Date Filed: September 15, 2026

Witness: Julia Frayer
Request from: Office of Consumer Counsel

Question:

Performance Based Ratemaking Panel Exhibit CLP-PBR-1
Please state whether LEI evaluated whether OM&A PFP trends differed between utilities operating under the PBR and utilities operating under traditional cost-of-service regulation, and whether utilities' OM&A PFP trends differed between periods before PBR application and under PBR application. If so, please provide the results of the analysis. If not, please explain why such an analysis was not performed and provide, if available, the OM&A PFP growth rates separately for the two different groups.

Response:

This would be an interesting analysis, but there are several empirical challenges to conducting it reliably. First, incentives to pursue efficiency improvements can arise from a range of formal and informal features of a regulatory regime, including stay-out provisions, multi-year rate plans, voluntary rate freezes, and regulatory lag between rate cases. As noted in our response to OCC-540, a number of utilities have operated, or currently operate, under some form of PBR (formula based or MYRP), while others have experienced extended periods of rate freezes or regulatory lag, such as MidAmerican Energy in Iowa (who went for 10 years without a rate case). LEI has not undertaken an exhaustive review of the regulatory regimes applicable to every utility over the study period. The sub-sample of companies identified in that Response is unlikely to cover the entire industry, and an analysis limited to it would therefore not constitute an industry-wide study.

Second, and more fundamentally, the strength of the incentive to improve efficiency depends on multiple, interacting features of a regulatory regime rather than on any single characteristic. Distribution ratemaking in the U.S. is the domain of state regulators, so there are diverse regulatory mechanisms in place. For example, one utility may be subject to a formal stay out provision, others may be under voluntary rate freeze, while another may have an earnings sharing mechanism, or a forecast-based multi-year plan with advance ratemaking treatment for certain investments, variance accounts or other mechanisms. Cost and productivity outcomes may also be affected by factors unrelated to PBR, such as corporate restructuring or merger-related synergies. As a result, regulatory regimes that appear similar at a high level may create materially different efficiency incentives. Given the diversity of regulatory frameworks across U.S., a simple classification based

on the presence (or lack thereof) of a specific regulatory feature may not provide a sufficiently robust basis for an industry-wide empirical comparison.

A further challenge is that adoption of PBR-like regulatory mechanisms may have occurred at different times and for different durations across utilities. The second part of the question contemplates a comparison of productivity before and after "PBR" adoption, but given there is no common implementation date for various PBR mechanisms, it would be difficult to get a cohesive industry-wide "before-and-after" comparison.

For the above reasons, LEI did not perform a PBR-versus-COS or pre-/post-PBR OM&A PFP analysis as part of this study. The purpose of LEI's TFP study was to estimate the long-term productivity trend for the industry, rather than at a firm-specific level. Economic theory then recommends using the industry productivity trends to establish the X Factor under an I-X framework.

The broader proposition that incentive regulation can strengthen incentives for cost efficiency relative to traditional cost-of-service regulation is supported by the regulatory economics literature and evaluations of incentive regulation. For example, Jamasb and Pollitt's study of British electricity distribution under incentive regulation found that the regime was associated with reductions in costs, prices, and energy losses while maintaining service quality.[1] LEI's review of the UK experience similarly observed that the stronger incentives under PBR were associated with substantial productivity improvements and that utilities responded to tighter price controls by reducing operating costs, labor, and materials.[2]

The Alberta Utilities Commission reached similar conclusions in its evaluation of Alberta's PBR experience. The Commission found that PBR had incented utilities to find efficiencies and that utilities engaged in productivity improvements to reduce costs, concluding that "in this respect, PBR was successful." The Commission also found that customers experienced lower rates under PBR than would have been expected under COS regulation. [3]

These studies and regulatory findings provide evidence regarding the efficiency incentives associated with PBR, but they are not a substitute for the utility-by-utility empirical analysis described in this interrogatory.

[1] Paul L. Joskow, "The Expansion of Incentive (Performance-Based) Regulation of Electricity Distribution and Transmission in the United States," Review of Industrial Organization, Vol. 65 (2024), pp. 455–503. https://link.springer.com/article/10.1007/s11151-024-09973-x and Tooraj Jamasb and Michael Pollitt, "Incentive Regulation of Electricity Distribution Networks: Lessons of Experience from Britain," Energy Policy, Vol. 35, No. 12 (2007), pp. 6163–6187. https://www.jamasb.org/publication/re-p-ec-eee-enepol-v-35-y-2007-i-12-p-6163-6187

[2] A. J. Goulding, Julia Frayer, and Jeffery Waller, "X Marks the Spot: How U.K. Utilities Have Fared Under Performance-Based Ratemaking," Public Utilities Fortnightly, July 15, 2001, https://www.fortnightly.com/fortnightly/2001/07-0/x-marks-spot-how-uk-utilities-have-fared-under-performance-based-ratemaking.

[3] Alberta Utilities Commission. "Evaluation of Performance-Based Regulation in Alberta." June 30, 2021.