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M I C H I G A N  
ENERGY INNOVATION  
BUSINESS COUNCIL

**9. What have other jurisdictions' energy efficiency programs relied on: mandates, incentives, or both? What has the experience been with mandates and incentives?**

One level at which this question can be considered is in terms of the use by states of policy mandates or incentives for utilities to provide customer energy efficiency programs. The best source of comprehensive comparative information about state policies and experience with utility energy efficiency programs is the American Council for an Energy Efficiency Economy ([www.aceee.org](http://www.aceee.org)) and the Database of State Incentives for Renewables and Efficiency (DSIREUSA) managed by North Carolina State University ([www.dsireusa.org](http://www.dsireusa.org)). These resources provide a broad range of data that should be examined deeply in any comparison of jurisdictional energy efficiency programs. A particularly accessible but comprehensive perspective can be found in the ACEEE's). ACEEE regularly reviews and reports data on state policies and achievements. Their most recent report is "The 2012 State Energy Efficiency Scorecard" which can be downloaded from <http://www.aceee.org/sites/default/files/publications/researchreports/e12c.pdf>.

The data published by ACEEE shows that a total of 24 states (including Michigan) have established "Energy Efficiency Resource Standards" (EERS), whereby specific energy efficiency savings requirements are established for utility companies (<http://www.aceee.org/files/pdf/policy-brief/state-eers-summary-0912.pdf>). An additional two states have "voluntary" EERS goals, but those states rank fairly low (21<sup>st</sup> and 37<sup>th</sup>) in ACEEE's 2012 state Scorecard.

One lesson that has been learned over the three decades of experience with utility energy efficiency programs is that providing some type of incentive to utilities for energy efficiency accomplishments helps encourage them to perform well in delivering customer energy efficiency programs. This practice has become fairly widespread, such that 19 of the 24 states with mandatory EERS requirements for utilities also provide some type of mechanism for utilities to earn financial incentives for good performance with their energy efficiency programs (<http://www.aceee.org/sites/default/files/publications/researchreports/e12c.pdf>).

In fact, all six of the highest ranked states in the ACEEE 2012 Scorecard have both a mandatory EERS and some type of incentive to the utility for good performance, as do 11 of the top 15 states (<http://www.aceee.org/sites/default/files/publications/researchreports/e12c.pdf>). Overall, utilities tend to be doing very well in meeting their EERS requirements, with a majority actually exceeding their EERS targets (<http://www.aceee.org/files/pdf/policy-brief/state-eers-summary-0912.pdf>).

In contrast, five states (OK, KY, LA, SD, and SC) have a mechanism for utilities to earn financial incentives for energy efficiency achievements, but no EERS savings requirement. That approach of "incentives available but no mandate" does not appear to be very successful, as none of those five states are in the

top 30 in terms of the percent of their annual kWh sales that are saved by energy efficiency programs (<http://www.aceee.org/sites/default/files/publications/researchreports/e12c.pdf>).

Michigan has used a combination of mandates and incentives in its utility policies. An energy efficiency resource standard, known in Michigan as the Energy Optimization Standard, is mandated for all energy utilities. In addition, investor-owned electric utilities have been offered incentive payments for exceeding the mandated standards. This approach has been very successful for Michigan, and Michigan was recognized as one of two “most improved states” in the 2011 ACEEE Scorecard.

Another level at which this question can be considered is with regard to the types of approaches that states are using in their energy efficiency programs for customers. Both mandates and incentives have been used effectively to achieve energy efficiency goals, however usually in different applications. For example, mandates might include adoption of the latest IECC (International Energy Conservation Code) in building standards to ensure that new buildings are being constructed to high efficiency standards. Mandates might also include requirements that a utility meet a certain percentage of their sales through energy efficiency, but the utility may meet those mandates by offering customers incentives to encourage participation. It should also be considered that our prevailing utility business model actually punishes a utility for achieving energy efficiency goals because they are selling less of the commodity from which they earn money (kWhs or BTUs). As a result, many states have adopted one of two mechanisms for providing a utility with cost recovery for their investments 1) decoupling or 2) energy efficiency incentive payments. With decoupling, a utility’s sales are “decoupled” from their revenues – meaning if they sell fewer kWh, rates are adjusted so they are held harmless in their revenues. As a result, there is an incentive for a utility to find the greatest efficiencies in their system and implement those efficiencies because it will mean a greater return for their company. Notably, Michigan lawmakers included language in PA 295 to allow for such a decoupling mechanism. However, in a case brought by the Michigan Attorney General and industrial electricity consumers, the Michigan Court of Appeals struck down the Commission’s decoupling program. One obvious corrective measure would be to reinstate the legislature’s intent in the 2008 legislation to once again allow the Commission to develop and implement a rate decoupling program.

In an incentive payment structure, legislation can specifically state that energy efficiency and lost revenue from sales should be compensated so that efficiency has the highest rate of return for the business. In Colorado, this system has been implemented to great success – the utility receives an incentive once they achieve 80% of the goal and have higher incentives for exceeding the goal.

There is also an important third way to advance energy efficiency, which normally requires support in state policy but differs from directly mandating energy efficiency performance or steps but also doesn’t offer financial incentives. This class of policies are often called “market transformation” and are focused on changes in institutional arrangements or transactions rules to enable and encourage energy efficiency. Market transformation efforts include such practices as labeling (Energy Star, for example), revising mortgage practices so that energy-efficient buildings are eligible for either better interest rates due to their reduced risk of default or enlarged borrowing limits reflecting the combined financial burden of mortgage and energy costs in less efficient buildings. Governor Snyder is to be commended for proposing that energy ratings be incorporated into real estate transactions in Michigan. The top-rated states in the nation on energy efficiency all use a combination of the three types of approaches

described above. <http://www.aceee.org/sites/default/files/publications/researchreports/e12c.pdf>

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A quick overview of state energy efficiency rules, regulations, and policies (mandates) is available at DSIREUSA (<http://www.dsireusa.org/summarytables/rrpee.cfm>) . Most states have adopted energy standards for public buildings as well as building energy codes, though they vary in stringency. Some states have adopted appliance and equipment standards, though most have relied on Federal standards for this purpose. Some states also have public benefits funds that are used by third-party organizations to implement energy efficiency projects or market transformation efforts. Michigan's defunct LIEEF fund made small contributions of this kind, although it was mostly devoted to low-income assistance.

In addition, many states have adopted rebate programs for energy-efficient programs, usually through utility energy efficiency resource programs mandated by the states. Many have also adopted some form of advantageous loan program for energy efficiency programs, like Michigan SAVES. Less commonly, states have adopted tax credits, expedited permit processing for green buildings, or discounted permit fees.