Gauging Success of the Nation's First Efficiency Utility: Efficiency Vermont's First Two Years

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ABSTRACT

In March of 2000, Efficiency Vermont opened its doors as the nation's first statewide energy efficiency utility. Less than two years later, its results have exceeded the state's expectations. By the end of 2001, one of every seven electric customers in Vermont had installed energy saving measures with help from Efficiency Vermont. Annualized savings totaled 60 GWh and lifetime savings totaled 860 GWh, accomplished with an Efficiency Vermont investment of $13.9 million. That's 2.5 cents per kWh over a period when Vermont's electric utilities paid approximately 4 cents per kWh for comparable electric supply.

The efficiency utility is funded by a small "energy efficiency charge" on all ratepayer bills (ramping up to an average of 2.6 mills per kWh in 2002). Services are delivered by a non-utility entity operating under a three-year, performance-based contract with the Public Service Board. This performance contract has a fixed budget and 35 specified measures of performance. How well the contractor performs in meeting these measures determines how much it earns of the performance award set aside as an incentive for superior performance, payable at the end of the contract period. The definitions of performance indicators, their targets and their individual award values were all set through negotiations between the contractor and the Public Service Board.

This paper discusses how the Vermont energy efficiency utility model has been designed, and what has been achieved and learned thus far, both with respect to the delivery model itself and the use of this type of performance contract to successfully administer and deliver public-benefits energy efficiency.

Background

Vermont employs an "energy efficiency utility" (EEU) to deliver all public-benefits energy efficiency through a single, statewide entity, operating under the name "Efficiency Vermont." Efficiency Vermont is delivered by an independent non-utility contractor, operating under a multi-year, performance-based contract with the state's Public Service Board (PSB). Funding is provided by an energy efficiency charge that is phasing in over multiple years. In 2000, the charge averaged 1.5 mills/kWh, rising to an average of 2.1 mills in 2001 and 2.6 mills in 2002. The resultant budgets for Efficiency Vermont were $5.6

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million in 2000, $10.2 million in 2001 and $11.3 in 2002 – a total of $27 million for the initial three-year contract period.

The energy efficiency utility concept was initially considered as part of electric restructuring deliberations in 1996-1997, but the Vermont Legislature did not proceed with retail competition. At the same time, the Vermont Department of Public Service (DPS) was asked to produce a report that included a review of efficiency potential and utility-administered energy efficiency efforts since 1990. The report concluded that a statewide, non-utility alternative should be considered regardless of whether or not the state proceeded with restructuring. The primary benefits that the DPS found with this approach were: (1) increased (statewide) availability of services and uniformity of services, instead of varied program offerings from 22 separate utilities; (2) reduced regulatory contentiousness and cost; (3) reversal of a downward trend in utility program spending since 1993; and (4) greater administrative and delivery effectiveness and efficiency (Vermont Department of Public Service, 1997).

In 1999, the Vermont Legislature confirmed the authority of the PSB to create an energy efficiency utility, set an annual funding cap for it of $17.5 million, and notably did not include a "sunset" of the authorization. The PSB ordered the creation of an energy efficiency utility, adopting a negotiated settlement among the state's regulated utilities, the DPS, and business, consumer and environmental groups that spelled out many of the details of how the efficiency utility would operate. The PSB order relieved Vermont electric distribution utilities of their obligation to deliver system-wide energy efficiency, and described the continuing roles and responsibilities of the electric distribution utilities and the DPS. It also established the alternative administrative structure, set up the energy efficiency charge (EEC) and rules for handling of the funds, defined a set of initial "core" programs to be implemented statewide, and set initial five-year budgets (Vermont Public Service Board, 1999). A "Request for Proposals" for contractors to act as the energy efficiency utility was issued in October 1999, with the contractor selection made by the end of the year, and March 1, 2000 established as the start date for full delivery of services.

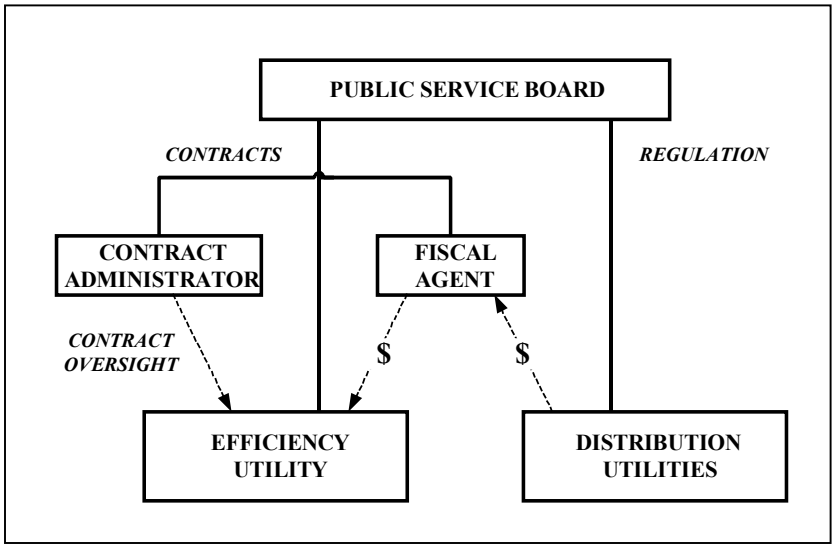
Efficiency Utility Structure

The structure for Vermont's efficiency utility is illustrated in Figure 1. The model uses a "Contract Administrator," who is hired as an independent contractor by the PSB, and handles any day-to-day contract administration responsibilities on behalf of the PSB. It also includes a "fiscal agent," also an independent contractor, who receives EEC collections from the utilities and disburses funds against bills submitted by Efficiency Vermont upon approval by the Contract Administrator. It is notable that because the funds collected never become funds of the State, they are less exposed to redirection, and many procurement limitations associated with use of state funds are avoided.

The responsibility for the design, marketing and implementation of public-benefits energy efficiency in Vermont sits entirely with the PSB's contractor: Efficiency Vermont. This entity acts as an independent contractor to the State, under an extensive and detailed contract with the PSB. In addition to a detailed scope of work, the contract contains policy guidance, legal and accounting rules, and a lengthy set of negotiated measures of performance for the contractor. These performance indicators include quantified goals for MWh energy savings and TRB for the end of the initial three-year contract period, as well as

over thirty additional activity milestones and result indicators (described further below). A financial performance incentive equal to approximately 2.9% of the contract value was agreed upon for 100% attainment of these performance results, which is far less than the typical rate historically allowed under most utility-administered arrangements.

Figure 1. Structure of Vermont's Energy Efficiency Utility



The DPS has responsibility for review of the savings claims made by the Efficiency Vermont contractor each year. The DPS engages in an ongoing process of review and update with Efficiency Vermont of prescriptive savings algorithms, and conducts an annual verification process of all savings claims. The DPS is also responsible for assessing and reporting on market potential, setting efficiency baselines, program evaluation, and making recommendations to the PSB on directions and priorities for the future of Efficiency Vermont

The PSB also established an Advisory Committee composed of representatives from distribution utilities, consumers, the DPS, and others deemed necessary by the Board to provide substantive public and utility input on program design, annual re-allocation of funds within programs, and other policy issues.

Decision-Making Processes

Due the performance-based nature of the contract, the PSB has given wide latitude to the Efficiency Vermont contractor regarding program design and implementation. The contractor is required to seek approval of the PSB for "major" program changes and for major shifting of funds among programs. The contractor is required to submit an Annual Plan each fall for the coming year, which is reviewed in a workshop setting before the PSB, with opportunity for any interested parties to offer comments to the PSB regarding its approval of the plan.

Objectives

There are multiple objectives for Efficiency Vermont set forth in legislation, regulatory order and the PSB contract. Because these objectives are potentially conflicting, Efficiency Vermont pursues a reasonable balance among them, guided by dialogue with interested parties, pubic input and feedback from customers. The key objectives that determine Efficiency Vermont's service offerings and strategies are:

- With limited resources, lost opportunities (e.g., new construction, equipment replacement) are prioritized over discretionary retrofits, with a reasonable balance being sought. At the end of the first two years of implementation, approximately 70% of the resources were spent on lost-opportunity markets and 30% on retrofits, with 82% of MWh savings in lost-opportunity markets. Of the retrofit spending and savings, the majority (approximately 60%) was in services targeted to low-income households, with the balance in targeted services to large commercial/industrial, school, and general residential retrofit opportunities.
- Efficiency Vermont seeks to balance the attainment of immediate electrical energy and demand reductions with maximizing long-term electrical and total resource benefits. In its first two years, the average measure life of savings has been 15 years, which has been a satisfactory balance on lifetime savings. To maximize acquisition of total resource benefits, all Efficiency Vermont services are designed to secure not just electrical savings and demand, but to leverage electric ratepayer investment in securing savings of all fuels, as well as water.
- Efficiency Vermont is expected to allocate resources to maximize benefits to all ratepayers, and to balance this with efforts to return benefits equitably among ratepayers across the state. Specifically, there are objectives to return benefits equitably by geographic location (e.g., by county, proportional to population), by distribution utility (proportional to the total EEC paid by customers in each of the state's 22 electric utilities, and by percentage of total rate class revenue (approximately 50% residential and 50% commercial and industrial). At the end of the initial two years, these distributional equity objectives had been met to a very high degree.

Efficiency Vermont's Performance Contract

Efficiency Vermont's contract contains 35 measures of performance with specific targets in 2000, 2001, and 2002. How well Efficiency Vermont performs against these targets determines how much it earns of the performance award set aside as an incentive for superior performance, payable at the end of the contract period. The amount and basic design of the performance incentive were part of the contractor's proposal. The definitions of performance indicators, their targets and their individual award values were all set through negotiations involving the PSB, the Contract Administrator, the DPS, and the Efficiency Vermont team.

Efficiency Vermont has three types of performance indicators: program results, activity milestones, and market effects. Program results include separate indicators for electric energy savings and TRB by year-end 2002. In the Efficiency Utility contract, TRB is defined to include estimated economic value of electricity, gas, propane, oil, and water

savings, but not environmental benefits. Program results also include the electricity savings and resource benefits associated with projects in the "pipeline" (under contract, but not complete) at the end of the contract in new construction, commercial equipment replacement, and the low-income multifamily programs.

Activity milestones involve the completion of tasks considered critical to superior Efficiency Vermont performance, either for individual programs or for the enterprise as a whole. The intent of these milestones was to create challenging deadlines early in the contract period. Consequently, most of the activity milestones applied to the first year of the contract; in fact, they were the only form of performance indicator that Efficiency Vermont had in 2000. Perhaps the most challenging activity milestone for Efficiency Vermont was the design, development, and demonstration of full functionality of a complete, custom data tracking system in six months.

The two "market effects" indicators involve market share of various Energy Star appliances in 2002. The contract calls for the PSB to decide annually Efficiency Vermont's level of attainment for each year's performance targets, so Efficiency Vermont can "bank" the awards soon after they are earned.

Figure 2 depicts the relative weighting placed on each type of indicator. Table 1 presents the breakdown numerically and indicates how much of the total award is associated with each type of indicator in each year. Most of the incentive award (55%) is for Efficiency Vermont's performance regarding the electric energy savings and the economic value of all resource savings. The value of activity milestones and other program results are worth roughly the same (20% and 22% respectively). Market effects are valued at 3%.

Figure 2. Relative Weight of Performance Indicators

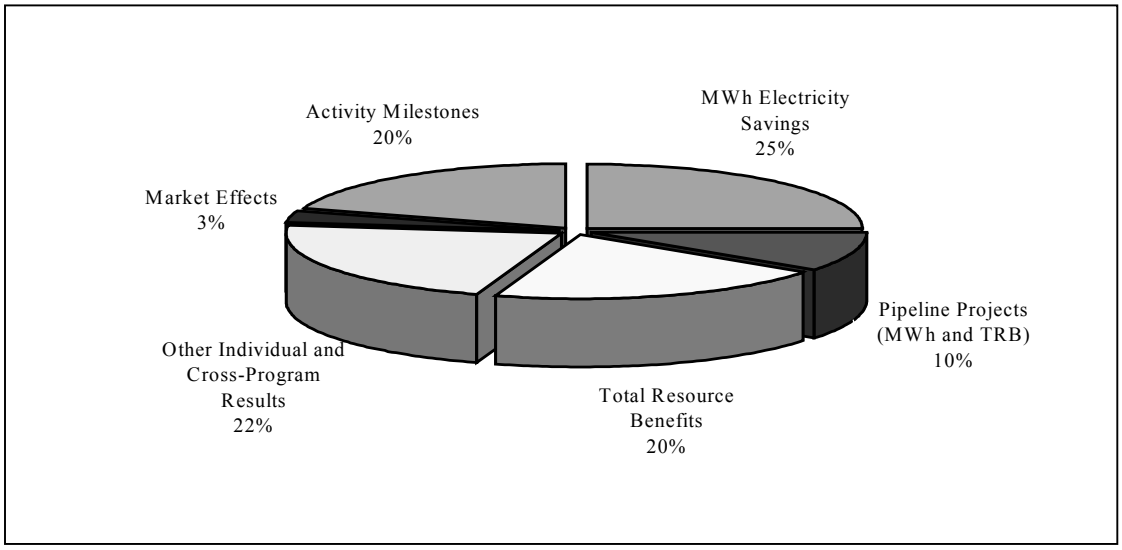


Table 1. Categories, Weights, and Performance Award Amounts

Performance Indicator	Potential Amount of Award	Overall Weight	Amount of Total Award Eligible to be Earned in Each			Number of Indicators
			2000	2001	2002	
Program Results						
Annual Electricity Savings	$198,750	25%			$198,750	1
Pipeline Projects	$79,500	10%			$79,500	2
Total Resource Benefits	$159,000	20%			$159,000	1
Other Individual & Cross-Program Results	$174,900	22%		$15,000	$159,900	
Number of Indicators:			0	1	9	10
Market Effects	$23,850	3%			$23,850	
Number of Indicators:			0	0	2	2
Activity Milestones	$159,000	20%	$100,000	$59,000		
Number of Indicators:			14	6	0	20
Maximum Possible Performance Award	$795,000	100%	$100,000	$74,000	$621,000	36

Money is not the prime motivator for the Efficiency Vermont contractor; it does, however, provide a signal as to the relative value of different types of success to Vermont's regulators. Tying half the overall value of Efficiency Vermont's performance to the electricity savings achieved by energy-efficiency properly reflects the need to deliver value to the people paying for it. The activity milestone incentive offered Efficiency Vermont is significant reward for meeting challenging deadlines for tasks considered vital to the early and long-term success of Efficiency Vermont. The three percent for market effects reflects more the limited ability to measurably change markets within the relatively short period of the initial contract than it does the importance that the PSB attaches to long-term market transformation.

For illustrative purposes, Table 2 summarizes the nine individual program results targets for the year 2002, along with the two market effects indicators. Most program results awards and both market effects awards are scalable up or down to maximum and minimum values, respectively. With a few exceptions, most continuous variables offer 50% of the target award at 75% of achievement, and no award below 75%. For superior performance up to 110% of the target performance level, Efficiency Vermont can earn up to 120% of the target award. Since the total performance award is capped, Efficiency Vermont can only take advantage of scalability above target outcomes if it fails to reach targets for at least one other performance indicator.

Efficiency Vermont had to meet a minimum number of the activity milestones for 2000 and for 2001 to qualify for an award for superior performance. In 2000, Efficiency Vermont had to meet a minimum of 11 out of the 14; if it had met 10 or fewer, it would lose the incentives associated with all the activity milestones for that year. In 2001, Efficiency Vermont had to meet four of the six to qualify for any activity milestone awards.

Table 2. Market Effects and Program Results Indicators for 2002

Program	Indicator	Performance Target
Efficient Products	Market share of Energy Star washers in Vermont in 2001	27%
Efficient Products	Percentage-point increase in ratio of total number of Energy Star dishwashers and refrigerators on display by Vermont appliance retailers over the number of all such appliances on display	6%
Residential New Construction	Number of single-family Energy Star homes outside Chittenden County certified in 2002	66, of which a maximum of 13 can be single-family attached
Low-Income Single Family	Average annual kWh savings per participant in 2002	1000
Commercial Energy Opportunities	Number of participants in "Comprehensive Track"	6, with at least 2 using "enhanced options" in large buildings
Commercial Energy Opportunities	Number of new architect or engineer participants in Building Solutions 2002 conference	15, of which at least 4 must be engineers
Commercial Energy Opportunities	Number of sample documents issued by dairy farm network members promoting Efficiency Vermont incentives and services after Nov. 1, 2001, to indicate results of targeted Efficiency Vermont business development efforts	3
Low-Income Multifamily	Number of new, private, non-subsidized projects in progress (audit completed)	5
Low-Income Multifamily	Number of Public Housing Authorities that include energy efficiency measures as part of their annual capital improvement plan submitted to HUD	2
Emerging Markets Initiatives	Total Resource Benefits	$4,110,000
CEO, Low-Income Multifamily and Residential New Construction	Total Resource Benefits	$1,950,000

Efficiency Vermont's Experience to Date

Implementation Experience, Results, Costs and Savings

With only a two-month period from notice of contractor selection, the Efficiency Vermont contractor took full responsibility for administration and operation on March 1, 2000. Starting that day, all requests for efficiency services were re-directed from utilities to Efficiency Vermont and all on-going projects became the responsibility of Efficiency Vermont. All of the activity milestones for rapid ramp-up in the first year were met, though this required enormous effort on the part of the contractor.

Virtually all parties appear to be very pleased with this new approach to delivering statewide public-benefits energy efficiency. The utilities are supportive and refer customers routinely to Efficiency Vermont. They also routinely provide full electronic customer identification and consumption records so that Efficiency Vermont can maintain a single,

statewide database on customer energy use and assign savings to individual customers. In the workshops before the PSB on both of the first two Annual Plans submitted by Efficiency Vermont, there have been no serious concerns raised by any party, the DPS or the PSB. Each Annual Plan has been approved as submitted, as has every request for budget modification. Reports delivered to the state Legislature on the performance of Efficiency Vermont have also been very well received.

Efficiency Vermont has put unprecedented effort into developing supportive partnerships with statewide dealer and vendor networks, as well as with design and engineering professionals, economic development agencies and business and trade associations. This has been very fruitful and resulted in positive support for this model.

Most importantly, the public appears to find the efficiency utility model sensible, simple and worthwhile. There is a single statewide source for all efficiency services, with a single toll-free number and website. The services available are the same statewide for all customers and anecdotal feedback from the public to Efficiency Vermont staff suggests they find the notion that separating the roles of selling electricity from saving it makes sense in terms of the motivation of the entity they are dealing with.

The total number of Efficiency Vermont customers who made energy-saving improvements in the first 22 months of operation is 43,777 (not counting repeat participants) – or 1 in 7 electric utility customers in the state. Illustrative breakdowns of 2001 activity by market and measure are presented in Table 3.

Table 3. Breakdowns of Participation and Measures in 2001

Type of Participant		Number of Participants
Residential	Buyers of Retail Lighting and Appliance Products	27,596
	New Construction	622
	Low-Income Households	2,191
	Homes with High Electric Use	88
Commercial & Industrial	Dairy Farms	81
	New Construction	77
	Equipment Replacement	286
	Large Electric User Retrofit	19
	School Retrofit	6

Type of Efficiency Measure		Number of Participants
Residential	Heating, Air Conditioning and Ventilation	2,877
	Lighting	28,190
	Major Appliances	4,043
	Water Heating	1,417
Commercial & Industrial	Lighting	311
	Motors	97
	Heating and Cooling	210
	Industrial Process	16
	Refrigeration	32

Efficiency Vermont makes the benefits of energy efficiency available to Vermonters statewide, reaching out to serve people with the greatest barriers to participation and to equitably distribute benefits to all counties of the state, to every utility service territory and to all types of business and residential electric consumers.

As illustrated in Table 4, the percentage of people that Efficiency Vermont serves in each county correlates well with the percentage of the state's population residing in each county. The economic benefits distribution by county shows a similar pattern of equity. The $42.8 million value of efficiency from Efficiency Vermont activity through the end of 2001 was also reasonably proportional throughout the state.

Table 4. Distribution of Participation and Benefits by County 3/1/2000 – 12/31/2001

County	% of Statewide Population	% of Total Participants	% of Total Resource Benefits	Present Value Total Resource Benefits
Addison	5.9%	6.9%	4.3%	$1,852,351
Bennington	6.1%	5.4%	17.1%	$7,320,980
Caledonia	4.9%	4.9%	3.3%	$1,418,875
Chittenden	24.1%	24.8%	22.8%	$9,775,503
Essex	1.1%	0.6%	0.3%	$109,779
Franklin	7.5%	8.1%	5.4%	$2,292,162
Grand Isle	1.1%	1.3%	0.7%	$283,976
Lamoille	3.8%	5.2%	3.7%	$1,564,768
Orange	4.6%	3.7%	1.9%	$824,687
Orleans	4.3%	3.5%	5.1%	$2,201,806
Rutland	10.4%	11.8%	10.7%	$4,585,496
Washington	9.5%	11.1%	6.8%	$2,930,181
Windham	7.3%	5.2%	10.2%	$4,370,819
Windsor	9.4%	7.3%	7.6%	$3,271,943
Total	100.0%	100.0%	100.0%	$42,818,217

This balanced benefit distribution is the result of a strategic effort by Efficiency Vermont in 2001. At the end of year 2000, Efficiency Vermont conducted an analysis of under-participating sectors of the state and designed its 2001 efforts to improve distributional equity. Efficiency Vermont was able to achieve these positive results through targeted marketing, personal outreach to utility and business leaders, and increased visibility at public events in targeted counties and utility territories.

Table 5 presents the results of GWh savings that Efficiency Vermont has achieved in the first two years of operation and their distribution by sector. The 50/50 split of benefits between residential and commercial/industrial electric utility customers corresponds well with the 50/50 allocation between the residential and commercial/industrial sectors in the five-year budgets contained in the regulatory order for the initial period of operation of the EEU.

With respect to cost-effectiveness, one perspective is that in 2001, Efficiency Vermont spent $8.5 million to provide Vermonters with services and financial assistance that generated 37 GWh of annual electricity savings. With lifetime savings of 536 GWh (average measure life of 14.5 years), Efficiency Vermont investments saved energy in 2001 at a cost of 2.5 cents per kWh at a time when electric utilities were paying an average of 4.0 cents per kWh for comparable electric supply.

Table 5. Distribution of Benefits by Sector

	Commercial & Industrial	Residential
2000 GWh Savings	12	11
2001 GWh Savings	18	19
GWh Savings to Date	30 (50%)	30 (50%)
Total Resource Benefits (Million)	$20.5 (50%)	$20.5 (50%)

A more complete indicator of the cost-effectiveness of Efficiency Vermont's electricity-saving activities through 2001 is the total cost compared to the dollar value of all the savings. As summarized in Table 5, the total cost consists of Efficiency Vermont costs ($13.9 million) plus participant and third-part investment toward efficiency measures ($9.1 million) - a total investment in energy efficiency of $23 million. If this investment had not been made, with its resulting 60 GWh annual savings, Vermont utilities would have had to supply that much more electricity over each of the coming years. Using currently accepted estimates of the statewide avoided costs of electricity supply in Vermont, the cost of providing that electricity is estimated to be $34.6 million (present value). Including the fossil fuel and water resource impacts, the TRB are $40.9 million, a net benefit of $17.9 million, which is 1.8 times the cost of the total investment in energy efficiency.

Table 6. Summary of Costs and Benefits

Efficiency Vermont Total Expenditures	$13.9 million
Participant and Third-Party Investments	$9.1 million
Total Investment in Energy Efficiency	$23.0 million
Total Resource Benefits (NPV)	$40.9 million
Net Benefits	$17.9 million

More detail on results, costs and savings are contained in the latest Annual Report submitted by the Efficiency Vermont to the PSB and publicly available (Efficiency Vermont 2001).

Performance Indicator Results

Electricity savings. At the end of 2001, the preliminary estimate for Efficiency Vermont cumulative annualized savings was 60 GWh, 72% of the goal set for exemplary performance in the initial contract period. This had been achieved with expenditure of only 55% of the available funds for the contract period.

Total resource benefits. At the end of 2001, Efficiency Vermont had achieved $40.9 million in cumulative TRB, well above the three-year total goal of $36.2 million. It has not yet been determined why Efficiency Vermont was able to surpass this goal so significantly, but there are indications it may have to do with higher-than-expected savings and TRB in the Efficient Products and CEO programs.

Activity milestones. Efficiency Vermont has met all but one of the 20 activity milestones.

Individual program results. Efficiency Vermont met the single program result indicator for 2001. The goal was to increase the number of participating retailers in the efficient products program to a minimum of 115, which was successfully achieved (virtually every major household appliance dealer in the state is now a participant, working with Efficiency Vermont to promote and sell ENERGY STAR appliances.

Efficiency Vermont has made solid progress toward all nine of the 2002 individual program result targets. For example, Efficiency Vermont has averaged over 1500 kWh in savings per participant in the single-family low-income program; the performance target is 1000, with the ability to earn 120% of the award amount for achieving 1100 kWh. For the non-residential market-driven program, Efficiency Vermont has already enrolled the minimum number of large comprehensive new construction projects in the first quarter of 2002.

Lessons Learned and Recommendations

When the Efficiency Utility model was developed and the RFP for contractors issued, there was a set of "core" program designs that were specified as a starting place for what should be offered. Efficiency Vermont began with those program definitions, but has increasingly moved away from identifying, marketing or offering separate "programs." As the sole statewide source for whatever assistance consumers need with energy efficiency, it is simpler for both customers and Efficiency Vermont to simply direct customer needs in various markets to appropriate Efficiency Vermont services. It had also been assumed, at the time of the RFP, that the design and relative funding of different programs would be an issue that might be contentious and require extensive processes of deliberation and approval that resembled the process under regulated utility delivery of programs. This has turned out not to be the case, particularly in the context of a performance-based contract. With the contractor accountable for bottom-line results, the contractor has been given wide latitude to modify and adjust service offerings as its sees best to respond to changing markets, new opportunities, customer feedback and the experience of implementation.

Another lesson is that it took time for everyone to become fully comfortable in his or her new roles. Efficiency Vermont needed to learn fast how to position itself in the market and define its role with customers and trade allies. Efficiency Vermont and the DPS had to establish an unprecedented relationship and process for establishing savings, data reporting requirements savings verification. The DPS had to get used to abandoning its traditional adversarial role while taking responsibility for market assessment. The PSB got to spend far less time on DSM-related proceedings, but had to make time in its crowded regulatory schedule to act on details put before it by the Contract Administrator.

Planning, capability development and the ability to implement longer-term efficiency strategies require a relatively stable period of performance and funding. Experience suggests that a four to five year period minimum would be advisable from this perspective.

The performance contract model has been a very strong and positive driver with many attributes. The basic structure of the performance contract and performance incentive mechanism are well suited for application elsewhere. Setting target values and incentive amounts well in advance has been particularly beneficial. Having cumulative targets for electricity savings and economic value made much more sense than "hard-wiring" individual years' levels. And while the monetary value for individual performance indicators was small, they did get Efficiency Vermont staff's attention and appealed to everyone's desire to excel. Requiring Efficiency Vermont to meet most of the activity milestones, each of which Efficiency Vermont staff considered a stretch to reach, magnified the incentive to meet every one. With hindsight, the key parties all see room for improvement in specifying and balancing performance indicators. Despite concerted efforts to define the indicators precisely, there is still a need to consult occasionally with the Contract Administrator to clarify definitions or means of verification. In the future, the Efficiency Vermont contractor will seek to reduce the number of performance indicators, with more attention to those that are cost effective to pursue.

Efficiency Vermont is currently contracted to a multi-organizational team, with the lead contractor being a non-profit, mission-oriented energy services organization. Using a team approach enabled us to draw on the particular strengths of each organization, not just in winning the bid, but also in meeting the objectives of the contract and its performance targets. It is generally recognized that a good part of Efficiency Vermont's success is attributable to the consistency of the prime contractor's organizational mission with that of the Efficiency Vermont enterprise. The ready availability of, or prospects for developing, such an organization may well be an important consideration in considering the replicability of the Vermont model elsewhere.

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