**BEFORE THE PUBLIC UTILITIES COMMISSION**
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| Order Instituting Rulemaking to Create a Consistent Regulatory Framework for the Guidance, Planning, and Evaluation of Integrated Distributed Energy Resources. | Rulemaking 14-10-003 (Filed October 2, 2014) |

# COMMENTS OF THE CALIFORNIA ENERGY STORAGE ALLIANCE ON THE ASSIGNED COMMISSIONER'S RULING INTRODUCING A DRAFT REGULATORY INCENTIVES PROPOSAL FOR DISCUSSION AND COMMENT

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In accordance with Rules of Practice and Procedure of the California Public Utilities Commission ("Commission"), the California Energy Storage Alliance ("CESA")[1] hereby submits these comments on the *Assigned Commissioner's Ruling Introducing a Draft Regulatory Incentives Proposal for Discussion and Comment*, issued on April 4, 2016 ("Ruling").

## I. INTRODUCTION.

CESA is generally supportive of the concept of the draft Regulatory Incentives Proposal ("Proposal") that would allow the utilities to earn a return on contracted payments to third-party

[1] 1 Energy Systems Inc., Advanced Microgrid Solutions, AES Energy Storage, Aquion Energy, Brookfield, CODA Energy, Consolidated Edison Development, Inc., Cumulus Energy Storage, Customized Energy Solutions, Demand Energy, Dynapower Company, LLC, Eagle Crest Energy Company, East Penn Manufacturing Company, Ecoult, ELSYS Inc., Energy Storage Systems, Inc., Enersys, Enphase Energy, EV Grid, GE Energy Storage, Gordon & Rees, Green Charge Networks, Greensmith Energy, Gridtential Energy, Inc., Hitachi Chemical Co., Ice Energy, IMERGY Power Systems, Innovation Core SEI, Inc. (A Sumitomo Electric Company), Invenergy LLC, K&L Gates, LG Chem Power, Inc., LightSail Energy, Lockheed Martin Advanced Energy Storage LLC, LS Power Development, LLC, Mitsubishi Corporation (Americas), NEC Energy Solutions, Inc., NextEra Energy Resources, NRG Solar LLC, OutBack Power Technologies, Panasonic, Parker Hannifin Corporation, Pathfinder, Powertree Services Inc., Primus Power Corporation, Princeton Power Systems, Recurrent Energy, RES Americas Inc., S&C Electric Company, Saft America Inc., Sharp Electronics Corporation, Skylar Capital Management, SolarCity, Sovereign Energy, Stem, SunEdison, SunPower, Toshiba International Corporation, Trimark Associates, Inc., Trina Energy Storage, Tri-Technic, UniEnergy Technologies, Wellhead Electric, Younicos. The views expressed in these Comments are those of CESA, and do not necessarily reflect the views of all of the individual CESA member companies. (http://storagealliance.org).

distributed energy resource ("DER") providers to defer or displace utility infrastructure investments. Under the Proposal, with the rate of return set appropriately high enough and costs fully recovered through rate cases, CESA agrees that utilities will be better incentivized to invest in third-party DER solutions for certain use cases (*e.g.*, distribution deferral).

CESA understands that the Commission wishes to take a "walk, jog, run" approach to defining utility roles and business models with respect to DER deployment.[2] In the near term, CESA supports the Commission's validation of this Proposal in the demonstration projects scheduled in the Distributed Resources Plan proceeding (R.14-08-013). However, in the next phase of this proceeding, CESA hopes that alternative sourcing mechanisms such as tariffs or other mechanisms will be explored and tested. In many cases, RFOs may prove too cumbersome and alternative sourcing mechanisms may be more appropriate in deploying cost-effective DERs.

## II. CESA'S RESPONSES TO QUESTIONS POSED IN THE RULING.

***Question 1:*** ***Is the description of the source of utility shareholder value summarized above and discussed in the Appendices accurate? If so, why not?***

CESA believes that the Proposal correctly attributes the "value engine" for utility investments to be the difference between the return on equity ("r") and its cost of equity ("k").

***Question 2:*** ***Would an incentive program such as that described above achieve the objective of promoting the cost-effective deployment of DERs? If not, why not?***

For the distribution deferral use case where cost-effectiveness comparisons to traditional capital investments (*e.g.*, substations or distribution line upgrades) can be more readily made, the proposed incentive program can promote the cost-effective deployment of DERs. When making

[2] Ruling, p. 2.

these comparisons, however, CESA believes is important that the investor-owned utilities ("IOUs") consider portfolios of DERs during utility solicitations rather than limiting their RFOs to specific or single resource types. The IOUs' RFOs should be technology agnostic, identifying system constraints that DER solution providers should address rather than seeking specific resources or technologies. For example a solution may consist of aggregated energy storage systems or solar-plus-storage systems, which together provide greater functionality in deferring infrastructure investments than a standalone energy storage system.

Furthermore, as highlighted in the paper appended to the ruling,[3] the scale of investments is an important incentive for the IOUs. If third-party DER solutions are more cost-effective, even if the percentage return is set at (r-k), because that value is applied against a lower amount, the IOUs will still be biased in favor of the more costly conventional utility solution. To address this, the return on contracted payments will need to be higher than (r-k) to account for the reduced cost of the third-party DER solution. Additionally, further clarity is needed on how the Locational Net Benefits Analysis ("LNBA") from R.14-08-013 would overlay the cost-effectiveness analysis employed in these RFOs. CESA understands that these details will be worked out later in the proceeding, so at this point just intends to highlight the importance of determining how LNBA inputs should be incorporated in the cost-effectiveness calculations.

Finally, it is unclear how DER deployment would be incentivized outside of the distribution deferral use case currently being considered. The proposed (r-k) incentive framework appears to apply to only a narrow set of large capital investments. However, there are a significant number of DER applications where they may be cost effective, but are not of

[3] *You Get What You Pay For: Moving Toward Value in Utility Compensation*. Attachment B, published on June 2015, pp. 19, 21-22.

sufficient scale where an RFO would be a reasonable contracting mechanism. In many cases, tariffs or other type of contracting approaches may be preferable and more reasonable given the relatively small scale of many distribution system investments.

***Question 3: What alternative approaches should the Commission consider at this time?***

The (r-k) incentive framework proposes to allow the IOUs to earn a return on contracted payments to third-party DER providers to defer or displace utility infrastructure investments. While these service payments to DER providers would potentially make it more viable for utilities to invest in DERs, the utilization of these DER assets will be sub-optimal if the contractual terms unduly limit the ability of DER providers to use their systems to provide other services beyond those the solution is specifically contracted to provide. A key advantage of DERs such as energy storage is that they can provide multiple services from a single asset, unlike most traditional IOU capital investments. To provide the greatest value to ratepayers and the grid, the Commission should seek to ensure that DERs are allowed to provide secondary grid services (perhaps as a market resource in the wholesale market or retail services to a host customer) when they are not needed for distribution deferral and reliability. Allowing for these multiple value streams will help IOUs and ratepayers realize the full benefit of DERs.

As noted above, alternative sourcing mechanisms should also be considered and validated for the appropriate use cases. CESA hopes that California can eventually advance to a "plug-and-play" grid where DERs can freely and quickly interconnect to meet identified grid needs. This could come in the form of utility incentives resulting from performance-based regulation, from a more market-based approach, such as an hourly or real-time distribution marginal price, or from tariffs that require certain types of dispatch control in exchange for some form of compensation.

***<u>Question 4</u>: Is the proposed incentive, in the range of 3.5% grossed up for taxes, approximately correct?***

The Ruling does not seek to set the precise value of the incentive at this time and only seeks to validate the concept, but for the purposes of discussion, proposes an incentive in the range of 3.5%. However, CESA finds that this 3.5% range is likely insufficient to incentivize DER deployment given the lack of IOU experience in procuring DERs for distribution deferral. There will be institutional barriers and inertia that are likely to limit the willingness of the IOUs to fully embrace DERs without some additional incentive beyond what would be required to make them financially indifferent. Additionally, as noted above, the mechanism will need to grapple with how to address the lower gross amount the utilities earn when they elect to pursue DER contracts in lieu of more costly utility investments. CESA does not propose a specific value that would represent a sufficiently high incentive for utilities to deploy DERs, but will work with parties later in this proceeding, as intended in the Ruling, to determine this value.

***<u>Question 5</u>: Are there other disincentives to the deployment of DERs that this proposal does not address that should be considered at the same time? If so, please explain.***

There are several non-financial disincentives for DER deployment that are not addressed by the Proposal. Some of these barriers include the lack of familiarity IOUs have with procuring and operating DERs on their distribution grids, which will require the IOUs to develop new competencies and possibly groups or divisions within their procurement organizations. These issues will likely need to be considered and resolved outside of the Proposal.

***<u>Question 6</u>: Is the suggested process for identifying and approving DER projects that would generate an incentive reasonable and appropriate? How could the process be improved?***

One of the reasons that the Proposal argues against DER procurement directives is that "the regulatory process necessary to make such determinations may be so lengthy, detailed and contentious that the underlying data would become stale before any decision could be reached."[4] But in proposing a (r-k) incentive approach, the Proposal as it stands now does not expedite the regulatory approval process for DER deployments. The Proposal proposes that Tier 3 Advice Letters be submitted to detail the solicitation for DERs for identified needs in certain locations, followed by a public workshop, opportunities for comments and protests, and finally applications for approval. CESA believes that this regulatory process for approving DER deployments does not avoid the regulatory lag concerns expressed by the Commission when rejecting DER procurement directives as a DER deployment approach. To expedite the regulatory process, CESA recommends that the Commission consider pre-authorizations for incremental DER investments over a set period of time that meet the goals of this proceeding. These investments could be later reviewed for prudency. With this approach, CESA believes that the regulatory lag will be reduced. At a minimum, the Commission should not require the IOUs to submit applications for the projects they ultimately select through their solicitations. Instead, the Commission should rely on a less burdensome advice letter process.

In addition to the lengthy regulatory approval process for DER projects under the pilot, CESA is concerned about using RFOs to solicit DER project bids. The bidding process tends to be very expensive and time-consuming, which may discourage DER providers from engaging in

[4] Ruling, p. 7.

an RFO, especially if there is significant uncertainty about the timing and outcome of the process. Where appropriate, CESA therefore recommends the development of standard contract terms to shorten the bidding process or to consider the development of tariffs or other contractual approaches to procuring DERs services. After all, one of the key advantages of DERs is that they can be quickly deployed as compared to traditional capital infrastructure.

***Question 7: Is there a need for a limit on the number of projects or the amount of dollars that a utility could propose during this pilot program? If so, what should it be?***

CESA has no comment at this time.

***Question 8: Would participation in a DER solicitation by a utility affiliate require any changes to the Affiliate Transaction Rules, or any changes to the process for review and approval of proposed DER solutions?***

CESA has no comment at this time.

***Question 9: What would be the appropriate role of the IOUs themselves in the deployment of cost-effective DERs? Should direct IOU participation in DER deployment be encouraged, foreclosed, or allowed with certain caveats? Please fully explain your answer.***

CESA does not support IOU ownership of DERs for the foreseeable future. There are numerous third party solution providers with the necessary operational experience in aggregating and managing DERs. As such, there does not appear to be any rationale to support IOU ownership. Additionally, to the degree the objective of the pilot is to eliminate the conflict of interest that currently exists, whereby the IOUs prefer to make utility-owned investments over third-party owned DER solutions, allowing the utilities to own those DERs would appear to replace one conflict of interest with another. Understandably, CESA recognizes that there may be some risk profiles associated with DERs providing distribution reliability services due to the lack of operational experience of IOUs in using DERs for this use case. For this reason, the

Commission should also consider how to use the (r-k) framework to fairly compensate utility shareholders for undertaking these perceived risks.

## III. CONCLUSION.

CESA appreciates the opportunity to submit these comments on the Ruling and the Proposal and looks forward to working with the Commission, the IOUs, and other parties in this proceeding to advance development and implementation of new regulatory incentives that encourage the deployment of energy storage and other DERs.

Respectfully submitted,

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