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STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

**IN THE MATTER OF THE COMMISSION'S)
INVESTIGATION, PURSUANT TO IC § 8-1-2-)
58, INTO THE EFFECTIVENESS OF DEMAND)
SIDE MANAGEMENT ("DSM") PROGRAMS)
CURRENTLY UTILIZED IN THE STATE OF)
INDIANA, INCLUDING AN EXAMINATION)
OF ISSUES THAT COULD IMPROVE THE)
EFFECTIVENESS OF DEMAND SIDE)
MANAGEMENT PROGRAMS IN THE STATE)
INCLUDING CONSIDERATION OF THE)
ESTABLISHMENT OF AN INDEPENDENT)
DSM ADMINISTRATOR MODEL ON A)
STATE-WIDE BASIS)**

CAUSE NO. 42693

PHASE I ORDER

**RESPONDENTS:)
RESPONDENTS: ALL JURISDICTIONAL)
ELECTRIC AND GAS UTILITIES IN THE)
STATE OF INDIANA)**

APPROVED: APR 23 2008

**BY THE COMMISSION:
David E. Ziegner, Commissioner
Scott R. Storms, Chief Administrative Law Judge**

On July 28, 2004 the Indiana Utility Regulatory Commission ("Commission" or "IURC") initiated an investigation pursuant to Indiana Code § 8-1-2-58 to consider and review Demand Side Management ("DSM") issues and programs in the State of Indiana. The Commission initiated the investigation to examine the overall effectiveness of DSM programs in the state and to allow it to consider any and all issues that may improve DSM programs. The Commission also indicated that its review of the issues would include consideration as to whether an independent DSM administrator model should be established in Indiana on a statewide basis.

On October 19, 2006, the Commission found that its investigation would be done most effectively through utilization of Commission staff as part of a phased proceeding structured to result in the development of a report to the Commission regarding the current state of DSM programs in Indiana. The Commission designated Dr. Bradley Borum, Director of the Commission's Electricity Division, Mr. Shawn Kelly, a Utility Analyst with the Commission's Gas/Water/Sewer Division, and Ms. Susan Stratton, Executive Director of the Energy Center of Wisconsin as testimonial staff ("Testimonial Staff") in this proceeding.

The Commission instructed the Testimonial Staff to address several issues including existing DSM programs, the utility-led DSM model and the independent third-party administrator DSM model. The Commission also sought recommendations on whether improvements to the DSM programs in Indiana can be accomplished within the existing utility-led DSM framework or whether the Commission should continue its examination of possible improvements to DSM programs throughout the State as part of a subsequent phase of this Investigation. The Commission determined that following the preparation and submission of the staff report, and review of any additional evidence that may be submitted by the parties, it would issue a Phase I Order that contained findings and conclusions and make any necessary determinations regarding the most appropriate manner in which to proceed with any additional phases of this proceeding.

Petitions to intervene in this cause were filed by the Indiana Industrial Group, ("Industrial Group"); Indiana Municipal Power Agency ("IMPA"); Wabash Valley Power Association, Inc., ("Wabash Valley"); Hoosier Energy Rural Electric Cooperative, Inc. ("Hoosier"); the Board of Commissioners of LaPorte County, Indiana ("LaPorte County" or "LaPorte"); and the Citizens Action Coalition of Indiana, Inc. ("CAC"). Each of the petitions to intervene were granted by the Presiding Officers.

After agreed-to modifications of the originally approved procedural schedule, the Testimonial Staff filed its report on April 16, 2007 and the parties pre-filed responsive testimony on May 18, 2007 and reply testimony on June 8, 2007.

Pursuant to notice, duly published as required by law, an Evidentiary Hearing was held in this Cause on June 27, 2007 in the Commission's Offices at the National City Center, 101 West Washington Street, Suite 1500 East, Indianapolis, Indiana. Respondents Duke Energy Indiana, Inc. ("Duke"); Indiana Michigan Power Company ("I&M"); Indianapolis Power & Light Company ("IPL"); Northern Indiana Public Service Company ("NIPSCO"); Southern Indiana Gas & Electric Company, d/b/a Vectren Energy of Indiana, Inc. ("Vectren"), and, Citizens Gas & Coke Utility ("Citizens"), participated in the Evidentiary Hearing. The Office of Utility Consumer Counselor ("OUCC") and Intervenors CAC; LaPorte County; Industrial Group; Wabash Valley; and, IMPA appeared by their respective counsel and participated in this proceeding. At the Evidentiary Hearing, the testimony and exhibits of the parties were offered and admitted into the record. No members of the general public appeared or participated in this proceeding.

This Commission, having examined the evidence and being duly advised in the premises, now finds that:

- 1. Notice and Jurisdiction.** Due, legal and timely notice of the Evidentiary Hearing in this matter was given as required by law. Respondents are all jurisdictional electric and gas utilities in the State of Indiana and are operating utilities, or municipally owned utilities, within the meaning of those terms in Ind. Code § 8-1-2-1(a) and (h) of the Public Service Commission Act, as amended, and are subject to the jurisdiction of the Commission in the manner and to the

extent provided by the laws of the State of Indiana. The Commission has jurisdiction over the Respondents and the subject matter of this cause.

2. Respondents and Intervenors Characteristics and Businesses. Duke is a corporation organized under the laws of the State of Indiana, with its principal office and place of business located at 1000 East Main Street, Plainfield, Indiana. Duke provides electric service to over 750,000 retail electric customers located in 69 counties in the central, north central and southern parts of the State of Indiana.

I&M is a wholly-owned subsidiary of American Electric Power Company, Inc. I&M's service area consists of approximately 8,260 square miles and is located in northern and eastern Indiana and southwest Michigan. I&M provides electric service to approximately 454,000 retail electric customers within the State of Indiana. I&M is an operating company subsidiary in the AEP system of American Electric Power Company, Inc.

IPL is a corporation organized and existing under the laws of the State of Indiana, with its principal office located at One Monument Circle, Indianapolis, Indiana. IPL's service area consists of approximately 528 square miles and is located principally in and around the City of Indianapolis and in portions of Boone, Hamilton, Hancock, Hendricks, Johnson, Marion, Morgan, Owen, Putnam and Shelby counties. IPL provides electric service to approximately 465,000 retail electric customers within the State of Indiana.

NIPSCO is a corporation organized under the laws of the State of Indiana, with its principal office and place of business located at 801 East 86th Avenue, Merrillville, Indiana. NIPSCO provides electric service to approximately 450,000 retail electric customers located in 21 counties in northern Indiana.

Vectren is a corporation organized and existing under the laws of the State of Indiana, with its principal office located at One Vectren Square, Evansville, Indiana. It is engaged in rendering natural gas and electric utility service to the public within the State of Indiana and owns, operates, manages, and controls plant and equipment used for the distribution and furnishing of such service. Vectren South provides natural gas service to 112,000 customers and electric service to 140,000 customers in southwestern Indiana.

Citizens' principal office is located at 2020 North Meridian Street, Indianapolis, Indiana. Its Gas Division is engaged in rendering natural gas utility service to the public within the State of Indiana and owns, operates, manages and controls plant equipment used for the distribution and furnishing of such service. Citizens provides gas service to approximately 265,620 customers in and around Marion County, Indiana.

Intervenor CAC is a membership organization operating as not-for-profit Corporation under the laws of the State of Indiana and its principal office is at 5420 North College, Indianapolis, Indiana.

Intervenor Hoosier is a rural electric cooperative organization organized and existing pursuant to the laws of the State of Indiana, with its principal place of business at 7398 State

Road 37, Bloomington, Indiana. Hoosier provides all the electric power and energy requirements for 17 member systems, all of which are electric utilities delivering service to their retail customers.

Intervenor IMPA is a joint agency within the meaning of Indiana Code § 8-1-2.2-2(c) and is a political subdivision of the State of Indiana. IMPA has its principal office at 11610 North College Avenue, Carmel, Indiana. IMPA provides all of the electric power and energy requirements of its 40 member municipalities.

Intervenor Industrial Group is an ad hoc group of industrial customers located in the State of Indiana, including Haynes International, Inc., International Truck & Engine, National Starch & Chemical Co., Praxair, Inc., Rolls-Royce Corporation, and USG Corporation.

Intervenor LaPorte County is the Board of Commissioners of LaPorte County, a county government in northern Indiana within the geographical bounds of the electric service territory of NIPSCO.

Intervenor Wabash Valley is a generation and transmission cooperative with its principal place of business in Indianapolis, Indiana. Wabash Valley is a non-profit cooperation organized and existing pursuant to the Indiana Non-Profit Corporation Act. Wabash Valley was formed by its members for the purpose of providing wholesale power and transmission service to its members for resale to their retail customers. Wabash Valley's native load consists of 30 members, 28 of which are not-for-profit cooperatives serving electric energy to their members at retail, and located primarily in the rural areas of the States of Indiana, Michigan, Illinois and Missouri.

3. Direct Testimony and Report of Testimonial Staff. Ms. Susan Stratton, Executive Director of the Energy Center of Wisconsin, sponsored and testified regarding her report entitled *Indiana DSM Investigation Report: Report on Current Programs and Future Directions* ("Energy Center Report" "Stratton Report" or "Report"). In her testimony, Ms. Stratton provided an overview of the Energy Center Report in a manner that highlighted the specific findings and recommendations contained within the Report. Full details regarding Ms. Stratton's specific recommendations are contained in the Report which was sponsored by Ms. Stratton.

In her testimony Ms. Stratton provided an overview and summary of the current status of DSM programs in Indiana; options for governance, infrastructure and program delivery; and, recommendations for next steps necessary to improve overall effectiveness of DSM in the state including consideration as to whether an Independent DSM Administrator Model should be established in Indiana on a state-wide basis. According to Ms. Stratton, Indiana is in a good position to move toward a more consistent statewide DSM effort which could remedy the current inconsistent patchwork of DSM program offerings in the state. Additionally, Ms. Stratton concluded that an effective statewide DSM program could provide economic and environmental benefits though an overall reduction in energy use in Indiana.

The Stratton Report specifically concludes that compared to other states, Indiana's energy environment is characterized by low energy prices and high energy consumption. While Indiana ranked 47th among the 50 states and the District of Columbia in cost of both retail electricity and all energy sources in 2003, it has relatively high energy consumption, ranking sixth in total energy consumption per capita. Report at 11. The Report further notes that the presence of large, energy-intensive industry in the state contributes to this high ranking - accounting for half of Indiana's consumption- but further notes that other Midwestern states with high industrial energy consumption consume substantially less energy per capita than Indiana. *Id.*

The following table from the Report presents a comparison of Indiana's per-capita energy consumption to other Midwestern states and to the United States as a whole:

Industrial Midwestern States' Per-Capita Energy Consumption in 2003

State	Million British Thermal Units
Indiana	470.1
Ohio	348.7
U.S. avg.	339.0
Michigan	313.4
Illinois	309.7

Id. at 12.

Compared to the rest of the country, Indiana's combination of low prices and high spending results in moderate per-capita spending for electricity and high spending on energy overall. In 2003, Indiana ranked 27th in electricity expenditures per capita (\$863 compared to a nationwide average of \$884), but 6th in total energy expenditures per person (\$3,063 compared to \$2,590). *Id.*

Ms. Stratton indicates in her testimony that comparing Indiana's per-capita energy demand, prices, and spending to other Midwestern states, and the nation as a whole, leads to the conclusion that increased DSM programs can result in overall cost savings to energy consumers in the state. In reaching her conclusion that increased DSM Programs can result in overall cost savings in the state of Indiana, Ms. Stratton turns her attention to the review and consideration of existing DSM Programs in Indiana.

A. Historical Evolution of Existing DSM Programs. As reflected in the Report, collectively Indiana utilities provide various types of DSM efforts, although the level of effort and focus varies greatly across companies. Electric utilities offer both programs and tariffs designed to reduce peak demand and encourage lower overall electric consumption. Natural gas utilities offer programs designed to promote efficient use of their product. Each of these existing DSM programs were discussed and included in the Report.

Ms. Stratton indicates that DSM programs may be discussed by utilities as part of their integrated resource planning process and may ultimately be presented to the Commission for consideration in a formal regulatory proceeding. However, under the current regulatory framework, utilities have substantial discretion in deciding whether or not to propose DSM

programs and the types of programs that are, or are not, presented to the Commission. This approach has manifested itself in extensive differences in the scale and scope of DSM efforts employed by utilities throughout the state. While Indiana utilities collectively provide various types of DSM programs, the level of effort and focus varies greatly across companies. Report at 14.

According to the Report, only two of the five major electric utilities offer substantial programs that help customers increase energy efficiency. While all major electric utilities point out that DSM programs are considered as part of their integrated resource planning process, the Report concludes that the current combination of programs offered in Indiana places the state below average in spending for energy efficiency and in savings attained in the Midwest region and nationally.

B. Electric Industry DSM- Reduction of Peak Demand. Ms. Stratton testified that the Report indicates that all major electric utilities have either tariffs or programs intended primarily to reduce peak demand. Tariffs provide incentives for customers to curtail load during times of day characterized by high usage or during specific peak demand events. According to Ms. Stratton, most of these tariffs are designed for larger commercial and industrial customers and provide reduced rates in exchange for participation. Programmatic efforts identified in the Report include the installation of utility controlled equipment on central air conditioners and other devices that the utility can cycle off and on as needed during peak demand events. These programs, which are designed mostly for residential and small business customers, provide incentives for participation. Report at 15.

Reported Programs and Tariffs Designed Primarily for Demand Reduction, 2006

Utility	Programs Reported	Tarriffs Reported	Participating Customers	Share of Peak Demand Addressed through DSM
Indiana Michigan Power	0	14	19,245	7%
Indianapolis Power & Light	1	10	16,071	3%
NIPSCO	0	11	4,753	8%
Duke Energy Indiana	2	0	10,827	8%
Vectren	1	0	32,070	4%

Id.

C. Electric Industry DSM- Reduction in Overall Consumption. Ms. Stratton testified that efforts to actually reduce electricity consumption are concentrated among two utilities with little activity elsewhere in the state. Generally, these programs tend to follow traditional rebate-based approaches for residential, commercial, and smaller industrial customers. (Detailed information about these efforts is attached in Appendices A and B of the Report).

Reported Programs Designed to Reduce Electric Consumption, 2006

Utility	Programs Reported	Participating Customers	Expenditures
Indiana Michigan Power	1	22	\$30,000
Indianapolis Power & Light	4	2,518	\$980,000
NIPSCO	0	0	\$0
Duke Energy Indiana	9	6,581	\$2,850,000
Vectren	0	0	\$0

Id. at 16

According to Ms. Stratton, whether utilities offer programs designed to reduce consumption appears to be correlated with the cost-benefit criteria the utilities utilize in considering whether to undertake a DSM program. When asked about preferred and actual criteria for planning DSM programs, the utilities that offer more than minimal programs indicated that they utilize a variety of cost-benefit tests, including the Total Resource Cost Test, the Utility Cost Test, the Ratepayer Impact Measure, and the Participant Test. Two of the utilities with minimal or no such program offerings emphasized that they utilize the rate-impact test, which according to the Report is one of the most restrictive tests available. *Id.* at 16. Based on the foregoing, the Report concludes that the cost-benefit criteria by which potential programs are judged has a significant effect on the level of effort deemed to be appropriate by individual utilities. *Id.*

D. Comparisons to Other States. As reflected in the Report, DSM programs in the state place Indiana below average in spending for energy efficiency and in savings attained. The Report indicates that Indiana ranks 31st nationally and 6th among 7 Midwestern states in spending for electric energy efficiency - both on a per capita basis and as a percentage of utility revenue. Report at 18. The following tables from the Stratton Report graphically depict these findings:

Energy Efficiency Spending per Capita, 2003

State	Rank (of all states)	Energy Efficiency Spending per Capita
Wisconsin	7	\$ 11.33
Iowa	10	\$ 10.17
Minnesota	14	\$ 8.65
US Average	n/a	\$ 4.65
Ohio	25	\$ 1.37
Michigan ¹	27	\$ 0.99
Indiana	31	\$ 0.48
Illinois	35	\$ 0.24

Id. at 19

**Energy Efficiency Spending
as a Percentage of Utility Revenue, 2003**

State	Rank (of all states)	EE Spending as % of Revenues
Wisconsin	7	1.4%
Iowa	11	1.2%
Minnesota	12	1.2%
US Average	n/a	0.5%
Ohio	25	0.2%
Michigan	26	0.1%
Indiana	31	0.1%
Illinois	34	0.0%

Id.

¹ According to the Report, Michigan is pursuing a significant increase in its DSM spending that is likely to put it closer to Wisconsin, Iowa, and Minnesota levels. See the Michigan Public Service Commission's recently released "21st Century Energy Plan" at www.cis.state.mi.us/mpsc/electric/capacity/energyplan/index.htm. New legislation in Wisconsin has also increased the spending level effective July 1, 2007 (2005 Wisconsin Act 141).

Indiana fares slightly better in a similar comparison of energy savings as a percentage of utility sales, placing 22nd nationally and 4th among the 7 Midwestern states.²

Energy Savings (kWh) as a Percentage of Utility Sales

State	Rank (of all states)	Cumulative Annual kWh savings as % of kWh Sales
Minnesota	4	6.7%
Wisconsin	9	4.4%
Iowa	16	2.8%
US Average	n/a	1.9%
Indiana	22	0.8%
Ohio	26	0.3%
Illinois	38	0.1%
Michigan	48	0.0%

Id. at 20

E. Natural Gas DSM Programs. Based on findings reflected in the Report, natural gas DSM programs appear to be more modest in scale and scope than electric programs in Indiana. The Stratton Report indicates that two of the three largest natural gas utilities offer rebates to customers who purchase high-efficiency natural gas appliances. One of these utilities has a fairly broad offering of rebates for residential and business customers, as well as new construction, for part of its service area. The other utility advertises rebates only for two residentially-oriented appliances. Both of these utilities offer programs to help low-income customers reduce their consumption - and thereby their bills. The third utility does not advertise any DSM programs, but does offer incentives for customers switching from other vendors to the use of natural gas equipment.

DSM Programs Identified for Natural Gas Customers

Utility	Residential	Business	New Construction (homes)	Low Income
Citizens Gas	Yes	No	No	Yes
NIPSCO	No	No	No	No
Vectren	Yes	Yes	Yes	Yes

Id. at 15

² A similar comparison of demand savings was not available.

F. Program Administration. Of the states referenced in the Report, (Illinois, Minnesota, Ohio and Wisconsin) three administer their programs through a state agency; the fourth administers its programs via a state agency that contracts most of the administrative functions to a non-profit corporation. While not included in the following comparison table, the Report notes that in January 2007, Michigan completed its first electric energy plan in 20 years. The plan makes a strong commitment to energy efficiency (as well as renewable energy).

State DSM Program Comparison

State	Administration	Funding	Benefit Measure	Incentives
Illinois	Illinois Department Of Commerce and Economic Opportunity	\$3 Million/Yr From Utilities; Pro Rata Share Of \$3 Million, Based On Prior Year's	Utility test	None
Minnesota	State Agency Sets Goals, Approves And Evaluates Programs. Utilities Retain Funds; Design and Implement Programs.	53 Million +/-Yr; 1.5 – 2.0% Of Each Electric Utility's Gross Operating Revenues	Modified societal benefits	Cost recovery and performance incentives
Ohio	Ohio Department Of Development	\$15 million/yr for 5 years; \$5 million/yr until \$100 million total; Temporary rider collected by electric utilities of 0.10758 mills/kWh	Simple payback less than five years or other measures.	None for utilities
Wisconsin	Wisconsin Department of Administration subcontracts most program administration to non-profit corporations (through 2007)	\$62.3 million +/-yr possible; Gas and electric utility rate-based fees and new statutory fees from all electric utilities	Total resource cost and societal benefits tests	Some shared savings; Some tax exemptions.

G. Building a DSM Strategy. Based on the foregoing overview of existing state programs in the Midwest and Indiana's relative ranking, the Energy Center Report goes on to discuss the general building blocks of an effective statewide energy efficiency ("DSM") program. The Report identifies the following as central necessary steps:

- Policy development
- Governance
- Infrastructure
- Implementation

1. Policy Development. As discussed in the Report, policy development begins with identifying the reasons for pursuing energy efficiency. These reasons can be codified in enabling legislation and/or regulatory agency orders. Broad policy reasons for pursuing energy efficiency can include:

- Ensuring the most efficient economy possible by correcting market failures;
- Deferring investments in new generation;
- Addressing transmission constraints;
- Reducing environmental damage by lowering the emission of harmful air pollutants;
- Positioning the state's energy sources to respond to external factors (*e.g.*, price and supply volatility, a more carbon-constrained situation should the United States adopt carbon regulations);
- Lowering the overall cost of electricity without reducing comfort or convenience;
- Reducing resource waste;
- Creating jobs and stimulating the economy.

Id. at 23

The Report further indicates that establishing an overarching purpose is critical in defining the administrative structure, delivery model, and other components of energy efficiency initiatives. Without this guidance, components of the DSM portfolio may pursue competing goals or fail to accomplish the state's greatest needs cost-effectively. Similarly, an overall policy statement can provide guidance concerning the scope of the DSM programs on other critical factors in which policymakers have a clear goal. *Id.* at 23-24.

According to the Report, to the extent possible, it is useful for policy statements to identify goals concerning:

- whether programmatic approaches should emphasize the immediate saving of energy (resource acquisition) or slower, but longer-lasting interventions in the market (market transformation);
- the degree to which programs should be available uniformly across the state;

- the sectors of the economy in which energy efficiency should be offered and promoted; and
- the criterion by which the scale of energy efficiency efforts will be determined over time.

Id. at 24.

The Report outlines general approaches to DSM and indicates that various approaches reflect different needs and circumstances, target different program audiences, and entail policy choices when weighing and implementing various policy options. The policy approaches discussed in the Report include:

- Resource Acquisition;
- Market Transformation;
- Tariff-based Approaches;
- Geographic Uniformity;
- Market Sector Coverage;
- Efficiency Criteria;
- Cost Benefit Tests.

Report at 23-26.

2. Resource Acquisition. As reflected in the Report, historically resource acquisition was the goal for most ratepayer funded energy efficiency programs in the U.S. The primary goal of resource acquisition is to reduce energy use where energy efficiency represents a more economical resource alternative to construction or procurement of new supply. Resource acquisition programs target the customer directly and generally offer financial incentives or rebates for purchasing energy efficient equipment or provide technical assistance or other motivation for changing behavior. *Id.* at 24.

3. Market Transformation. With respect to Market Transformation the Report indicates that the goal of these types of programs is to remove identified barriers so that the energy efficiency market will function on its own. Market transformation programs target market actors upstream of the end use customers such as retailers and contractors. *Id.*

4. Tariff-based Approaches. This approach depends on specific price signals to consumers to affect the desired reduction in energy or peak demand. These approaches require a method of communication to customers regarding prices so that consumption is made with full understanding of costs as they may change daily or hourly. Peak load reduction approaches typically depend on real-time pricing, which reflects hourly market rates, or on interruptible contracts which allow the utility to request (with some notice) load shedding or interruption for a specific period of time. Energy reduction approaches may use time of day rates or real-time pricing. *Id.*

5. **Geographic Uniformity.** According to the Report, geographically uniform programs can be offered consistently to all consumers in the state, thereby ensuring consistency and equity across utility service areas. Such consistency is important for efforts to influence the energy-consuming behavior of market actors that span across utility service areas and tends to provide economies of scale over programs limited to a utility's in-state service area. *Id.* at 25

6. **Efficiency Criteria.** One additional policy consideration is the criterion by which the scale of efficiency efforts should be determined. Identification of policy objectives can provide guidance concerning the overall size of programmatic efforts and ensure consistency across programmatic efforts. *Id.*

7. **Cost Benefit Tests.** As discussed previously with respect to the specific criteria utilized by various utilities in Indiana, for purposes of evaluating potential DSM programs, the use of cost-benefit tests provides assurance that individual programs or portfolios can be justified on cost-effectiveness grounds. Common tests include:

- **The Participant Test.** Measures the difference between the quantifiable costs incurred by a participant in a DSM program and the subsequent cost savings received by that participant; programs are cost effective if the value to the participant exceeds the costs incurred by the participant.
- **Rate Impact Measure.** Measures distribution of equity impacts of DSM programs on nonparticipating utility ratepayers; programs are cost effective if they reduce utility rates. Societal Test-variation on total resource cost test; includes quantified effects of externalities (*i.e.*, environmental costs).
- **Total Resource Cost Test.** Measures the difference between the total costs of a DSM program plus any participant costs and the avoided costs of utility supply; programs are cost effective if the avoided supply costs exceed total program costs.
- **Utility Cost Test.** Measures the difference between the costs incurred by a utility (program costs) and the avoided supply costs due to the program (costs and benefits incurred by program participants are excluded); programs are cost effective if avoided supply costs exceed program costs.

Id. at 26.

H. **Governance and Oversight.** As discussed in the Energy Center Report, in the early days of demand side management most ratepayer funded energy efficiency programs were administered, designed and delivered by utilities under the oversight of - and in accordance with expectations set by - state regulators. Currently the oversight, administrative, and delivery

functions for energy efficiency programs run the gamut from general administration (with reporting responsibility to the oversight agency or organization) to the actual field delivery of individual programs (or the oversight of contractors providing that service). In between it includes all the tasks necessary to develop programs and assess their effectiveness, including studying energy efficiency potential, identifying program approaches, developing program logic models, designing programs, budgeting, hiring and managing staff and sub-contractors, and assessing and evaluating program impacts. *Id.* at 27

Oversight involves the broad range of responsibilities for the portfolio of programs with particular emphasis on ensuring that policy objectives for the programs are accomplished. This responsibility could also include involvement in high level planning and design, broad market research and evaluation, and the broader decisions affecting program delivery. This responsibility can vary depending on the administration and delivery model chosen. Administration and delivery of energy efficiency programs can reside with several different entities:

- **Single Utility.** Individual utilities design and implement DSM programs, generally under the oversight of the regulatory agency (which may set goals, approve and evaluate programs). Iowa and Minnesota use this model.
- **Multiple Utilities.** Individual utilities administer a set of standardized programs approved and overseen by the regulatory agency. California uses this model.
- **Third-Party Organization.** An independent, non-governmental organization administers statewide programs with broad policy direction and review from the regulatory agency. Oregon and Vermont use this model.
- **Government or Quasi Government Agency.** A governmental agency administers statewide programs with governance and oversight from the regulatory agency. New York uses this model.

Id.

There are also variations on these models such as administrative responsibility invested in a government agency that subcontracts to non-profits for program administration - as in Wisconsin. And there are other organizational layers (regional market transformation organizations such as the Midwest Energy Efficiency Alliance, Northwest Energy Efficiency Alliance, and Northeast Energy Efficiency Partnerships) whose goals can complement and/or augment a state's energy efficiency initiatives. As discussed in the Report, there are benefits and drawbacks to each of these administrative models. *See*, Report at 28.

I. Infrastructure and Implementation. As discussed in the Stratton Report, statewide energy efficiency programs involve an infrastructure of regulators, administrators, evaluators and program deliverers. Details concerning the infrastructure depend

on the policy objectives and governance structures described above. With the large number of possible combinations of policy objectives and governance approaches, the Report limits its consideration of this issue to program costs and transition from existing programs.

1. **Program Costs.** Program costs comprise the cost of delivering programs, any incentives paid, and administrative costs. The program delivery costs and incentives depend largely on the scale of DSM efforts. Experiences of other states studied by the American Council for an Energy Efficiency Economy suggests that one percent of utility revenue is a likely "floor" of needed funding for a statewide program that addresses the available efficiency potential. The other cost component -administrative costs- needs to be added to these costs and can be estimated as a percentage of the overall effort. According to the Report, while costs may be lower, total administrative costs can be expected to range between 10 and 15 percent of total portfolio costs depending on the existing capabilities of the administering entity and the level of evaluation activity. *Id.* at 31

2. **Transition of Utility Legacy Programs.** The Stratton Report concludes that if a statewide program is to provide consistent offerings to all residents, then existing programs will need to be replaced, or folded into, the statewide effort. Given the nature of existing programs in Indiana, this effort should occur relatively seamlessly. To facilitate a smooth transition, the Report recommends that any existing programs be kept in place until new offerings are ready to be rolled out. *Id.*

J. **Overall Conclusions of the Stratton Report.** Ms. Stratton concluded her testimony by referencing conclusions in the Report that indicate that the fractured nature of Demand Side Management programs in the state places Indiana in a good position to move toward a more consistent statewide DSM effort. This conclusion is based on overall findings contained in the Report which are summarized as follows:

- **Inconsistent Patchwork of DSM Programs.** The current approach to DSM in Indiana provides an inconsistent patchwork that excludes some customers (geographically and by sector) from the benefits of energy efficiency services.
- **High Energy Consumption.** Indiana has high energy consumption, even when compared to other manufacturing intensive states, which offsets low energy prices and results in overall energy costs that could be reduced through energy efficiency.
- **Benefits of Reduced Energy Costs.** Where attainable in cost-effective manner – reduced energy costs provide overall benefits to the economy.
- **Environmental Issues.** Environmental issues regarding new or increased regulatory requirements associated with energy

generation and consumption provide an additional justification to increase emphasis on energy-efficiency.

See, Report at 33

Notwithstanding the identification of these issues, the Stratton Report concludes that Indiana is not yet ready to select an administrative model for improved DSM throughout the state. According to the Report, the primary obstacle to the development of a cohesive statewide DSM effort is the current inconsistent effort regarding DSM across the state and the absence of clearly enunciated policy objectives necessary to address the issue in a comprehensive fashion.

Although policy objectives need to be a primary driver of the administrative structure for any statewide DSM efforts, Indiana's current DSM environment does provide some guidance that should be considered when making choices about an appropriate policy-driven governance approach. According to the Energy Center Report, these existing attributes represent some of the "building blocks" from which any statewide DSM programs would need to be built. Each of the following topics are discussed in the Report:

- **In-State Expertise with DSM Program Design and Delivery.** Current in-state experience with DSM appears to be concentrated among a small number of utilities. Reliance on out-of-state consultants is high for functions such as DSM program screening, assessment of energy efficiency potential, and delivery of programs. Development of a statewide DSM program would require the creation of additional expertise regardless of the administrative model chosen. As such, Indiana's current experience does not necessarily favor any particular administrative model. *Id.* at 33.
- **Strong Stakeholder Involvement.** Indiana's reliance on stakeholder input provides a solid foundation on which a stakeholder process for a statewide DSM program can be built. Depending on the policy objectives established for such a program, environmental and economic development interests may need to be added to this process. *Id.* at 34
- **Collaborative Orientation of Existing Programs.** There is a history of collaboration among several utilities and other stakeholders. This experience provides a basis for multi-utility administered approaches to a statewide DSM program if other factors suggest that such an approach is appropriate for Indiana. *Id.*
- **Utility-Specific Planning Process.** The utility-centric nature of the integrated resources planning process has resulted in parallel efforts by the utilities to identify and evaluate potential DSM measures, as well as market and potential studies that cover only

individual utility service areas. This approach to planning and data collection for DSM programs provides a barrier to effective implementation of statewide programs regardless of administrative and delivery model. *Id.*

- **Diverse Corporate Profiles of Utilities.** Indiana's major utilities range from geographically small companies that serve only Indiana to subsidiaries of multi-state corporations. There are utilities on both ends of the spectrum with and without active DSM programs in Indiana, although the multi-state utilities have programs outside the state. This mix would provide a modest (but by no means insurmountable) barrier to developing consistent utility-administered programs with a statewide focus. *Id.*
- **DSM Administrative Precedents.** Existing and emerging programs generally have established the utility service area as the geographic reach of programs with utility administration in the electric sector. A statewide program will need to transcend utility boundaries in some way. The use of both utility and third-party administration offers little guidance, although the utility administration has much longer historic roots. *Id.*
- **Role of Coal in the State's Economy.** Coal is an important natural and economic resource in Indiana, which would suggest its continued use. Because energy consumption is increasing annually throughout the American economy there is no need to see energy efficiency as a threat to the development of Indiana's coal resources. As a result, we see the role of coal in Indiana as an issue to be considered when choosing fuel sources and technology of new power plants and when marketing energy-efficiency's environmental benefits over the use of coal-based power, but not as a factor in the establishment of a statewide DSM program. *Id.*
- **Role of Energy-Intensive Industry in Economy.** Indiana's economy includes a fair amount of energy intensive manufacturing, which has resulted in a strong voice for low energy prices for this sector. This customer class' apparent preferences would suggest that opt-out provisions should be considered for customers whose in-house energy practices already are consistent with the societal and economic needs to be addressed by DSM programs. However, the Report concludes that the cost-effective energy-saving potential within the industrial sector needs to be considered before such decisions can be made and that this sector's energy needs should be seen in light of energy costs, not energy prices. *Id.* at 34-35

- **Existing DSM Requirements.** The existing requirements that utilities explore DSM programs as part of their integrated resource planning process provides a mechanism through which the Commission could provide further instructions to utilities concerning the scale or scope of such efforts and possibly the expectation that DSM programs be implemented in a coordinated, statewide fashion. The use of regulatory requirements in this manner lends itself to administrative delivery models over which utilities have responsibility, but not to models in which third party administrators operate independently of utilities. *Id.* at 35.
- **Role of Program Branding.** Current programs are branded with the utilities' name rather than an umbrella brand for the state. Should the Commission decide on an overall brand/communication strategy for a utility administered program, it would be appropriate to allow a co-branding approach to give customers confidence that the utilities are still behind the program. *Id.*

Ms. Stratton testified, consistent with findings contained in the Report, that the next step for Indiana's deliberations regarding a statewide DSM approach lies with the Indiana Utility Regulatory Commission. In particular, she recommended that the Commission establish the policy objectives it wishes to achieve through DSM efforts in Indiana. According to Ms. Stratton, policy discussions and statements should specify the goals that statewide DSM programs are to achieve, such as whether demand reduction or overall consumption is of primary concern.

With policy objectives in hand, the Commission can then begin to consider the building blocks and overall framework discussed in the Report. Ms. Stratton recommended that this process include discussions with stakeholders representing, at minimum, the utility industry and broad representation of energy consumers. Critical issues to Indiana -such as economic development, environmental quality, and preparing for potential future carbon constraints- need to be included in discussions about the balance between energy generation and energy efficiency. Broadening the discussion to include economic development and environmentally oriented policymakers and interests would help address this need.

In reaching these conclusions and making these recommendations, Ms. Stratton suggested that one possible way to hold this discussion would be through facilitated stakeholder meetings held throughout the state. However these discussions are organized, they should remain focused on the best ways for Indiana to achieve the policy objectives identified by the Commission. The policy objectives and input from stakeholders can then be used to develop both a long-range plan for DSM efforts in Indiana and a transition plan that maps out the path from the current efforts to the vision outlined in the long-range plan.

4. **Direct Testimony Presented by Respondent or Intervening Utilities.** Duke, I&M, IPL, NIPSCO, and Vectren, (collectively "Sponsoring Utilities"), submitted a joint responsive exhibit ("Responsive Exhibit"). The Sponsoring Utilities testified that Indiana

already has policy objectives for DSM efforts that were enacted by the Commission following the passage of the National Energy Policy Act of 1992. *See*, 170 IAC 4-8-3. The Sponsoring Utilities also pointed to the Energy Policy Act of 2005 (“EPAAct 05”) and the “Economic Growth from Hoosier Homegrown Energy, Indiana’s Strategic Energy Plan” (“Homegrown Energy Plan”) which sets forth additional policies and statewide objectives on DSM.

With respect to administrative models available for DSM programs, the Sponsoring Utilities encouraged the Commission to continue to use the Single Utility Model. The Sponsoring Utilities stated that a utility specific approach allows utilities to tailor programs to the different qualities of their service territories. The Sponsoring Utilities also noted that there are a number of examples where utilities have worked cooperatively on programs. The Sponsoring Utilities noted that Vectren, Duke Energy, IPL and I&M all have market potential studies in some stage of development. The Sponsoring Utilities expressed concern that a statewide market potential study would only duplicate these efforts and be an inefficient use of the scarce resources of utilities, shareholders, and customers.

In their Responsive Exhibit, the Sponsoring Utilities also expressed concern regarding what they contended to be the Stratton Report’s emphasis on statewide programs. Additionally, the Sponsoring Utilities testified that under the existing DSM rules, they believe that the utility-specific model has worked efficiently and effectively in Indiana. The Sponsoring Utilities concluded that they believe that the current framework sets forth reasonable objectives which have resulted in significant DSM initiatives in Indiana. The Sponsoring Utilities further testified that the Commission’s existing DSM rules provide for program cost recovery, lost revenue collection, and the incentives necessary to achieve the comparability of demand-side and supply-side options. Finally, the Sponsoring Utilities indicated that if statewide programs are appropriate, there are reasons it may be desirable to create such programs through a legislative process rather than a process at the Commission. However, notwithstanding these issues, the Sponsoring Utilities indicated they would support a series of workshops to allow for further dialog on the issues and conclusions presented by the Energy Center Report.

The Sponsoring Utilities did not recommend any changes to the cost recovery rules regarding DSM programs. They stated that the concept that utilities should be allowed timely and complete cost recovery via customer rates is already well established in Indiana and should continue under any new DSM program. The Sponsoring Utilities testified that to the extent costs do change, to provide incentives to utilities to pursue DSM, the Commission should continue to make tracking mechanisms available for cost recovery. The Sponsoring Utilities also commented on measurement and verification aspects of DSM programs and agreed that these steps are critical components to such programs. However, the Sponsoring Utilities cautioned that the Commission should not create a system that makes measurement and verification onerous and expensive, because that would result in funds being diverted from program implementation to program overhead.

With regard to the conclusion in the Energy Center Report that Indiana’s energy environment is characterized by low energy prices, high consumption and that Indiana is below average in spending for energy efficiency, the Sponsoring Utilities testified that lower prices do not provide as much motivation or incentive to reduce energy consumption. The Sponsoring

Utilities cautioned against state-to-state comparisons of energy efficiency spending and activity, as well as in policy development generally.

The Sponsoring Utilities responded to the Energy Center Report regarding cost tests used in DSM proceedings. The Sponsoring Utilities noted 170 IAC 4-7-7 requires the participant test, the ratepayer impact measure, utility cost test, and total resource test. The Sponsoring Utilities testified that each test has strengths and weaknesses in evaluating the net benefit from various viewpoints and the Commission should not adopt one type of test over another.

With regard to administrative costs, the Sponsoring Utilities testified that costs are program specific and dependent on numerous program attributes so that it cannot be assumed that DSM administrative costs will fall within a range of ten percent to fifteen percent of total costs. The Sponsoring Utilities testified in order to assure consistency in measuring the efficacy of DSM programs, it may be necessary to adopt evaluation standards which require specified levels of marketing, measurement and verification costs that may push total administrative costs above the ten to fifteen percent range.

The Sponsoring Utilities also testified that differences between electric and natural gas DSM are significant enough that separate proceedings are merited to consider natural gas programs. The Sponsoring Utilities noted that electric DSM programs have a longer history and are tied to construction issues. Natural gas DSM, on the other hand, is tied to the purchase of natural gas.

In addition to the Responsive Exhibit, several Utility Respondents or Intervenors also submitted separate testimony in this proceeding. In addition to participating as a sponsor to the Responsive Exhibit, Duke Energy Indiana submitted the direct testimony of Theodore E. Schultz. Mr. Schultz, while noting the integrated resource plan ("IRP") rules, was supportive of other efforts to expand on the state's energy efficiency policy. Mr. Schultz offered suggestions on what statewide policy objectives should be, including, leveraging expertise and other resources to keep DSM costs down, create utility incentives for DSM achievements, expand DSM programs to achieve all cost-effective DSM, provide allowances for creativity and flexibility, and provide for the creation of a comprehensive set of utility sponsored DSM for a variety of customer classes. Mr. Schultz testified that Duke recognizes there may be a need for a large business customer classification that only focuses on access to demand response since those sophisticated customers may have already implemented cost-effective DSM programs on their own.

IPL submitted the testimony of Lester H. Allen. Mr. Allen testified that IPL has a pending request to extend its existing DSM programs for 2 years. He testified that extending the programs should provide for continuity of the current programs and provide the Commission with additional information that could be useful in this investigation.

Vectren submitted the testimony of Douglas A. Karl. Mr. Karl testified that since submitting information to the Energy Center on interruptible tariffs, that a settlement agreement has been entered into that provides for the implementation of new interruptible tariffs. Mr. Karl also testified that Vectren does track its utility staffing for its DSM programs. Finally, Mr. Karl

stated that Vectren South has worked collaboratively with stakeholders on a Market Potential Study and plans to submit a DSM plan to the Commission.

NIPSCO submitted the testimony of Barbara A. Penkala. Ms. Penkala testified that NIPSCO is presently engaged in evaluating DSM options and demand response rate designs for implementation in the near future. She testified that NIPSCO anticipates that its 2007 IRP will contain one or more DSM programs not presently offered. Ms. Penkala also testified that NIPSCO has a low income weatherization program and an educational program that relate to DSM, but were not included in the Energy Center Report.

Intervenor Wabash Valley filed the testimony of Cathy L. Ellis. Ms. Ellis testified that Wabash Valley and its member cooperatives are currently active in various DSM initiatives, including residential and agricultural peak reduction, commercial and industrial interruptible load, and residential and commercial energy efficiency education and support. She stated that the single utility model has been effective for its programs. Ms. Ellis testified that if Wabash Valley is identified as a utility participant in a statewide initiative, it would like to be included as a stakeholder in any discussions moving forward.

5. Direct Testimony of the Indiana Industrial Group. Nicholas Phillips, Jr. testified on behalf of the Indiana Industrial Group. Mr. Phillips recommended that the Commission continue to consider DSM programs as part of the IRP process for each electric utility. He testified that through the IRP, both supply-side and demand-side resources can be considered as alternatives. Mr. Phillips also testified that the objective of the IRP is to provide utility services at the lowest overall reasonable cost, consistent with service that is safe, reliable and in accord with all regulatory requirements. Mr. Phillips testified that the uniqueness of each individual utility system and each utility IRP makes the establishment of DSM targets invalid and inappropriate. The Industrial Group recommended against setting any type of DSM target or mandatory amount of DSM. Mr. Phillips while recommending that the Commission continue its IRP process, noted that if the Commission determines there is insufficient opportunity for it to encourage or approve DSM programs through the IRP process, that any new policy under consideration should be directed toward the enhancement of the IRP process.

Mr. Phillips testified that historically, DSM programs have not targeted large industrial customers. According to Mr. Phillips, large industrial customers have unique manufacturing processes and internal engineering staffs which continually review and implement DSM and energy efficiency measures to remain competitive. Mr. Phillips testified that he believes that self-directed programs of industrial customers based on market forces are more efficient than utility DSM programs as self-directed programs result in investment on the customer's side of the meter without the cost of utility administration. Mr. Phillips also indicated that generally more DSM can be achieved per dollar expenditure than is the case with the utility funded programs. Finally, Mr. Phillips testified that self-directed DSM programs can be implemented much sooner than utility sponsored programs which often require pilot programs or regulatory approval before going into effect.

Mr. Phillips drew a distinction between DSM programs and demand response programs, which he called tariff-based DSM. Mr. Phillips recommended that tariff-based DSM be offered

to customers as part of cost-based ratemaking programs. He noted that the Commission is investigating Section 1252 of the EPAct 05, in Cause Number 43083.³

Finally, Mr. Phillips noted that increased conservation and DSM activity by Indiana ratepayers does not automatically result in any less generation activity by Indiana utilities. He testified that the output from generation plants in Indiana is also influenced by off-system sales, often to other states. Therefore, he cautioned that reduced consumption by retail ratepayers in Indiana may simply allow utilities to sell more power (and earn more profit) from sales to other markets. According to Mr. Phillips, it would be particularly unfair to implement conservation and DSM programs that would not result in an overall reduction in generation from Indiana plants while providing additional profits to utilities.

6. Direct Testimony Presented by the OUCC. Barbara A. Smith testified on behalf of the OUCC. In her testimony, Ms. Smith was supportive of the Energy Center Report and its conclusion that Indiana can benefit from coordination of its DSM programs on a statewide basis. The OUCC recommended that any decision about whether programs should be utility led or administered by an independent third-party be made with stakeholder input after the Commission articulates statewide policy objectives to be achieved with the implementation of any DSM program. Ms. Smith testified that the OUCC believes that the Commission has the authority it needs to issue appropriate and enforceable orders regarding DSM in Indiana, noting the DSM guidelines and rules contained in 170 IAC 4-8-3. Ms. Smith also noted the Homegrown Energy Plan and its reference to energy efficiency efforts.

Ms. Smith testified that having a statewide DSM effort does not necessarily mean that each utility has to have the same programs. She testified that program differences should be based on their respective cost effectiveness based on an individual utility's avoided costs. Ms. Smith stated that the OUCC recommends that the Commission host a series of workshops to allow Commission staff and stakeholders to discuss the issues raised in this proceeding and to collaborate and develop well-defined DSM policy objectives for Indiana. Ms. Smith also indicated that the OUCC encourages the development of a uniform DSM database, using market potential studies that are currently underway to shape future programs and to consider DSM programs in Indiana.

In reaching these conclusions, the OUCC also recommended that the Commission limit this proceeding to electric and steam utilities. The OUCC noted that the three major natural gas utilities are actively engaged in energy efficiency/DSM initiatives. It noted that all three natural gas utilities' programs were relatively new and each utility had spent considerable time and effort to work with the OUCC and other interested stakeholders to design programs that best meet the specific requirements of their customers. The OUCC recommended that the programs should proceed, unencumbered but along a parallel path with this proceeding.

7. Direct Testimony Presented by the CAC. Grant Smith testified on behalf of the CAC and expressed support for the Energy Center Report and additional DSM efforts generally. Mr. Smith was supportive of the Energy Center's suggestion to develop policy goals. He

³ An Order was issued by the Commission in that Cause on August 1, 2007.

testified that the overriding obligation of utilities is to provide least cost service and that DSM programs are a critical component of providing least cost service. Mr. Smith testified that energy efficiency resources are available and that such programs are typically cost-effective and provide economic, community development, and environmental benefits. Mr. Smith stated that a statewide program would promote equity and consistency.

With respect to administration of DSM programs, Mr. Smith indicated that it was important for the Commission to consider different options for the implementation of DSM, and that Indiana should pursue a path that allows for effective and cost-efficient delivery. In an effort to accomplish this objective, the CAC recommended the development and utilization of an independent statewide administrative model (Third Party Administrator Model). The CAC noted that some utilities are already moving toward implementing gas DSM programs with independent administration.

With respect to funding, Mr. Smith recommended that funding be achieved through some sort of similar rate mechanism between all utilities or through a legislated tax or surcharge (systems benefits charge). Mr. Smith testified that he believes that third-party administration offers an effective means to prevent conflict and would eliminate any disincentive toward DSM on the part of the utilities. In reviewing any proposals for lost margin recovery, Mr. Smith urged the Commission to look carefully at what portion of the utility's actual margin is at risk. He further stated that any lost margin recovery should be based on company specific actual use data and not projections. Finally, Mr. Smith testified that the level of program funding should be sufficient to make a substantial impact on the energy efficiency industry. Ideally, the CAC would like to see budgets be large enough to support all cost-effective energy efficiency programs and to achieve market transformation of key efficiency measures.

Mr. Smith was supportive of the Energy Center's recommendation to go beyond stand-alone utility market potential studies and proposed several alternatives to existing market potential studies. Mr. Smith testified that he believes that some DSM programs can be proposed and implemented without a market potential study. Mr. Smith recommended the development of a statewide program that relies on an independent administrator. Such a program could develop a "best practices" portfolio and perform a statewide analysis which would be used for future modifications and refinements of DSM programs. In the alternative, Mr. Smith recommended that the Commission develop a core group of "best practices" programs for utilities to implement in a prescribed way that would provide the framework necessary for the timely transition to a statewide program.

With regard to the approach to DSM, Mr. Smith disagreed with the Energy Center Report, to the extent that it suggested that Indiana should decide between resource acquisition and market transformation as these are not mutually exclusive approaches. Mr. Smith supported working toward some degree of geographic uniformity with respect to DSM. However, he stated that the policy goals should be to achieve cost effective DSM, and that data should determine which programs are cost effective and which market sectors should be targeted. According to Mr. Smith, policy development regarding non-homogeneous customers, such as commercial and industrial customers with unique attributes, may require and should receive unique approaches. The CAC agreed with other parties that stakeholder involvement is critical to the success of

DSM programs. Mr. Smith testified that a statewide and/or third-party administration model offered potential for greater and more equal stakeholder participation.

The CAC's testimony also discussed several cost-effectiveness tests including the participant test, energy system test, total resource cost test, societal cost test, and ratepayer impact measure test. Mr. Smith recommended that the Commission adopt the societal cost test or the energy system test for screening energy efficiency measures and programs. The CAC also recommended that the Commission adopt, at a minimum, several program goals to advance the design and delivery of well-designed DSM programs. These included, seeking opportunities to overcome existing market barriers, and minimizing "lost opportunities" and "cream skimming." Additional program goals should be designed to provide efficiency savings for all types of customer classes and sub-classes; be cost effective by design; and address as many different cost-effective end-uses as possible.

The CAC further recommended that the Commission adopt specific requirements for DSM program implementation in order to allow for the development of a consistent program design, incentives and eligibility criteria, "whole-house" or "whole-building" approaches, development of strategic partnership, continual update of programs to deliver maximum savings while reducing free ridership, and a comprehensive portfolio of programs.

8. Reply Testimony Presented by Respondents or Intervening Utilities. In their Joint Reply the Sponsoring Utilities indicated that, while they would be willing to participate in a collaborative as suggested by the OUCC they also noted that the Commission already has an articulated policy which provides a regulatory framework to consider DSM through the IRP process. In response to the OUCC's recommendation regarding the creation of a statewide database, the Sponsoring Utilities indicated they would be willing to work with the OUCC on such an undertaking with the understanding that the cost of such a database would be borne by the State Utility Forecasting Group or the Commission. In response to the OUCC's proposal to address cost recovery, the Sponsoring Utilities indicated that the OUCC had not identified any deficiency in the Commission's current rules regarding program cost recovery mechanisms.

In response to comments from the OUCC and CAC that suggest Indiana lags the nation and some other states in spending for energy efficiency, the Sponsoring Utilities testified that the Energy Information Administration ("EIA") recently began showing data that summarizes energy usage and energy availability in each state. According to the Sponsoring Utilities, the EIA reported that Indiana's per capita electric consumption is above normal due to its energy intensive industry and that the state's household electric consumption is below the national average. Therefore, the Sponsoring Utilities testified that caution should be exercised when comparing Indiana's energy intensities with the energy intensity of consumers in other states.

The Sponsoring Utilities further testified that large commercial and industrial customers have already undertaken energy efficiency measures that benefit their business. The Sponsoring Utilities disagreed with CAC's testimony that no utility has any significant industrial programs, and agreed with the Industrial Group that large commercial and industrial customers have pursued self-directed programs. Furthermore, the Sponsoring Utilities also testified that each of

the individual utilities have significant and effective commercial and industrial DSM programs consisting of various tariff offerings, which provide incentives for cost-effective DSM.

The Sponsoring Utilities also indicated that they do not support a "one-size-fits-all" statewide DSM program as Indiana has unique customer and utility characteristics that vary across service territories. Furthermore, the Sponsoring Utilities contended that there are significant differences between utilities, including the general cost structure of service areas that can lead to quite different, yet appropriate decisions regarding DSM implementation. They further testified that DSM programs are highly customer and end-use specific and that a particular utility's mix of customers and end-usage will have a strong influence on opportunities for cost-effective DSM programs.

The Sponsoring Utilities disagreed with the CAC's testimony that utilities have incentives to increase sales to increase profits, and that this creates a conflict with the goal of providing least-cost energy services to ratepayers. They testified that the IRP process attempts to eliminate or offset regulatory or financial bias against DSM. The Sponsoring Utilities testified that adherence to the existing rules which provide for recovery of direct and administrative costs of the programs, as well as lost margins from declining energy use and incentives accomplish the objective of encouraging DSM. The Sponsoring Utilities further testified that their ability to communicate and affect energy efficiency in an established environment of trust and credibility is an advantage over third-party administration. The Sponsoring Utilities pointed to demonstrated success in customizing DSM to specific customer segments with regard to commercial, industrial and residential customers.

With regard to CAC's recommendations of various requirements for DSM programs and implementation, the Sponsoring Utilities testified that many of the CAC's recommendations seemed beyond the jurisdiction of the Commission and if they are thought appropriate, would be better addressed as a legislative matter. The Sponsoring Utilities concurred with Mr. Phillips' recommendation that DSM programs be considered as part of the IRP process and be implemented on a utility by utility basis. They testified that rate design issues or the appropriate treatment of off-system sales were not appropriately considered in the initial phase of this proceeding.

In addition to the Joint Reply, several Utility Respondents or Intervenors submitted separate reply testimony in this proceeding. IPL submitted reply testimony of Lester H. Allen. Mr. Allen disagreed with the CAC's assertion that IPL's DSM program is relatively modest. He testified that IPL has offered DSM programs continuously since 1993 and that the programs have resulted in energy efficiency programs with approximately 65 MW in demand reduction. Mr. Allen also testified that IPL has participated in dual fuel programs and stated that such programs can be successfully implemented without the need for a statewide DSM program or third-party administrator.

Duke Energy Indiana submitted the reply testimony of Theodore E. Schultz. Mr. Schultz testified that Duke agrees with the OUCC's comments that the Commission should not endorse the concept of third-party administration in the context of this phase of the Commission's investigation. Furthermore, he testified that Duke did not believe that third-party administration

is in the best interest of consumers or utilities. According to Mr. Schultz, utilities have the expertise, infrastructure and customer relationships to provide universal access to energy efficiency services and new technology. Mr. Schultz indicated that collective efforts are better spent on developing an approach to energy efficiency that enables the State of Indiana to leverage the capabilities that exist within utilities. With regard to the OUCC's suggestion to create a statewide database, Mr. Schultz testified that there are already publicly filed documents that contain the necessary information to evaluate DSM program activity and impact. He stated while Duke Energy Indiana was not opposed to the creation of a database, it felt that additional reporting requirements should be minimized and that utilities should not be responsible for costs of administering the database.

In response to issues presented by the CAC in its testimony with respect to Duke, Mr. Schultz testified that Duke estimates it has saved 161 megawatts over the past fifteen years through its DSM program offerings. Mr. Schultz testified that Duke does not believe in a one-size-fits-all approach. He also stated that Duke strongly believes that utilities should deliver DSM programs to their customers rather than have this function performed by a third-party administrator. Mr. Schultz also discussed Duke's current efforts through its DSM collaborative to conduct a market potential study and to then meet and discuss program options and recovery methods. Mr. Schultz disagreed with the CAC's recommendation that the societal cost test be utilized for evaluating the cost-effectiveness of DSM programs. According to Mr. Schultz, the utility cost test and participant test should be utilized as the use of the societal cost test, as the sole criteria by which a DSM program is selected, could result in over-spending on programs.

In response to the Industrial Group, Mr. Schultz testified that Duke agreed that DSM should be included in the IRP process. With regard to Mr. Phillips' testimony about industrial customers participating in DSM activity, Mr. Schultz indicated that Duke generally believes that all customer segments benefit from DSM activity but recognizes that some of the largest business customers may have already invested in energy efficiency. According to Mr. Schultz, these customers should have an opportunity to opt out of paying for energy efficiency programs, but not for demand response programs. However, Mr. Schultz testified that this issue should be discussed further and encouraged the Commission to include all customer segments in the development of policy goals.

9. Reply Testimony of the Indiana Industrial Group. Nicholas Phillips sponsored reply testimony on behalf of the Indiana Industrial Group and testified that he agreed with the CAC and others that DSM is a component of a utility's least cost planning. Accordingly, he testified that just as each IRP is unique for each utility, each DSM portfolio will be unique to utilities in Indiana. Mr. Phillips also testified that he believes that utility sponsored administration is appropriate as each utility has the responsibility to perform an IRP and to provide safe, reliable service based on least-cost standard to ratepayers within its service territory. According to Mr. Phillips, a third-party administrator would not have knowledge of each utility's IRP and would not have the responsibility to provide safe, reliable electric service at the lowest possible cost to ratepayers. Mr. Phillips testified that he agreed with the OUCC and Sponsoring Utilities testimony that this proceeding should be limited to electric utilities and exclude gas utilities.

Mr. Phillips responded to the CAC's testimony that there are no electric DSM programs for large commercial or industrial customers and indicated that this is not a concern as large industrial customers engage in self-directed energy efficiency programs through which the customer makes the investment rather than the utility. He further stated that these customers frequently have highly specialized plants or processes with technical resources of their own. He also testified that the CAC's comments overlook the fact that some of these customers also participate in demand response programs if suitable programs are offered by their utility.

With regard to determining the cost-effectiveness of various DSM options, Mr. Phillips stated he did not believe it was appropriate to mandate which tests the utilities should use in their IRP process at this time. However, he recommended the use of the participant test and the non-participant test or ratepayer impact measure test.

Mr. Phillips testified that the Commission should not mandate a system benefits charge or like funding mechanism that would increase rates to ratepayers and fund various DSM programs. He called the system benefits fund a tax on ratepayers. He testified that the cost of DSM should be considered through the IRP process, including any incentives, and both should be considered as a rate increase to ratepayers and treated with appropriate procedures to protect ratepayers from excessive increases. For this reason, he pointed out that DSM measures do not always require rate increases and funding mechanisms, as shown by recent experience in the gas industry where very real reductions in gas usage have occurred without the creation of surcharges.

10. Reply Testimony of the OUCC. In her reply testimony Ms. Smith recommended that the Commission not include cost recovery for DSM programs in this proceeding. According to Ms. Smith, the establishment of a statewide program is necessary regardless of the approach for cost recovery. Ms. Smith also testified that all parties to the proceeding should continue to engage with regional transmission organizations to pursue demand response initiatives. She also agreed with IPL's testimony that existing programs should continue until policies or programs established by this proceeding are implemented.

11. Reply Testimony of the CAC. In his reply testimony Mr. Smith indicated that he does not believe that the IRP process alone can determine if utilities are employing and developing adequate DSM. Mr. Smith testified that while stakeholder input is critical it should not serve to delay DSM initiatives or efforts in this proceeding. Mr. Smith testified that a statewide program administered by a third-party administrator could reach all Hoosiers regardless of their utility or energy supplier and indicated that the Commission has the requisite authority to promote DSM in this matter.

Mr. Smith testified in response to the Sponsoring Utilities testimony in support of the single utility model and their contention that utilities are natural providers of DSM. According to Mr. Smith, such a conclusion is contradicted by indications from the Sponsoring Utilities that utilities need decoupling, lost-margin recovery and incentives in order to be effective DSM providers. He testified that if DSM is so natural to the utilities, they should not require additional incentives to encourage the implementation of such programs. Mr. Smith further testified that he believes that a statewide market potential study would not duplicate other studies and could focus on more customer types and end-uses than has been done in the past. Mr. Smith

indicated that he believes that a statewide program could also offer more types of programs than a single utility could offer.

Mr. Smith disagreed with Mr. Phillips recommendation to allow industrial customers to pursue self-directed DSM programs. Mr. Smith testified that industrial customers should participate in and fund DSM programs, however, he also stated that such programs need to be carefully crafted to accommodate the specific and sometimes unique needs of those customers. Mr. Smith also stated that other jurisdictions have programs that are targeted at large end-users. With regard to the continued inclusion of natural gas utilities in this proceeding, Mr. Smith disagreed with the Sponsoring Utility testimony that different rate recovery mechanisms are needed for gas and electric utilities. While he testified that issues such as decoupling may best be resolved in a separate proceeding, he also indicated that this should not be a deterrent to a statewide program.

12. Discussion and Findings of the Commission. We began this investigation in order to examine the overall level and effectiveness of DSM Programs in the State of Indiana and to allow for the consideration of issues that may lead to the enhancement of DSM efforts statewide. We further indicated that our review of the issues would include consideration as to whether an independent DSM administrator model should be established in Indiana on a statewide basis. To facilitate our evaluation of the issues we obtained the assistance of the Energy Center of Wisconsin, a not-for-profit organization with experience in the design and implementation of DSM programs. Through the cooperation of the parties and the efforts of Testimonial Staff, which resulted in the completion of the Stratton Report, the Commission has obtained substantial information regarding existing DSM tariffs and programs, and an overview of issues for our consideration in determining how best to proceed with efforts to enhance DSM programs throughout Indiana.

The Stratton Report indicates that prior to moving forward to the second phase of this proceeding it is of central importance that the Commission establish an overarching purpose in defining the administrative structure, delivery model, and other components of an energy efficiency initiative. The Report points out that absent such initial guidance, components of the DSM portfolio may pursue competing goals or fail to accomplish the State's greatest needs cost-effectively. Similarly, an overall policy statement can provide guidance concerning the scope of the DSM programs on other critical factors in which policymakers have a clear goal.

Based on the evidence presented in this matter, and the recommendations contained in the Stratton Report, we find that a second phase of this proceeding is necessary to seek input on the development of statewide policy objectives necessary to improve the existing approach to DSM in Indiana and to develop a proposed path that will address the issues identified and discussed in the Report. In reaching this conclusion we set forth the following overview of issues and determinations reached in this matter that will form the foundation for our consideration of the issues in the second phase of this proceeding.

A. Overview of Issues.

1. Inconsistent Patchwork of DSM Programs. As discussed by the Commission in Cause No. 42418, and confirmed in the Stratton Report, the current approach to DSM in Indiana has resulted in an inconsistent patchwork of programs that exclude customers, geographically and by sector, from the benefits of energy efficiency services. This fact is specifically borne out in the Report and was not refuted by any testimony presented in this Cause.

With respect to tariffs or programs intended primarily to reduce peak demand, jurisdictional electric utilities in the state offer a degree of uniformity in offerings. However, there is much room for an increased number of programs and improved levels of participation. With respect to electric industry DSM Programs that result in a reduction in overall consumption, the Report concludes that efforts to actually reduce electric consumption in Indiana are concentrated among two utilities with little activity elsewhere in the State. This determination is perhaps the most troubling finding contained in the Stratton Report as it is unmistakable that the current procedure, in which jurisdictional utilities consider DSM as part of their IRPs, and propose DSM programs to the Commission at their discretion, has failed to lead to the creation and implementation of creative, effective, predictable, and comprehensive DSM Programs throughout the State.

In considering the issue of the existing inconsistent patchwork of DSM programs in Indiana as part of this proceeding, it is not the Commission's expectation that uniform and ubiquitous coverage of effective DSM Programs will appear across the state overnight. Rather, the initial focus of this effort will be the consideration of the steps that must be taken by those utilities that are currently doing little or nothing with respect to DSM to do something, while also considering the steps that must be taken by utilities that have existing DSM Programs to do more. Satisfaction by any utility regarding their respective existing DSM efforts, or the efficacy of the current regulatory approach to DSM in the state, would be misplaced in considering this issue as part of this investigation. Based on the findings in the Stratton Report it is clear that all electric utilities can improve with respect to the development and implementation of effective DSM programs.

In applying these to-be-determined objectives, we are mindful that each utility in Indiana has undertaken DSM to a greater or lesser degree; has a different cost structure; different generation mix; and, different service territories. Therefore, we find that a collaborative process shall initially be undertaken to determine if there are elements of successful programs that can be incorporated into broad, statewide DSM policy objectives and possibly into other utility-specific programs.

In undertaking this effort, we note that the Sponsoring Utilities indicated in this proceeding that they utilize independent contractors for many DSM efforts. We find that the creation of a degree of uniformity with respect to a base level of programs could prove to be a beneficial first step in addressing the current inconsistent patchwork of programs. As part of such an effort, we recognize that assistance by contractors could be improved through the creation of a degree of uniformity as it would eliminate the need for individualized training with

respect to many DSM programs. This initial, but important, first step could play an important role in reducing overall costs through the creation of uniformity with respect to DSM on a statewide basis.

It is our expectation that the parameters for consideration of this issue will be fully considered and reviewed in Phase II of this proceeding and will result in the development of a critical path forward for the overall improvement of DSM programs in Indiana. Additionally, it is our hope that Phase II of this proceeding will attract the active involvement of even those utilities that fall outside the jurisdiction of the Commission as the broad DSM issues being analyzed and developed should prove beneficial to all participants.

2. Low Overall Spending on DSM. Additionally, according to the Stratton Report, Indiana lags well behind its neighboring states--and the nation as a whole--with respect to spending on DSM. Indiana currently ranks 31st nationally and 6th among 7 Midwestern states in spending for electric energy efficiency - both on a per capita basis and as a percentage of utility revenue. Report at 18. According to the Report, experiences of other states studied by the American Council for an Energy Efficiency Economy suggests that one percent of utility revenue is a likely "floor" of needed funding for a statewide program that addresses the available efficiency potential. Report at 31. Based on findings in the Report, Indiana's expenditures on energy efficiency, as a percentage of utility revenues in 2003, was one-tenth of one percent.

While the Commission recognizes that increased spending alone will not substitute for the effective development and consideration of DSM Programs in Indiana, current spending levels, when viewed in conjunction with the dearth of existing DSM Programs in the state, demonstrates that the opportunity exists to do much more with respect to DSM in a cost effective manner. Therefore, Phase II of this proceeding shall also include consideration of how the enhancement of overall DSM efforts in the state will impact Indiana's current standing with respect to DSM spending in the Midwest region and nationally. In considering this issue the parties should carefully review expenditures for DSM in surrounding states, as discussed in the Stratton Report, and offer specific proposals that will enhance and improve Indiana's overall standing in this area. As the Stratton Report concludes that Indiana has lagged behind its neighboring states with respect to DSM, cost recovery issues (or issues of past cost savings due to a lack of DSM Programs) should not be central to the discussion of this issue in the near term.

3. High Energy Consumption. The second phase of this proceeding must also consider the issue of high overall energy consumption in the State. While the Stratton Report finds that Indiana enjoys relatively low energy prices that present potential cost savings to consumers, the Report also finds that much of these savings are eroded by high overall energy costs.

The Stratton Report specifically addresses the issue of energy costs and concludes that compared to other states Indiana's energy environment is characterized by low energy prices and high energy consumption. While Indiana ranked 47th among the 50 states and the District of Columbia in the cost of retail electricity and all energy sources in 2003, the state has relatively high energy consumption, ranking sixth in total energy consumption per capita. Report at 11. According to the Stratton Report, compared to the rest of the country, Indiana's combination of low prices and high spending results in moderate per-capita spending for electricity and a high

level of overall expenditures on electricity. In 2003, Indiana ranked 27th in electricity expenditures per capita (\$863 compared to a nationwide average of \$884), but 6th in total energy expenditures per person (\$3,063 compared to \$2,590). *Id.*

Indiana has long been recognized as a relatively low cost producer of electricity vis-à-vis many neighboring states and nationally. While the relatively low cost of electricity has benefited the state, it has also been cited by some, without additional investigation or analysis, to support a generalized conclusion that DSM cannot work effectively in Indiana. The Sponsoring Utilities cling to this conclusion in their Joint Response, while some of these same utilities individually recognize that much more can and should be done with respect to DSM across the state. The Stratton Report confirms that comparing Indiana's per-capita energy demand, prices, and spending to other Midwestern states, and the nation as a whole, leads to the conclusion that increased DSM programs can result in overall cost savings to energy consumers in the state. Therefore, this issue must be fully examined in Phase II of this proceeding.

4. Additional Benefits of Increased DSM Programs. The Stratton Report further notes that effective DSM Programs act to reduce energy costs and can provide overall economic benefits. Additionally, the increased utilization of DSM can mitigate environmental issues, and lessen the costs associated with new or increased regulatory requirements regarding energy generation. For purposes of this proceeding these additional benefits are important to our consideration of the steps necessary to enhance the role DSM plays in Indiana as they capture and recognize the opportunity to broaden the discussion beyond the framework of existing regulatory requirements.

As discussed in the Stratton Report, Indiana has three government agencies with explicit energy responsibilities. These agencies include the Commission, the OUCC, and the Office of Energy & Defense Development ("OED") which focuses on economic development and the growth of Indiana's defense and energy industries. In 2006, the OED produced the Homegrown Energy Plan discussed in this proceeding. The Homegrown Energy Plan calls for exploiting Indiana's "home grown" energy sources -coal and biofuels- and also encourages improvement in conservation and energy efficiency. With respect to energy efficiency, the Homegrown Energy Plan specifically recognizes Indiana's challenge in meeting its growing energy needs while maintaining and improving its environment and keeping energy prices relatively low. The Homegrown Energy Plan asserts that effective and market-driven conservation measures will be important in achieving those goals. Report at 13.

The Stratton Report concludes that Indiana's Homegrown Energy Plan can serve as a starting point for coordinating and developing statewide programs as it sets the stage for creating a "stronger energy efficiency culture in Indiana's energy intensive manufacturing sector..." and for expanding energy efficiency efforts in all sectors. *Id.* Given the growing need for new resources to meet demand in growth as forecasted by the State Utility Forecasting Group, expanding DSM efforts will provide an excellent opportunity to enhance the development of energy efficiency in Indiana while reducing the need to construct new generation in response to growing demand. As discussed in the Homegrown Energy Plan, conservation plays an important role in Indiana's energy future, and the broad benefits provided by conservation must be considered by the parties in Phase II of this proceeding.

5. Consideration of Administrative Model. While the Stratton Report indicates that the State is not ready to select an administrative model for DSM programs, it concludes that this is due primarily to the existing state of DSM programs in Indiana and the lack of cohesive statewide DSM policy objectives. While it appears based on the overview presented in the Stratton Report, that a Third Party Administrator model, or hybrid thereof, could provide additional statewide benefits in a manner that could remedy the current inconsistent patchwork of DSM Programs in Indiana, we do not reach a conclusion on this issue in this proceeding. The Commission believes that selection of an “administrative” model for DSM programs should be deferred until the establishment of new statewide DSM policy objectives, and only after stakeholder input has been solicited in the second phase of this proceeding.

Notwithstanding our decision to defer the selection of an administrative model, we do believe it to be in the public interest that the Third Party Administrator Model be carefully reviewed and considered. While the Sponsoring Utilities advocated the Utility Led Model as the preferred choice for the implementation of DSM programs, and the OUCC recognized that third-party administration could offer an effective means to prevent conflict and would eliminate any disincentive toward DSM on the part of the utilities, it appears that the status quo may be insufficient to fully address the lack of geographic uniformity and participation in DSM Programs across the state. Regardless of the potential benefits of the Utility Led Model, it has not been utilized in an effective and uniform manner in Indiana and the shortcomings of this approach to DSM are fully revealed in the Stratton Report.

In examining the Third Party Administrator Model, the parties should consider the potential to design programs or objectives to reach common statewide policy objectives. Consideration of the Third Party Administrator Model should include potential implementation issues including a potential timeframe for the development and implementation of such a model and, as necessary, consideration of a hybrid or phased approach that may be undertaken to reach this objective.

6. Additional Issues to be Considered. In addition to the forgoing objectives, Phase II of this proceeding shall also include consideration of any additional means necessary to address issues that impact DSM Programs in the state. These additional issues shall include, but are not limited to, the following:

(i) **Issues Presented in EAct 2005.** In Cause No. 43083 (*Ind. Util. Reg. Comm’n*, August 1, 2007), the Commission declined to adopt smart metering standards based on our examination of the issue undertaken pursuant to Section 1252 of EAct05 (codified at 16 U.S.C. 2621(d)). This determination was based in large part on overall shortcomings in statewide DSM Programs. In that Cause the Commission indicated that:

Therefore, while we find and conclude that it is not appropriate to adopt the standards set forth in Section 1252 of EAct05 (codified at 16 U.S.C. 2621(d)), this conclusion is due in large part to the current lack of a solid foundation of demand response programs in the State from which such an action would constitute a logical and evolutionary next step. While the

Commission does consider it appropriate to ensure that every jurisdictional electric utility in the State of Indiana be prepared to offer advanced technologies to their customers, this cannot be accomplished from a standing start. Accordingly, we find that jurisdictional electric utilities must take steps now to ensure the creation of a solid foundation of demand response programs state-wide. This can be accomplished through the examination of the demand response issues within their respective Integrated Resource Plans; future evaluation and requests for consideration of such programs by the Commission; and, continued discussions and collaboration with customers, and the OUCC regarding the development of effective programs, including pilot programs, in each jurisdictional utility's service territory.

Cause No. 43083 Final Order at 36-37

In reaching this conclusion the Commission recognized that smart metering issues addressed in Cause No. 43083, may overlap with our investigation into Demand Side Management Programs generally in this proceeding. Therefore, the Commission noted that it is possible that further determinations regarding demand response issues and advanced technologies in the form of smart meters, may be undertaken in the context of that broader proceeding. *Id.* at 37, fn.1.

Accordingly, as the foundation we found lacking in Cause No. 43083, is to be evaluated and developed in Phase II of this proceeding, the issues shall include consideration of the role and impact that smart metering can play in the implementation of enhanced DSM Programs across the state of Indiana.

(ii) **Energy Independence and Security Act of 2007.** The Commission further recognizes that additional issues are to be examined under the provisions of the recently enacted Energy Independence and Security Act of 2007. This Act, which amended the Public Utility Regulatory Policies Act of 1978 ("PURPA") (as amended by Section 1252 of the EPAct05), added two new PURPA standards. These standards, reflected under PURPA section 111(d)(16) and (17), address: (16) Integrated Resource Planning and (17) Rate Design Modifications to Promote Energy Efficiency Investments and state as follows:

(16) INTEGRATED RESOURCE PLANNING.—Each electric utility shall—

- (A) integrate energy efficiency resources into utility, State, and regional plans; and
- (B) adopt policies establishing cost-effective energy efficiency as a priority resource.

(17) RATE DESIGN MODIFICATIONS TO PROMOTE ENERGY EFFICIENCY INVESTMENTS.—

- (A) IN GENERAL.—The rates allowed to be charged by any electric utility shall—
 - (i) align utility incentives with the delivery of cost-effective energy efficiency; and

(ii) promote energy efficiency investments.

(B) POLICY OPTIONS.— In complying with subparagraph (A), each State regulatory authority and each nonregulated utility shall consider—

- (i) removing the throughput incentive and other regulatory and management disincentives to energy efficiency;
- (ii) providing utility incentives for the successful management of energy efficiency programs;
- (iii) including the impact on adoption of energy efficiency as 1 of the goals of retail rate design, recognizing that energy efficiency must be balanced with other objectives;
- (iv) adopting rate designs that encourage energy efficiency for each customer class;
- (v) allowing timely recovery of energy efficiency-related costs; and
- (vi) offering home energy audits, offering demand response programs, publicizing the financial and environmental benefits associated with making home energy efficiency improvements, and educating homeowners about all existing Federal and State incentives, including the availability of low-cost loans, that make energy efficiency improvements more affordable.

These provisions will be considered generally in Phase II of this proceeding for purposes of compliance with this statutory provision. For purposes of examining this issue, and all other issues in Phase II, we will amend the caption in this matter to specifically reference all jurisdictional electric utilities including Harrison County and Northeastern REMC; and the cities of Anderson, Auburn, Mishawaka and Richmond, Indiana as necessary participants in this proceeding.

7. **Scope and Conduct of Phase II of this Proceeding.** As part of this proceeding, certain parties raised the issue of possibly narrowing the initial scope of this investigation by limiting further review of DSM issues to electric and steam utilities. These parties noted in their testimony that a separate investigation is pending in Cause No. 43180 relating to energy efficiency and rate design for gas utilities and that Indiana's major gas utilities all have efforts underway to implement increased energy efficiency program offerings. The Commission also notes that Natural Gas DSM Oversight Boards ("Oversight Boards") were formed as a result of Orders, *In re, the Verified Petition of Indiana Gas Company, Inc. and Southern Indiana Gas and Electric Company d/b/a Vectren Energy Delivery of Indiana*, consolidated Cause No. 42943/43046 (*Ind. Util. Reg. Comm'n*, December 1, 2006); *In re, the Verified Petition of Northern Indiana Public Service Company*, Cause No. 43051 (*Ind. Util. Reg. Comm'n*, May 9, 2007); and, *In re, the Petition of the Board of Directors for Utilities of the Department of Public Utilities of the City of Indianapolis, as Successor Trustee of a Public Charitable Trust d/b/a Citizens Gas & Coke Utility*, Cause No. 42767 (*Ind. Util. Reg. Comm'n*, August 29, 2007).

As a result of the activities in various proceedings that have been undertaken since the initiation of this Cause the Commission finds that Phase II of this proceeding can appropriately be limited to electricity and steam providers in the State of Indiana. In reaching this conclusion we find that the creation of Oversight Boards by gas utilities has shown promise as an approach that can provide the foundation for a more uniform approach to DSM between utilities across the State. Therefore, we further find that the formation of an Oversight Board for purposes of DSM in the electric utility sector shall be specifically examined and considered in Phase II of this proceeding.

Additionally it was discussed in this proceeding that historically, utilities have not focused their DSM programs on their largest customers (above 500 kW average peak demand) or required large customers to subsidize programs for other rate classes. The Commission has approved these methodologies in several prior proceedings. Because of the importance of energy to their operations, large customers, particularly, have responded to market signals, and can be expected to continue to do so without the need for utilities to provide additional resources or funding. Under customer self-directed programs, overall demand is reduced without the administrative costs of a utility sponsored DSM program, which the Sponsoring Utilities testified may be 10 – 15% or more of total program costs. Accordingly, it was argued that more DSM can be achieved per dollar expenditure by large customer self-directed programs than is the case with utility funded programs. Self-directed programs can also be implemented quickly without need for pilot programs or prior regulatory approval. Furthermore, many large customers have one of a kind or highly specialized plants or processes that require unique energy efficiency solutions.

While we recognize that issues may vary between various customer classes, we find that it would be inappropriate to limit our review of DSM without further review of the potential impact and benefit that DSM can play across all sectors. This is consistent with recommendations contained in the Stratton Report and suggested by certain utility parties that cost-effective energy-saving potential within the industrial sector needs to be considered before such decisions can be made. Therefore, consideration of the issues in Phase II shall include consideration of DSM efforts as they relate to all customer classes.

The CAC recommended that the Commission determine whether a statewide study of DSM market potential and feasibility should be performed. The CAC supports such a study in general, although the cost, scope, time frame, and goals of such a study would have to be established in detail. Respondents raised various concerns about a comprehensive statewide study being performed and indicated that such a study could be costly and require several months to complete. A number of Indiana utilities and intervenors, including Duke Energy Indiana, I&M, IPL, Vectren Hoosier Energy, and WVPA have market potential studies in some state of development. Therefore, while we encourage the development of Market Potential Studies, by utilities that have not undertaken this effort, we decline to require a *statewide* market potential study as part of Phase II of this proceeding. While reaching this conclusion, we are not abandoning the approach, but find that if further study is necessary it can be considered after stakeholders have had the benefit of the studies already underway.

The use of specific cost benefit tests was discussed by various parties to this proceeding. The Sponsoring Utilities noted that 170 IAC 4-7-7 provides for the utilization of the Participant Test, the Ratepayer Impact Measure, the Utility Cost Test, and the Total Resource Test. The issue of the utilization of various cost benefit tests was reviewed in the Energy Center Report, which concluded that utilities that offer more than minimal programs indicated that they utilize a variety of cost-benefit tests, including the Total Resource Cost Test, the Utility Cost Test, the Ratepayer Impact Measure, and the Participant Test. Conversely, the Report also concluded that utilities with minimal or no DSM offerings utilize the rate-impact test, which according to the Stratton Report is one of the most restrictive tests available. *Id.* at 16. While the Commission finds that it is not necessary to select one model over another as part of this proceeding, it is apparent that all utilities, especially those that have done little or nothing with respect to DSM program offerings, should utilize these various models broadly to evaluate and effectuate DSM programs in a manner consistent with this Order and current regulatory requirements.

The issue of cost-recovery for DSM programs was also an issue raised by the parties in this proceeding. Most parties took the position that cost-recovery should not be a part of this investigation as the existing IRP rules address cost recovery and cost-recovery issues should be conducted in the context of individual utility rate cases. While this is the case, the Commission does not wish to specifically exclude consideration of the issue of cost recovery from Phase II of this proceeding as it may have an overall impact on the parties' consideration of the issues. Therefore, while the Commission finds that the focus Phase II of this proceeding shall be on refining DSM policy, we recognize that cost recovery issues may play a secondary role in such discussions and decline to exclude the matter from our consideration of improvements to DSM Programs in Indiana.

8. Technical Workshops. As has been demonstrated by gas utilities in the State, collaborative efforts can lead to constructive solutions that result in advances in the pursuit of energy efficiency. The parties in this Cause have expressed their willingness to hold technical workshops to gather input on the issues raised in the Stratton Report. The Commission finds that the collaborative approach afforded by Technical Workshops could be useful and that such workshops should be scheduled and utilized as part of Phase II of this proceeding. The Technical Workshops shall be utilized to allow input from the parties regarding specific statewide DSM policy objectives that will be used to measure and evaluate current and future DSM programs, whether such programs are utility led, or ultimately administered by a third-party administrator.

The Technical Workshops will serve as a forum for the parties to engage in an open dialogue and unfettered exchange of information regarding potential programs and other policy matters. In addition to offering input on statewide policy objectives, the parties are also directed, as part of the collaborative, and in testimony as necessary, to investigate the issues discussed herein including, but not limited to, the following issues:

- Steps that can be taken to ensure a uniform offering of DSM Programs on a statewide basis including the feasibility and associated costs and benefits of a statewide Third Party Administrator.

- The means to address the findings in the Stratton Report regarding low spending levels on DSM Programs throughout Indiana and the state's high overall energy use.
- Consideration of additional means to address the inconsistent patchwork of DSM Programs in the state including possible development of a core group of "best practices" programs for utilities to implement in a prescribed way that would provide the framework necessary for the timely transition to a statewide program.
- Consideration of the possible development of a uniform EE/DSM database.
- The broader benefits of DSM identified in the Stratton Report.
- Issues identified in the Energy Policy Act of 2005 and the Energy Independence and Security Act of 2007, including consideration of new technologies such as automated metering and potential cost recovery issues associated with the development of new DSM Programs.
- Additionally, the parties shall strongly consider the value of the formation of an Oversight Board, possibly consisting of jurisdictional and non-jurisdictional electricity providers, to oversee the development of a more uniform statewide strategy with respect to DSM Programs in Indiana.

The Commission anticipates that Phase II of this proceeding will be results driven and culminate in the development of the framework necessary to allow the parties to fully address, in a quantifiable and systematic way, the very specific shortcomings with respect to DSM identified in the Stratton Report. Therefore, it is our expectation that the parties will work collaboratively to develop specific objectives in response to the issues discussed herein. As Phase II will require a specific proposal with a focused and well defined outcome, the Commission recognizes that the services of an outside consultant well versed in DSM issues may be useful to assist the Commission in overseeing and coordinating the process.⁴

Maintaining the status quo will not be satisfactory and will not substitute for the action necessary to improve DSM programs in the Indiana over the short and long term. As recognized in the Homegrown Energy Plan, Indiana must become a self sufficient leader with respect to its energy needs and such an effort is not limited to building new generation. Therefore, it is the Commission's expectation that the parties will set forth a plan in Phase II of this proceeding that will form a record that includes the identification of best practices necessary to greatly improve Indiana's effort and overall standing with respect to DSM programs.

IT IS THEREFORE ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION that:

1. The Commission hereby finds that Phase II of this proceeding shall be initiated to fully address the issues presented and discussed in this Order. Phase II of this proceeding is separate and apart from the issues in Phase I. Absent further action of the Commission, Phase II

⁴ Phase II of this proceeding is separate and apart from the issues presented and developed in Phase I. Absent further action of the Commission, Phase II will not include the assignment of Technical Staff in a testimonial capacity.

shall not include the assignment of Technical Staff in a testimonial capacity.

2. A Prehearing Conference shall be scheduled in this proceeding to allow for the development of a procedural schedule in this Cause that includes Technical Workshops to provide an opportunity for additional input into issues that will be considered in Phase II.

3. The Order constitutes notice to utilities subject to our jurisdiction of the matters to be considered in this proceeding. Consistent with determinations set forth in this Order we find that our review of the issues Phase II of this proceeding shall be limited to electricity providers in the state of Indiana.

4. This Order shall be effective on and after the date of its approval.

GOLC, SERVER AND ZIEGNER CONCUR; HARDY AND LANDIS ABSENT:

APPROVED: APR 23 2008

**I hereby certify that the above is a true
and correct copy of the Order as approved.**



**Brenda A. Howe
Secretary to the Commission**