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MEMO

To: Brian Cotterill, Matthew Walker, VT-PSD

From: Toben Galvin, David Purcell, Christy Zook, Navigant

CC: Randy Gunn, Stu Slote, Navigant

Date: April 28, 2014

Re: Comparison of Compensation Framework for Selected Efficiency Vermont Peer Group Organizations

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This memo summarizes Navigant's findings regarding the compensation structures of eight other demand side management (DSM) program administrators considered to be most similar to the Vermont Energy Investment Corporation (VEIC) / Efficiency Vermont (EVT) structure. The word "compensation" is used in this memo to represent additional payment above and beyond 100% of direct cost recovery associated with DSM program delivery. Compensation can be in the form of a guaranteed set amount (e.g. an operations fee on every dollar spent), or an at risk compensation amount subject to achieving specified performance goals.

Compensation is reviewed from the perspective of the "DSM Administrator", which we interpret as the entity with the overall responsibility for managing and directing the DSM programs, as well as for the DSM "third party implementation contactor" who is under contract to the DSM administrator.

Navigant believes the following organizations are most similar to VEIC/EVT for purposes of assessing compensation structure.

Most Similar

1) Non-profit administrators with a long-term delivery contract (e.g. Energy Trust of Oregon, Efficiency Nova Scotia).
2) Quasi-government administrators (e.g. Efficiency Maine Trust, New York State Energy Research and Development Authority (NYSERDA), Hawaii Energy)
3) Burlington Electric Department (in particular given it is the other electric EEU in Vermont).

Less Similar

1) Non-profit third party implementation contractors with short-term delivery contracts (e.g. Conservation Services Group)
2) For-profit third party implementation contractors with short-term delivery contracts (e.g. Leidos and Honeywell)
3) Municipal/Co-ops
4) Regulated investor owned utilities (IOUs)

Navigant believes considerations of the regulatory framework, lost revenue provisions, and organizational structure are important factors to include in a representative benchmarking when determining the most comparable DSM program administrators to VEIC/EVT. With that said, the unique overall structure of EVT and its non-profit administrator, VEIC, present challenges to finding a truly equivalent and comparable situation.

Reasons Why VEIC/EVT Is Not Comparable to Investor Owned Utilities (IOUs) for Assessing Compensation Structure

Navigant considers the overall organization type, and regulatory framework under which the DSM program administrator operates, as key factors in assessing which organization types are the most appropriate benchmark for compensation comparison purposes. For example, is the DSM program administrator independent from a utility, and thus more isolated from the impact of lost-revenue due to reduced electric sales? Next, Navigant considered the profit structure of the DSM administrator, and believes organizations that also are non-profit in structure are most similar to VEIC/EVT. Eight other DSM program administrators are included in this peer group. Navigant believes that IOU's are not an appropriate organization type for comparison to EVT for purposes of assessing performance compensation given the significant differences in the regulatory framework under which IOU's operate (e.g. shareholder financial interests and sensitivity to lost revenue). Even after taking into account whether or not the utility has a lost-revenue recovery mechanism, the significance of the operational differences between EVT, a non-profit organization, and the IOU class of program administrators makes the comparison less valuable. Even under a decoupled situation, IOUs can still be concerned with lost revenue.[1] Additionally, for IOU's energy efficiency is just a small portion of their annual operating budget, and historically, energy efficiency directly competes against other business objectives for load growth. As such, the use of performance compensation, above and beyond direct cost recovery, has been one tool, of several, to help motivate IOU management to take energy efficiency seriously and strive to achieve targets.

Navigant believes that treating 'DSM as a Business', including the use of performance compensation and lost-revenue recovery mechanisms where shareholders are at financial risk, is a valid and important framework for ensuring DSM goals are achieved. In this light, striving for equal financial treatment (and returns) for DSM activities should be relatively consistent with the financial returns earned from other business lines within the utility. The use of performance compensation, especially for regulated IOUs that do not have other forms of lost-revenue recovery mechanisms, is very important to assist with aligning management's commitment to meeting energy efficiency targets. With that said, examples exist across the industry of regulated IOUs achieving savings targets in the absence of a lost-revenue recovery mechanism or performance compensation..

Navigant believes there is no single 'preferred' performance compensation amount; what matters is designing a structure that achieves results and is determined to be fair and reasonable given various organizational qualities and the legislative and regulatory context under which the program operates.

Table 1 presents a summary of the organization type, lost revenue mechanism, and compensation status. The table distinguishes the program administrator (e.g. Hawaii Public Utilities Commission),

[1]Kihm, Steve, "When Revenue Decoupling Will Work…And When It Won't", The Electricity Journal, October, 2009.

from hired third party implementation contractors (e.g. Leidos (for profit firm) who might be working under contract for the program administrator.

Table 1: EVT Peer Group Compensation Summary Matrix

DSM Program Administrators Most Similar to VEIC/EVT	Organization Type (Non-Profit, Gov't/Quasi, Muni, IOU)	Annual DSM Budget	Lost-Revenue Mechanism (N/A, Decoupled, LRAM)	Compensation for Program Administrator (Yes/No)	Compensation for 3rd Party IC (Yes/No)	Guaranteed 3rd Party Compensation (Annual Amount and % of Budget)	Performance Based Compensation (Annual Amount and % of Budget)	Total Incentive Amount and % of Annual Budget
VEIC/EVT	Non-Profit	$41.4 M	N/A	Yes	Yes (if you view EVT as a 3rd party to VEIC)	1.7% / ~$700K (operations fee)	2.4% / ~$993K (annual)	4.1% / ~$1.7M[2] (annual) ($4.6 million over 3 years)
Energy Trust of Oregon	Non-Profit	$155.4 M	N/A	No	Yes	0%	$1.3% /$2 M	$1.3% / $2 M
Efficiency Nova Scotia	Non-Profit	$35.7 M	N/A	No	No	0%	0%	0%
Burlington Electric Dept.	Municipal	$1.8 M	None	No	No	0%	0%	0%
Hawaii Energy – (Project of HI PUC.)	State Gov't – PUC	$33.6 M	N/A	No	Yes (Leidos- For-Profit)	0%	0.40% / $133K [3]	0.40% / $133K
Efficiency Maine	Quasi-State Gov't	$26.6 M	N/A	No	No	0%	0%	0%
NYSERDA	Quasi-State Gov't	$123.3 M	N/A	No	No for core EE implementation; Yes for community awareness groups	0% for core EE	0% for core EE	0% for core EE

[2] Estimate from VT PSD, 4/2/14. This represents the total from EVT's performance compensation amount (2.4%) and operations fee (1.7%) of total DSM budget. Combined EVT's compensation is considered to be 4.1%.

[3] State of Hawaii Supplemental Contract No. 5. May 31, 2013. Detailing terms of the program administrator of public benefit funds.

DSM Program Administrators Most Similar to VEIC/EVT	Organization Type (Non-Profit, Gov't/Quasi, Muni, IOU)	Annual DSM Budget	Lost-Revenue Mechanism (N/A, Decoupled, LRAM)	Compensation for Program Administrator (Yes/No)	Compensation for 3rd Party IC (Yes/No)	Guaranteed 3rd Party Compensation (Annual Amount and % of Budget)	Performance Based Compensation (Annual Amount and % of Budget)	Total Incentive Amount and % of Annual Budget
Efficiency Smart-Ohio – (AMP-Ohio)	Municipal	$24.6 M	N/A	No	Yes (VEIC- Non-Profit)	2.1% / ~$508K[4]	4.2%/ ~1M[5]	6.3% / $~1.5M[6]
DC Sustainable Energy Utility	State Gov't	$20 M	N/A	No	Yes (VEIC-Non-Profit)	3.5% /~$700K[7]	4.0% / ~$800K [8]	7.5% / ~$1.5 M[9]

[4] EVT Materials submitted to PSD for Task 1.

[5] EVT Materials submitted to PSD for Task 1.

[6] Id.

[7] Id.

[8] Id.

[9] Id.

As noted in Table 1, if one distinguishes the "DSM Program Administrator" from the "Third Party DSM Implementation Contractor", then only one DSM program administrator, VEIC/EVT, directly receives performance compensation. The use of performance compensation for third party implementation contractors was confirmed for DC SEU, Energy Smart-Ohio, Hawaii Energy, Energy Trust of Oregon, and EVT (assuming one could consider EVT as the third party implementer of VEIC's EEU contract). Navigant confirmed that Efficiency Maine, Efficiency Nova Scotia, and NYSERDA do not offer performance compensation to third party IC's for core energy efficiency delivery.

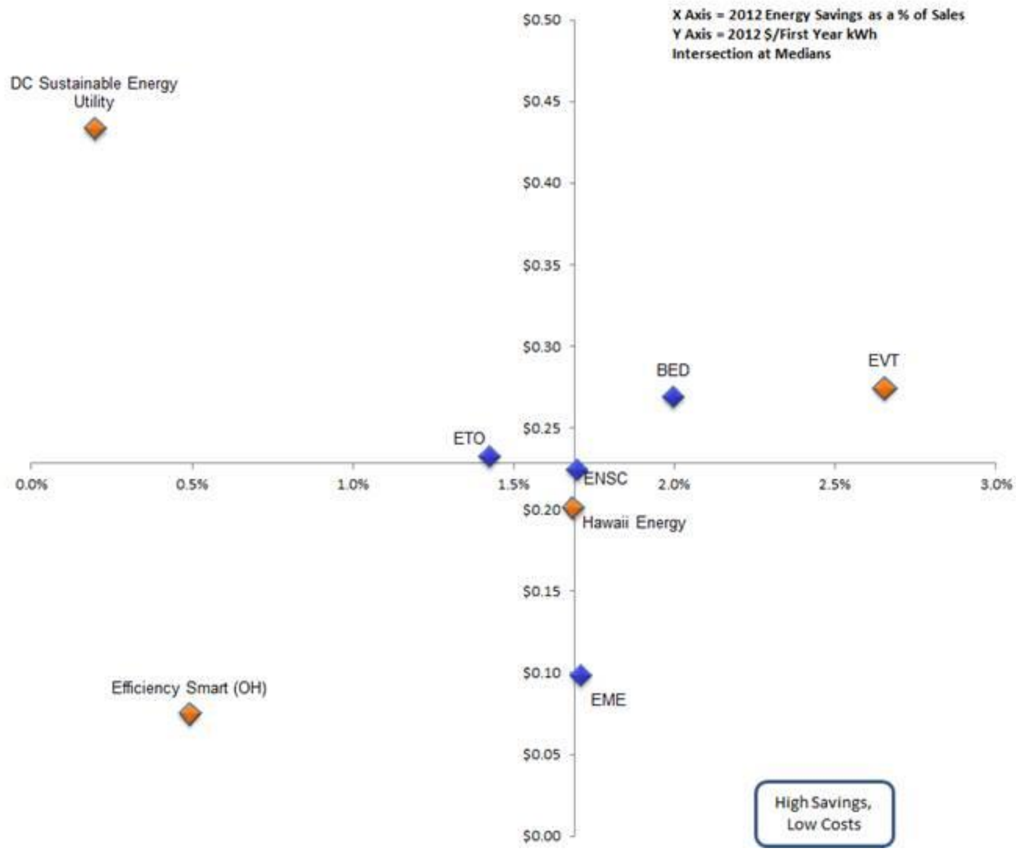
Navigant was able to conduct three interviews with third party for-profit implementation contractors (none of whom are working for the program administrators under review in this project) and found that the most common compensation structure for third party implementation contractors is a hybrid of time and materials combined with at risk performance based compensation. The implementation contractors Navigant spoke with summarized that on average, 100% time and materials compensation contracts are rare in the industry today, with a far more common structure being a blend of time and materials and at risk performance based compensation. The amount of compensation at risk typically ranges between 20% to 50%, and is earned through achieving agreed upon performance indicators. These performance indicators are typically a combination of achieving energy savings targets and non-volume performance indicators including customer satisfaction metrics, rebate processing time, safety performance, and other service level indicators. Our small focus group reported that the use of a performance compensation bonus, on top of base compensation (performance based or otherwise), is very rare, and almost non-existent (only one instance in the past five years was a performance bonus made available to a major for-profit implementation contractor with whom we spoke). As such, based on this early and limited feedback, Navigant can generalize that the use of some percentage of at risk performance compensation is standard in the industry, while the use of additional performance compensation bonus payments (above and beyond base compensation) is rare for third party implementation contractors. With that said, Navigant only spoke with three firms, as such, it is difficult to generalize confidently across the entire DSM industry.

Due to time limitations for this project, Navigant was unable to verify in detail the compensation structures and/or use of performance compensation bonuses for all of the third party implementation contractors working for the program administrators included in this review. Navigant assumes the pricing structure used by third party for-profit implementation contractors for base compensation includes a profit margin premium as part of their negotiated base compensation. As such, achieving goals and receiving full compensation includes direct labor costs plus a profit margin. Navigant is uncertain of the profit margins earned by third party implementation contractors (for profit or non-profit) and this could be an additional area of research upon request.

Benchmarking Performance of EVT Peer Group Organizations

Navigant completed a small benchmarking project to compare the savings as a percent of total sales and first year cost per kWh saved for the select group of peer organizations. Organizations confirmed to be providing a performance compensation to their third party implementation contractor (DC SEU, Hawaii, and Efficiency Smart Ohio, EVT), are noted in Figure 1 with a tan color.[10] The X axis in the figure represents savings as a percent of total electric sales in the service territory. The Y axis details first year cost per KWh saved for 2012. Where the two axis' cross is the median among the sampled group. EVT is located in the upper right quadrant, indicating compared to this peer group, EVT's savings are greater than median and at a cost that is higher than median.

Figure 1: EVT Benchmarking: 2012 Savings as a Percent of Sales and First Year Cost Per KWh

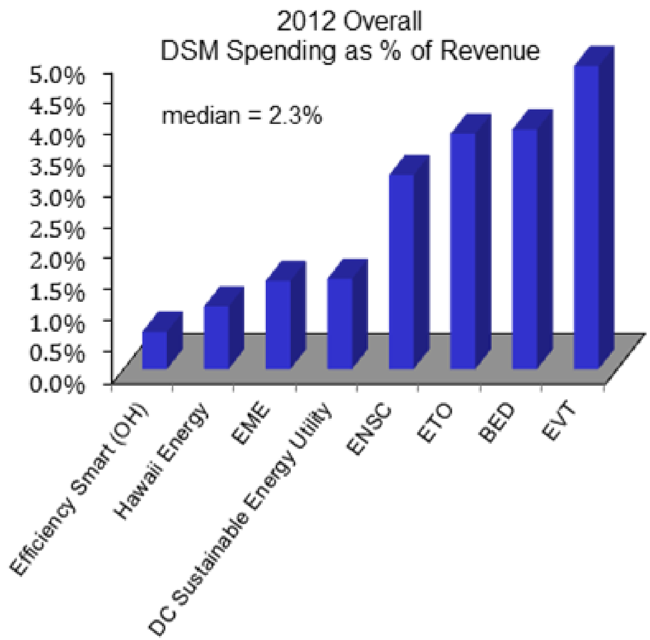


Source: Navigant –draft research.

[10] Due to time limitations associated with completing this research, the following disclaimers are required: a) NYSERDA is excluded from the benchmarking comparison due to data quality issues in NEEP's REED database currently; b) Navigant assumed that PEPCO (DC) as the basis for estimating overall energy sales in the District of Columbia; c) Navigant also assumed baseline sales for 3 HI IOUs for Hawaii Energy (Maui Electric Co, Hawaiian Electric Co, and Hawaii Electric Light Co) as the source for total energy sales for Hawaii.; d) Baseline total energy sales data for Efficiency Smart (OH) were provided to Navigant from an industry colleague, but noted as an approximate estimate only. Navigant was unable to confirm the specifics directly with Energy Smart –Ohio staff. Given these caveats, Navigant advises caution with the use of these benchmark findings. With additional time, Navigant is available to research and confirm these data points further.

Figure 2 presents a comparison of the level of DSM investment normalized to spending as a percent of overall electric revenue in the state or service territory as applicable.

Figure 2: 2012 Spending as a Percent of Revenue



Source: Navigant-draft research.

Conclusion

The primary objective of this analysis was to assess and document the use of performance compensation paid to the DSM program administrator as opposed to the third party implementation contractor. With respect to VEIC/EVT, if one considers VEIC as the program administrator, on par with other non-profit organizations like the Energy Trust of Oregon or Efficiency Nova Scotia, then VEIC was the only program administrator to receive performance compensation in our select peer group. If one considers EVT to be equivalent to a third party implementation contractor, working on behalf of a program administrator, then the use of performance compensation are more common for this identified peer group. However, further research is required to more comprehensively understand the use and design of performance compensation for third party implementation contractors working on behalf of the program administrators included in this peer group, and overall across the industry. Navigant's overall assessment, speaking broadly on our understanding of the DSM industry, is that typically third party implementation contractors just receive base compensation (which is blend of time and materials and at risk compensation), and the use of an additional performance compensation, above and beyond 100% of direct cost-recovery is less common.

Appendix A: Program Administrator Peer Group Performance Incentive Notes

This section presents additional summary detail by program administrator with respect to the use of performance compensation. With additional time, Navigant could expand this discussion, and note in more detail performance compensation structure.

VEIC/ EVT: VEIC is a non-profit organization that delivers the EVT contract under a 12 year order of appointment from the Vermont Public Service Board. VEIC, as the program administrator for EVT, receives performance compensation based on achieving negotiated performance indicators. Compensation is both guaranteed (operations fee) and at risk (performance awards).

Burlington Electric Department (BED): BED is a municipal utility and does not receive performance compensation. Navigant is uncertain if third party contractors working for BED receive performance compensation.

Efficiency Maine (EME): Efficiency Maine is a quasi-government program administrator that utilizes third party implementation contractors for program delivery. The administrator does not receive performance compensation. Navigant confirmed that third party contractors working for Efficiency Maine do not receive performance compensation.

Energy Trust of Oregon (ETO): Energy Trust of Oregon is a non-profit program administrator that utilizes third party implementation contractors for program delivery. The administrator (ETO) does not receive performance compensation. Third party implementation contractors working on behalf of ETO are eligible in most cases to earn performance compensation for exceeding their savings targets. The compensation increases, on a scale basis, as the percent of savings target is achieved, and then exceeded, up to a cap of 110% of the savings goal. Overall, ETO allocates approximately 1.3% of the annual operating budget for the bonus compensation, which in 2012 was approximately $2 million. More broadly, third party implementation contractors working for ETO operate under a contract structure that includes a 5% hold back retainage, which is paid upon 100% of savings and other specified performance targets being achieved. In addition, ETO offers additional compensation for contractors in the form of quarterly payments (e.g. $5,000 for meeting a specific quarterly performance milestone) that may be related to database accuracy, or processing time of rebate payments, etc.

Efficiency Nova Scotia (ENSC): Efficiency Nova Scotia is a non-profit program administrator that utilizes third party implementation contractors for program delivery. The administrator does not receive performance compensation. Navigant confirmed that third party contractors working for Efficiency Nova Scotia do not receive performance compensation.

NYSERDA: NYSERDA is a quasi-state government program administrator that utilizes third party implementation contractors for program delivery. The administrator does not receive performance compensation. According to, NYSERDA, under the Green Jobs – Green NY Program, Constituency Based Organizations who help conduct program outreach for residential and other customer types do have performance bonuses. However, for core energy efficiency program delivery, such as the

Commercial/Industrial programs, implementation contracts have performance targets but no bonus structures. In some cases, if applicable, the "reward" is renewal of the contract. In the Multifamily Program, there are no bonuses but part of the contract is performance based and there is a penalty if targets are not attained. Some of NYSERDA's contracts also have retainage of a percent of payments until certain milestones are met.

Efficiency Smart – Ohio: Efficiency Smart -Ohio is the DSM brand for American Municipal Power – Ohio, a network of municipal utilities. Navigant assumes AMP-Ohio, as a municipal utility program administrator, does not receive performance compensation. AMP Ohio utilizes third party implementation contractors (VEIC) for program delivery and issues performance compensation.

DC Sustainable Energy Utility (DC SEU): The DC Sustainable Energy Utility is a quasi-government organization. Navigant assumes the DC SEU, as a municipal government program administrator, does not receive performance compensation. The DC SEU utilizes third party implementation contractors (VEIC) for program delivery and issues performance compensation.

Hawaii Energy: Hawaii Energy is a quasi/government program administrator that utilizes third party implementation contractors for program delivery. Navigant assumes the administrator (Hawaii Public Utilities Commission) does not receive performance compensation. The third party implementation contractor (Leidos Engineering- for-profit) can receive a performance compensation, totaling 0.4% of total budget; $133,000 was available in 2012 for achievement above 100% of goal across five quantifiable performance target areas.

Leidos, the IC of Hawaii Energy, funds a "performance pool" hold back of approximately $700,000 annually through monthly holdback payments. Following evaluation, this performance pool of withheld funds may be earned commensurate with achievement across a series of Quantifiable Performance Indicators (QPIs) that are established by contract and outlined below. Achievement above 100% of goal entitles Leidos to a performance award of $133,000, or approximately 0.4% of the total budget.

PY2013 Performance Incentives				
		Program Incentive Award		
Performance Target Item	***% of Target***	***Minimum***	***Target***	***Maximum***
		75%	100%	123.8%
First Year Energy Reduction	35%	$ 183,750	$ 245,000	$ 303,188
Peak Demand Reduction	5%	$ 26,250	$ 35,000	$ 43,313
Total Resource Benefit	40%	$ 210,000	$ 280,000	$ 346,500
Infrastructure development	10%	n/a	$ 70,000	$ 70,000
Island Incentive Equity	10%	n/a	$ 70,000	$ 70,000
Total			$ 700,000	$ 833,000
Potential Award for Performance in Excess of Targets				$ 133,000

Total Incentives	$	21,904,787.00	65%
Total Operations	$	11,578,244.00	34%
Total Award in Excess of Target*	$	133,000.00	0%
Total Budget	$	33,616,031.00	100%

* = This Incentive Award budget amount is not earned until performance is achieved.

Source: State of Hawaii Supplemental Contract No. 5. May 31, 2013. Detailing terms of the program administrator of public benefit funds.