Elec. Co., Ltd., Docket No. 2017-0150, Decision and Order No. 36219, filed March 18, 2019.

The Consumer Advocate, the HECO Companies, and Ulupono support the continuation of the PPAC and ECRC, although the Consumer Advocate recommends an increased number of periodic reviews of these mechanisms.[156]

Blue Planet proposes increasing the ECRC's fuel risk-sharing amount.[157] Similarly, Ulupono recommends reviewing the ECRC's fuel-risk adjustment and considering the related benefits of adopting an RPS PIM.[158] The C&CH voices "concerns with maintaining the ECAC or ECRC and to the extent that fossil fuel costs are passed through the [PPAC]."[159] Blue Planet, Ulupono, and the C&CH support adjustments to the ECRC.[160]

Regarding the Companies' other cost trackers, the Consumer Advocate notes that "[a]dditional trackers exist . . . that were not mentioned [in the Staff Proposal] but should also be

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[156]See CA SOP at 14 and 31; HECO SOP at 6; and Ulupono SOP at 14-15 and 18.

[157]Blue Planet SOP at 12.

[158]Ulupono SOP at 18.

[159]C&CH SOP at 11.

[160]Blue Planet SOP at 11-12, Ulupono SOP at 19; and C&CH SOP at 11.

continued as part of the MRP."[161] Likewise, the Companies support continuing the pension and OPEB trackers and the REIP Surcharge.[162]

B.

Performance Mechanisms

The Staff Proposal recommends developing metrics to track and incentivize specific Outcomes, using a portfolio of Performance Mechanisms including Reported Metrics, Scorecards, and PIMs.[163] As the fundamental unit of measurement for tracking and assessing utility performance, the identification and development of metrics plays a critical role in shaping Performance Mechanisms. Depending on the reliability of the metric and the priority of the Outcome, this suggested portfolio provides for a range of options, from reporting and tracking (Reported Metrics and Scorecards) to financial incentives and penalties (PIMs).

Within this portfolio of Performance Mechanisms, PIMs represent the most risk, in that there are financial incentives linked to the underlying metrics, which can result in

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[161]CA SOP at 31.

[162]HECO SOP at 19 and 31.

[163]See Staff Proposal at 32-34.

financial gain or loss to the utility or ratepayers, depending on how the PIM's incentives and/or penalties are structured.

The Staff Proposal includes a table which suggests specific Performance Mechanisms to address specific Outcomes.[164] The Staff Proposal also recommends that any Performance Mechanisms that are developed in Phase 2 should be clearly and timely presented to both the Parties and the public in a concise and comprehensive manner.[165]

1.

Reported Metrics

The Staff Proposal recommends developing Reported Metrics for the Outcomes of *Affordability, Customer Equity, Electrification of Transportation, Capital Formation*, and *Resilience*.

Ulupono generally agrees with the proposed development and use of metrics, but supports the use of outcome-based (versus program-based) metrics, as they are "often prescribed by law and policy . . . . [and thus] are relatively well understood and well supported."[166]

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[164]Staff Proposal at 35-37.

[165]See Staff Proposal at 39.

[166]Ulupono SOP at 24.

The COH also supports developing Reported Metrics, but proposes using them to also measure the Outcomes of *DER Effectiveness* and *GHG Reduction*, in addition to the other Outcomes recommended in the Staff Proposal.[167] The COH also recommends considering using a Scorecard to measure *Affordability* (rather than a Reported Metric), as well as developing a Scorecard and/or PIM to track and incentivize *Customer Equity* (rather than a Reported Metric).[168]

The C&CH "recommends that any metrics, scorecards, or [PIMs] that incorporate financial or cost criteria should also include environmental and social factors (e.g., the social cost of carbon) in the analysis."[169]

The Consumer Advocate suggests that the commission refrain from limiting Phase 2 to discussion of the metrics identified in the Staff Proposal and should instead "allow for a full, robust discussion of reported metrics in Phase 2 . . . ."[170]

The DER Intervenors generally support the development of Reported Metrics and PIMs and "translat[ing] the information gathered . . . into dashboard tools that can be used to educate

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[167]See COH SOP at 10-15.

[168]COH SOP at 10-12.

[169]C&CH SOP at 5.

[170]CA RSOP at 44.

and inform the public and competitive service providers about system conditions and trends[.]"[171] With regard to developing Reported Metrics and Scorecards, the DER Intervenors stress "the need to rely on primary data and data that can be readily and reliably verified."[172] To that end, the DER Intervenors recommend "[that] the Commission incorporate either through a parallel proceeding or as part of Phase 2 a process for identifying data needs and protocols for data gathering and sharing to assist the Commission, HECO Companies, and parties in developing metric targets and scorecards, and PIMs."[173]

The Companies "propose that the majority of any new incentives be reporting or scorecard metrics initially so that the appropriate data on those mechanisms may be collected and assessed and in certain circumstances evaluated for possible conversion to a financial PIM in the future."[174] However, the Companies also caution that "costs should be considered, and some level of cost-benefit analysis should be applied to reporting and scorecard requirements as well."[175] On this issue, the Companies concur with

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[171]DER Intervenors SOP at 20.

[172]DER Intervenors SOP at 20.

[173]DER Intervenors SOP at 20.

[174]HECO RSOP at 73.

[175]HECO RSOP at 73.

Blue Planet's suggestion that prospective costs of reporting could be included in determination of base rates preceding the application of PBR.[176]

2.

Scorecards

The Staff Proposal recommends developing Scorecards for the Outcomes of *Interconnection Experience, Customer Engagement, Cost Control,* and *GHG Reduction.*

Again, while few Parties provided direct comments regarding staff's proposed development of Scorecards, there does not seem to be significant opposition. The Consumer Advocate offers general support, stating that it "believes that scorecards can play an important role in providing utilities with improved incentives to meet regulatory policy goals[,]" and recommends "a full, robust discussion of scorecards in Phase 2."[177]

Similarly, Ulupono "generally supports the use of scorecards" for the Outcomes of *Interconnection Experience, Customer Engagement, Cost Control,* and *GHG Reduction.*[178]

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[176]HECO RSOP at 75 (citing Blue Planet response to HECO/BP-16).

[177]CA RSOP at 45.

[178]Ulupono SOP at 25 and 27-28.

As noted above, the COH recommends developing Scorecards for the Outcomes of *Affordability* and *Customer Equity*.[179] As also noted above, the DER Intervenors support using primary, reliable data to develop Scorecards.

3.

Performance Incentive Mechanisms

PIMs were the primary focus of the Parties' briefing regarding staff's proposed Performance Mechanisms. The Staff Proposal recommends developing PIMs to address the Outcomes of *Reliability, Interconnection Experience, Customer Engagement,* and *DER Asset Effectiveness*.

The Parties all express general support for developing PIMs in Phase 2, but adopt differing positions as to the nature and specific details of appropriate PIMs.

Blue Planet favors developing PIMs that are "financially significant for the utility" and recommends that, "as a starting point, PIMs should account for at least the equivalent of 200 basis points on ROE."[180] In addition to the Outcomes identified in the Staff Proposal, Blue Planet suggests developing PIMs to also address the Outcomes of *GHG Reduction* and *Resiliency*, as well as

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[179]COH SOP at 10-11.

[180]Blue Planet RSOP at 17.

"cost-effective acceleration of RPS achievement" and "climate adaption of our electric system" (within the Outcome of *Resiliency*).[181] Blue Planet proposes a "portfolio" approach to designing PIMs where a range of PIMs would be integrated into a "single comprehensive PIM system that will translate PIM scores into annual reward or penalty amounts during the revenue cap period."[182]

Ulupono favors focusing PIMs "primarily on outcomes including achievement of major energy statutory mandates and policy objectives[,]" contending that if such PIMs are properly implemented, "the optimal mix of activities and programs will follow."[183] Ulupono does not object to Staff's proposed PIM range of 150-200 basis points.[184] Ulupono also supports "Blue Planet's proposed framework for structuring and calibrating PIMs, including coordination and relative weighting of PIMs."[185] Ulupono strongly supports developing an "RPS-A PIM" to incent the Companies to accelerate achievement of the State's RPS goals, which, Ulupono maintains, would also address the Outcomes of

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[181]Blue Planet SOP at 27 and 29.

[182]Blue Planet SOP at 22-23; see also id. at 23-26.

[183]Ulupono SOP at 26.

[184]Ulupono SOP at 26.

[185]Ulupono SOP at 26.

Interconnection Experience, Customer Engagement, and *GHG Reduction.*[186] Ulupono also states that its proposed RPS-A PIM could be used to address acquisition of renewable energy resources.[187]

The Consumer Advocate supports a more open-ended approach to developing PIMs. The Consumer Advocate raises concerns that, for proposed PIMs, "Staff's PBR Recommendation does not provide many details[,]"[188] and proposes realigning PIMs to different Outcomes than those identified in the Staff Proposal.[189] Rather than pre-determine the number and nature of PIMs at this time, "[t]he Consumer Advocate recommends that the Commission allow for a comprehensive, robust discussion of PIMs in Phase 2, and not limit the discussion in Phase 2 to the PIMs recommended in the Staff PBR Recommendations."[190] Relatedly, the Consumer Advocate sets forth a proposed seven-step process by which to identify PIM-appropriate Outcomes and develop corresponding PIMs.[191]

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[186] See Ulupono SOP at 18-22 and 27-28.

[187] See Ulupono RSOP at 35.

[188] CA SOP at 48.

[189] See CA RSOP at 51.

[190] CA RSOP at 51.

[191] See CA SOP at 43-45.

The HECO Companies "are in general agreement with and support the approach described in the Staff Proposal to further explore the development of PIMs in Phase 2 of this proceeding, including the further identification, development of details, refinement and clarification of PIMs."[192] The Companies emphasize the importance of gradualism and recommend "development of no more than three [PIMs}," and that those addressing "emergent" Outcomes be developed as "upside only."[193] In particular, the Companies propose developing new PIMs focused on "(1) the acquisition, integration, interconnection and utilization of cost-effective DER resources; (2) advancement of cost-effective CBRE; and (3) a sustained incentive for acquisition of large-scale renewable energy resources (a clean energy PIM)."[194]

The DER Intervenors offer general support for the consideration of PIMs, but also caution a gradual approach to development and implementation. The DER Intervenors favor staff's recommended benefit-cost analyses to inform development of PIMs, but do not expressly comment on specific PIM details, beyond that

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[192]HECO SOP at 38.

[193]HECO SOP at 4.

[194]HECO RSOP at 68.

they should provide "a financially meaningful portion of the utility's earning opportunities[.]"[195]

C.

<u>Other Regulatory Mechanisms</u>

In addition to Revenue Adjustment Mechanisms and Performance Mechanisms, the Staff Proposal identifies a third broad category of "Other Regulatory Mechanisms," grouped into the following sub-categories: Capex/Opex Equalization, Innovation, and Platform Service Revenues.

1.

<u>Capex/Opex Equalization</u>

Within the Capex/Opex Equalization subcategory, the Staff Proposal suggests the following mechanisms: SSMs, all-resource procurement mechanisms, return on service-based solutions, capitalization of prepaid contracts, and total expenditure ("Totex") accounting.[196]

<u>SSMs.</u> The Parties express different views on utilizing SSMs for PBR. The Consumer Advocate opposes the use of SSMs and

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[195]<u>See</u> DER Intervenors RSOP at 12-13 (citing Blue Planet SOP at 20).

[196]Staff Proposal at 39-45.

maintains that they are not needed with a COSR suspension.[197] Similarly, Blue Planet believes that SSMs are not needed with a revenue cap in place.[198] The HECO Companies generally support "further exploration of these types of regulatory mechanisms," but submit that SSMs "should have a clear and transparent methodology to develop baselines and a clear process for evaluating savings[.]"[199] Similarly, Ulupono's support for SSMs is "conditioned on firm bids, i.e., bids pursuant to which the bidder - including the HECO Companies - is responsible for any cost overruns."[200] Ulupono, along with the COH, also supports using SSMs to promote increased reliance on non-wire alternatives.[201]

While not specifically discussing SSMs, the DER Intervenors express interest in exploring "all of these [Capex/Opex Equalization] mechanisms in Phase 2[.]"[202]

<u>All-resource procurement mechanisms.</u> The Parties express varying levels of support for all-resource procurement mechanisms.

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[197] <u>See</u> CA SOP at 55.

[198] <u>See</u> Blue Planet at 35.

[199] HECO SOP at 42.

[200] Ulupono SOP at 33.

[201] <u>See</u> Ulupono SOP at 33-34; and COH SOP at 7.

[202] DER Intervenors SOP at 21.

The Consumer Advocate is supportive of all-resource procurement, "but emphasizes the need for well-defined processes to avoid an unwieldy selection process[,]" and recommends that this issue be discussed in the IGP docket.[203] Similarly, the HECO Companies state that all-resource procurement mechanisms are already being explored in the IGP docket.[204] Ulupono also supports "development and implementation of all-resource procurement mechanisms," and states that their "adoption and implementation . . . must be coordinated with the IGP process."[205]

The COH expresses generalized support, stating that "all resource procurement is leading to low-cost energy solutions in other jurisdictions, and should be considered in Phase 2 of this docket."[206]

While the DER Intervenors express interest in exploring "all" of the Other Regulatory Mechanisms, they note that "competitive solicitations [such as all-resource procurement] . . . comes with important shortcomings that can limit the ability of the utility to respond to near term (e.g., one to three year planning horizon) grid needs[,]" and should be considered

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[203]CA SOP at 54.

[204]See HECO SOP at 42.

[205]Ulupono SOP at 34.

[206]COH SOP at 7.

in tandem with other mechanisms such as "tariff-based procurement mechanisms."[207]

Blue Planet expresses skepticism towards all-resource procurement mechanisms, and maintains that "the revenue cap mechanism remains the most straightforward and comprehensive approach to capex/opex equalization compared to the specific other methods listed in [the Other Regulatory Mechanisms section of the Staff Proposal]."[208]

Return on service-based solutions. Again, Party responses to this proposal are mixed. The Companies, Ulupono, and the DER Intervenors support further consideration of this option, although Ulupono clarifies that if other PBR mechanisms, such as Ulupono's proposed Enhanced Procurement Mechanism, RPS PIM, and SSMs are implemented, "there may be less necessity to use return on service-based solutions[.]"[209]

Conversely, the Consumer Advocate and Blue Planet oppose this proposal. The Consumer Advocate contends that "this approach would appear to charge ratepayers more to solve a problem that does not exist when traditional COSR rate cases have been

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[207]DER Intervenors SOP at 21-22.

[208]Blue Planet SOP at 35.

[209]See HECO SOP at 42; Ulupono SOP at 37; and DER Intervenors SOP at 22-23.

suspended."[210] Likewise, Blue Planet states that this proposal appears akin to "ratebasing" operating expenses, "which would generally increase costs, and also fundamentally maintain the underlying COSR systems and its shortfalls in encouraging cost control."[211]

Capitalization of prepaid contracts. Similarly, capitalization of prepaid contracts evokes mixed responses. The Companies and DER Intervenors support further consideration of this approach.[212] Ulupono provides general support, but "cautions that the contract counterparty must be sufficiently established, capitalized and creditworthy."[213]

The Consumer Advocate and Blue Planet oppose this mechanism. The Consumer Advocate maintains that this proposal is unnecessary in light of the suspension of COSR rate cases and, furthermore, is "redundant to existing regulatory accounting provisions that already account for prepayments as an asset that is includable in rate base."[214] Blue Planet opposes capitalization of prepaid contracts on the same grounds as return on service-based

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[210]CA SOP at 55.

[211]Blue Planet SOP at 36.

[212]See HECO SOP at 42; and DER Intervenors SOP at 23-24.

[213]Ulupono SOP at 38.

[214]CA SOP at 56.

solutions: it is likely to increase costs, while failing to address the underlying COSR shortfalls in encouraging cost control, which can be better addressed through a long-term revenue cap.[215]

Totex accounting. The Parties express little support for exploring Totex accounting. The Consumer Advocate states that "Totex represents an entirely new accounting paradigm" and opposes it on the grounds that it would involve "complete redefinition of regulatory and [Generally Accepted Accounting Practices] accounting rules . . . ."[216] Furthermore, the Consumer Advocate contends, with COSR rate cases suspended, "concerns about capex bias are mitigated, eliminating the need for totex."[217] Similarly, Ulupono and Blue Planet do not support Totex, noting that implementing Totex would present numerous challenges, and a MRP with ARA is better-suited to address capex bias in Hawaii.[218]

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[215]See Blue Planet SOP at 36.

[216]CA SOP at 57-58.

[217]CA SOP at 58.

[218]See Ulupono SOP at 38-39; and Blue Planet SOP at 36.

2.

Innovation

Within the Innovation subcategory, the Staff Proposal suggests the following: an innovation fund, an expedited process for implementation of pilot programs, and a web-based innovation platform.[219]

The Companies state that they are already "actively stimulating innovation through the development of innovation centers," but are open to discussing other approaches, such as those identified in the Staff Proposal.[220] However, the Companies state that any innovation policies or programs will require "a commitment of resources and energy" and emphasize that "there would need to be clear guidance on eligibility for cost recovery at the outset and consideration of how pilots could then transition into full-scale programs and services . . . ."[221] Accordingly, the Companies also support "exploring an annual funding opportunity that could potentially be successful in directly providing the companies with a new source of capital to invest in innovative projects in Phase 2."[222]

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[219]Staff Proposal at 46-50.

[220]HECO SOP at 43.

[221]HECO SOP at 43.

[222]HECO SOP at 43.

The Consumer Advocate supports encouraging innovation through the development of web-based innovation platforms and an expedited pilot process, but opposes consideration of an innovation fund.[223] Noting that "Hawaii's ratepayers are already burdened with high electric rates and monthly bills[,]" the Consumer Advocate contends that "customers should not also be burdened with potential costs associated with research and development expenses that may result in profitable endeavors for the utility and/or third-parties at customers' expense."[224]

The DER Intervenors strongly support development of innovation policies and mechanisms and "emphasize that in no area in this proceeding is innovation more important than the way that PBR can animate markets for DER and provide an increasingly important role for non-utility competitive service providers to deliver ratepayer savings."[225] The DER Intervenors support developing "streamlined pilot programs" to "address gaps in integrating DER solutions."[226] They also emphasize that it is "essential that utilities are incentivized to seek innovative ideas from outside the utility walls by actively coordinating and

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[223]See CA SOP at 58-59.

[224]CA SOP at 59.

[225]DER Intervenors SOP at 24-25.

[226]DER Intervenors SOP at 25.

partnering with third party service providers to incubate, develop, test, and implement innovative solutions to grid needs."[227] The DER Intervenors also support developing "mechanisms to provide the utility incentives for developing innovative pilots that are rapidly scaled to system-wide deployment[,]" which could be structured as an adjustment to a SSM.[228]

Ulupono supports consideration of an innovation fund that combines elements from the United Kingdom's annual Network Innovation Allowance with an expedited innovation pilot process.[229] Ulupono also supports further discussion about web-based platform services.[230]

The COH supports developing an innovative pilot process, to be financed by an innovation fund, which, in turn, could be funded through a SSM.[231]

Blue Planet also offers broad support for all the proposed innovation options.[232]

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[227]DER Intervenors SOP at 26.

[228]DER Intervenors SOP at 26.

[229]Ulupono SOP at 39-40.

[230]Ulupono SOP at 41.

[231]COH SOP at 16.

[232]Blue Planet SOP at 37.

3.

Platform Service Revenues

The last subcategory of Other Regulatory Mechanisms identified in the Staff Proposal are platform service revenues.[233] As described in the Staff Proposal, "a *platform* is a business based on enabling value-creating interactions between external producers and consumers[,]" and "provides an open, participative infrastructure for these interactions and sets governance conditions for them, with the overarching purpose to facilitate transactions and create value for all participants."[234]

Blue Planet supports consideration of platform service revenues, but notes that "the details of such an approach remain largely unspecified at this time," and "submits that further guidance from the Commission and discussion among the parties are needed in Phase 2 to further develop the vision and direction, if not the basic framework, for the platform model, and the nearer-term steps necessary to proactively move forward along that path."[235]

Ulupono also supports consideration of a "network" of platform services, including "platform service revenues related to

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[233]See Staff Proposal at 50-52.

[234]Staff Proposal at 50 (emphasis in original).

[235]Blue Planet SOP at 38-39.

DER transactions from lead origination for third-parties, value-added data analysis, and other value-added services related to DER utilization . . . ."[236] Ulupono also supports considering platform service revenues generated from "the sharing of customer and system data," subject to appropriate privacy protections, "including the choice for utility customers to opt-in or opt-out of data sharing programs."[237]

Similarly, the COH supports platform revenue services as a "utility business model," but raises concerns about "addressing data as a source of revenue for the utility," including "establish[ing] a predicate that data from customer-owned energy applications are owned by the customers," and to what extent a utility should be permitted to access such data and earn revenues from it.[238]

The DER Intervenors strongly support further consideration of platform service revenues and urge the commission to use Phase 2 to "more fully characterize and plan for a vision of a platform service model for the electric utility business in Hawaii as a cornerstone to accomplishing the State's policy

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[236]Ulupono SOP at 41-42.

[237]Ulupono SOP at 42.

[238]COH SOP at 17.

objectives."[239] Acknowledging staff's and the Parties' concerns about the "unspecified" details of this approach, the DER Intervenors recognize that "there is a lack of definition for the desired utility business model end-state[,]" and, consequently, stress that this "will frustrate the ability to develop a workable platform service model . . . ."[240] Accordingly, "[t]he DER Intervenors recommend that the Commission direct and undertake more work to craft a fully formed vision of a successor business model for electric utilities under a PBR regime[,]" and reference the Companies' on-going strategic planning for 2020-2025 as containing many parallel considerations which could "provide a basis for finding common ground for developing a PBR framework and platform service model . . . ."[241]

The Consumer Advocate notes similar issues in developing platform service revenues and submits that they may be beyond the scope of this proceeding. According to the Consumer Advocate, "discussion about [platform service revenues] should occur in a context where platform services and the utility platform business model are clearly defined and understood[,]" and that "the platform business model is too broad and complex to be addressed in this

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[239]DER Intervenors RSOP at 17.

[240]DER Intervenors RSOP at 17.

[241]DER Intervenors RSOP at 18.

docket on performance-based regulation."[242] As a result, "[t]he Consumer Advocate believes that the platform business model would be better addressed in a different forum (or forums) that allows for a more detailed investigation of the many challenging issues . . . . [and] [i]n the absence of more clarity on the platform business model, it does not make sense to discuss [platform service revenues] as part of Phase 2."[243]

The Companies state that they "are already evaluating and putting into place the foundation for this type of platform which will foster the exchange of cost effective, third-party services," and refer to the Grid Modernization proceeding (Docket No. 2018-0141) and the IGP proceeding (Docket No. 2018-0165).[244] While expressing general support for further exploration of this issue,[245] the Companies also agree "that developing concrete steps towards developing platform services revenues may be beyond the practical scope of Phase 2."[246] The Companies state that "Phase 2 should be considered a first step, with further evolution to continue in future phases or dockets . . . . [and] [a]ccordingly,

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[242]CA SOP at 63-64.

[243]CA SOP at 65. See also, CA RSOP at 75.

[244]HECO SOP at 44.

[245]HECO SOP at 44.

[246]HECO RSOP at 80.

Phase 2 should be reasonably limited in scope so that desired changes get sufficient attention and consideration, thus increasing chances of successful design and mitigating risk of unintended consequences."[247]

[247]HECO RSOP at 81.

CERTIFICATE OF SERVICE

The foregoing order was served on the date of filing by mail, postage prepaid, and properly addressed to the following parties:

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