
A BILL FOR AN ACT

RELATING TO THE PUBLIC UTILITIES COMMISSION.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. The legislature finds that, in 2018, the
2 legislature enacted the Hawaii Ratepayer Protection Act to
3 provide proactive protections to the State's electric utility
4 customers. Act 5, Session Laws of Hawaii 2018 (Act 5), provided
5 that electric utility rates would be considered just and
6 reasonable only if they were derived from a performance-based
7 model for determining utility revenues. Act 5 emphasized that
8 the State should adjust electric utilities' interests to better
9 align with customers' interests. The legislature found that
10 there was "extraordinary urgency" for this realignment.

11 Act 5 directed the public utilities commission to establish
12 a performance-based model for utility regulation and ratemaking
13 based on performance incentives that "directly tie an electric
14 [utility's] revenues to that utility's achievement on
15 performance metrics and break the direct link between allowed
16 revenues and investment levels." The intent of this
17 performance-based model was to depart from the traditional



1 cost-of-service model that rewards utilities for increasing the
2 utility's capital expenditures and bases allowed revenues on the
3 value of the rate base, irrespective of the utility's
4 performance. The legislature recognized that the traditional
5 model misaligned the interests of customers and utilities
6 because it created a possible bias toward utilities that
7 expended capital on utility-owned projects, rather than
8 utilities that supported more efficient or cost-effective
9 options like customer-owned distributed energy resources or
10 independent, third-party projects. The legislature concluded
11 that the State needed a shift away from the traditional focus on
12 utility costs to a more modern focus on performance.

13 The legislature further finds that, in response to the
14 Hawaii Ratepayer Protection Act, the public utilities commission
15 opened its performance-based regulation proceeding as a
16 historic, multi-phase process that included participation from
17 local and national experts. In December 2020, the commission
18 established a comprehensive framework for performance-based
19 regulation that has since been nationally recognized as a
20 leading model. The guiding principles for this framework
21 include a customer-centric approach, including day-one savings



1 for customers; administrative efficiency through a simplified
2 regulatory framework; and utility financial integrity with the
3 opportunity to earn profits and rewards through performance.
4 The main features of the framework include a multi-year rate
5 period of five years, during which the utility's allowed
6 revenues are determined not by traditional rate cases but by an
7 objective index tied to general inflation. The utility's
8 profits are driven largely by its ability to capture cost
9 savings and efficiencies. The framework also includes
10 performance incentive mechanisms to reward or penalize a utility
11 based on its performance on public interest priorities like
12 reliability, accelerated progress toward renewable energy, and
13 improved customer service. The commission emphasized that, with
14 the transition away from traditional cost-of-service regulation,
15 customers would benefit from lower utility costs.

16 In establishing the performance-based framework, the public
17 utilities commission recognized the need for a transformative
18 and lasting shift away from cost-of-service regulation. The
19 commission made clear that, after the five-year rate control
20 period, the commission anticipated continuing to refine the
21 performance-based framework and did not envision returning to



1 cost-of-service regulation. However, now that the end of the
2 rate control period is approaching, the legislature is concerned
3 about the integrity of the performance-based framework and the
4 commission's compliance with the Hawaii Ratepayer Protection
5 Act. For example, last year, the commission adopted the
6 utility's proposal to initiate a traditional, cost-of-service
7 rate to "re-base" the utility's allowed revenues using its
8 projected increased costs. This cost-based rebasing of revenues
9 backtracks on the progress and reforms the State has made and
10 violates the commission's previous commitment not to return to
11 cost-of-service regulation.

12 The legislature is also aware that the public utilities
13 commission has insisted on requiring a "forward test year"
14 approach to the rate case, in which a utility requests a rate
15 increase based on future cost projections, rather than the
16 historical cost trends that have been controlled under the
17 performance-based framework. This return to forecast
18 cost-of-service ratemaking encourages utilities to make "wish
19 lists" of capital projects to boost utility profits, thereby
20 inflating customer rates. However, the predominant practice in
21 rate cases is to use historical costs adjusted for known and



1 measurable changes, rather than forecast future costs, as the
2 basis for regulatory rate analyses. Jurisdictions using
3 forecast costs instead of historical costs end up paying
4 substantially higher rates.

5 The legislature recognizes that the public utilities
6 commission has expressed the belief that it is constrained by
7 existing legal provisions to follow certain traditional cost-
8 bound methods, notwithstanding the mandates of the Hawaii
9 Ratepayer Protection Act. As a result, the commission is
10 inviting a return to "cost-plus" ratemaking that threatens to
11 undermine the benefits and progress achieved under the
12 performance-based framework. This poses the risk of significant
13 rate increases for customers.

14 Based on this stance by the public utilities commission and
15 the risk of rate increases for customers, the legislature
16 believes that further clarification and guidance are needed to
17 ensure that the commission upholds the legislature's original
18 intent under the Hawaii Ratepayer Protection Act and continues
19 the progress made under the commission's performance-based
20 regulatory framework. These clarifications will help ensure
21 that both electric utilities and ratepayers will continue to



1 benefit from the utilities' improved performance, lower costs,
2 and lower rates.

3 Accordingly, the purpose of this Act is to provide
4 clarification and guidance by:

- 5 (1) Clarifying that, for the purposes of regulating
6 electric utility rates, "performance-based incentives"
7 include revenue adjustment mechanisms; cost control
8 mechanisms, such as the multi-year rate period;
9 rewards for superior performance; and penalties for
10 subpar performance;
- 11 (2) Authorizing the public utilities commission to adopt
12 alternative ratemaking procedures to establish
13 electric utility rates and performance-based
14 incentives that fulfill the requirements of section
15 269-16.1, Hawaii Revised Statutes; and
- 16 (3) Requiring the public utilities commission to apply a
17 presumption in favor of considering historical cost
18 trends and external indices that reflect incentives to
19 control costs if resetting an electric utility's
20 allowed revenues based on consideration of the
21 utility's costs.



1 SECTION 2. This Act shall be known and may be cited as the
2 Hawaii Ratepayer Protection Act of 2026.

3 SECTION 3. Section 269-16.1, Hawaii Revised Statutes, is
4 amended to read as follows:

5 "~~§269-16.1 [Performance incentive and penalty mechanisms]~~
6 Performance-based incentives; regulation of electric utility
7 rates. (a) On or before January 1, ~~[2020,]~~ 2027, the public
8 utilities commission shall establish ~~[performance]~~
9 performance-based incentives, including revenue adjustment
10 mechanisms, cost control mechanisms, and reward and penalty
11 mechanisms, that directly tie an electric ~~[+]utility's[+]~~
12 revenues to that utility's ~~[achievement on]~~ performance
13 ~~[metrics]~~ and break the direct link between allowed revenues and
14 investment levels. The ~~[performance]~~ performance-based
15 incentives ~~[and penalty mechanisms]~~, as may be amended by the
16 public utilities commission from time to time, shall apply to
17 the regulation of electric utility rates under ~~[section 269-16.]~~
18 this chapter.

19 (b) Notwithstanding any law to the contrary, including the
20 ratemaking procedures described in section 269-16, the public
21 utilities commission may adopt, by commission order, alternative



1 ratemaking procedures to establish electric utility rates and
2 performance-based incentives for purposes of subsection (a);
3 provided that the rates shall be derived from a
4 performance-based model for determining utility revenues.

5 (c) If resetting an electric utility's allowed revenues
6 based on consideration of the utility's costs, the commission
7 shall apply a presumption in favor of considering historical
8 cost trends and external indices that reflect incentives to
9 control costs, rather than relying on a forward test period.

10 ~~[(b)]~~ (d) In developing ~~[performance incentive and penalty~~
11 ~~mechanisms,]~~ performance-based incentives, the public utilities
12 commission's review of electric utility performance shall
13 consider~~[, but not be limited to,]~~ the ~~[following]:~~

- 14 (1) ~~[The economic]~~ Economic incentives and cost-recovery
15 mechanisms described in section 269-6(e);
- 16 (2) Volatility and affordability of electric rates and
17 customer electric bills;
- 18 (3) ~~[Electric service reliability;]~~ Reliability of
19 electric service;



- 1 (4) ~~[Customer]~~ Level of customer engagement and
2 satisfaction, including customer options for managing
3 electricity costs;
- 4 (5) ~~[Access to]~~ Accessibility of utility system
5 information, including ~~[but not limited to public~~
6 ~~access to]~~ electric system planning data ~~[and],~~
7 aggregated customer energy use data ~~[and individual~~
8 ~~access to]~~, and granular information about an
9 individual customer's own energy use data;
- 10 (6) Rapid integration of renewable energy sources,
11 including quality interconnection of customer-sited
12 resources; and
- 13 (7) Timely execution of competitive procurement,
14 third-party interconnection, and other business
15 processes.

16 ~~[-e)]~~ (e) This section shall not apply to a member-owned
17 cooperative electric utility."

18 SECTION 4. Statutory material to be repealed is bracketed
19 and stricken. New statutory material is underscored.



1 SECTION 5. This Act shall take effect on July 1, 3000.



Report Title:

PUC; Ratemaking; Performance-Based Incentives; Hawaii Ratepayer Protection Act

Description:

Clarifies that, for electric utilities, "performance-based incentives" include revenue adjustment mechanisms, cost control mechanisms, rewards for superior performance, and penalties for subpar performance. Authorizes the Public Utilities Commission to adopt alternative ratemaking procedures to establish electric utility rates and performance-based incentives. Requires the Commission to apply a presumption in favor of considering historical cost trends and external indices that reflect incentives to control costs if the Commission resets an electric utility's allowed revenues based on consideration of the utility's costs. Effective 7/1/3000. (HD1)

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