

Comments in Response to the Draft NARUC MANUAL ON DISTRIBUTED ENERGY RESOURCES
COMPENSATION

by

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I offer the following comments based on my past experiences as the Chairman of the Michigan Public Service Commission, Managing Director and Senior Investment Analyst at UBS Global Asset Management, and Chief Financial Analyst of the Illinois Commerce Commission.

By preparing this draft Manual on Distributed Energy Resources Compensation, NARUC is providing an outstanding service to states by highlighting the timely need to address rate design related to distributed energy resources (DER). In addition to being generally thorough and balanced, the draft manual is extremely well-timed. Several state regulatory commissions have already begun implementing alternative rate designs in response to the growth of DER, while others will be confronted with this task in the near to intermediate term.

NARUC's mission is to serve in the public interest by improving the quality and effectiveness of public utility regulation. A key component of improving regulation is to facilitate the dissemination of emerging regulatory information to member Commissions to enable decision making before crises develop. By finalizing revisions to this draft manual in November, NARUC will provide a useful resource to the states and facilitate near and intermediate term regulatory and legislative decision making.

Different states may choose different solutions through different implementation pathways based on their own unique circumstances. Each state is equipped to select one or more appropriate forum to address DER rate design issues including legislation, rate cases, value of solar proceedings, other formal proceedings, and/or collaboratives. But regardless of the forum, this Manual can serve as a key resource to facilitate the decision making process.

As state jurisdictions clarify how DER rate design issues will be addressed and resolved, electric utility customers in the aggregate will benefit by the removal of the negative impacts of the cost shift that the draft Manual acknowledges accompanies net energy metering. The elimination of the cost shift would ensure that all customers enjoying the benefits of the grid pay their fair share.

Moody's Investors Services (Moody's), an organization that rates electric utility debt, aptly describes the nature of the DER cost shift on page 54 of its December 23, 2013 report entitled "Moody's Rating Methodology: Regulated Electric and Gas Utilities:"

“The distributed generation customer has no obligation to generate any particular amount of power, so the utility must stand ready to generate and deliver that customer’s full power needs at all times. Since most utility costs, including the fixed costs of financing and maintaining generation and delivery systems, are currently collected through volumetric rates, a customer owning distributed generation effectively transfers a portion of the utility’s costs of serving that customer to other customers with higher net usage, notably to customers that do not own distributed generation.”

More recently, Fitch Ratings (Fitch), another organization that rates electric utility debt, made the following observations in its July 18, 2016 special report entitled “Net Energy Metering: A Secular Credit Challenge for IOUs”:

“The conundrum for regulators and utilities from an energy policy point of view is facilitating development of distributed solar PV and its clean energy attributes without unduly burdening non-NEM customers with higher bills due to cross-subsidization of NEM customers.” (Page 1)

“Fitch believes the impact of PV solar is manageable within the regulatory compact, based on existing technology, via adoption of tariff mechanisms with appropriately calibrated fixed versus variable cost-recovery mechanisms and avoided cost-based payments for exports to the grid.” (Page 1)

“Fitch believes adoption of fixed-variable rate structures calibrated to reflect the utility industry’s mix of fixed and variable costs would address the cost shift caused by vanishing revenues used to support utility fixed costs when customers install solar PV systems. This would ensure self-generating customers would be required to pay their fair share of grid transmission, distribution, societal and others costs.” (Page 3)

These observations by Moody’s and Fitch support the concepts that the net energy metering cost shift is negatively impacting customers in the aggregate and that now is the appropriate time for state regulators to level the playing field by proactively addressing the cost shift.

If net metering were to remain in place indefinitely, the electric utility industry’s universal service that results from the obligation to serve all customers would be on a path to extinction. Net energy metering has served its purpose but is unsustainable going forward.

Technological advancement promises to deliver significant customer benefits. The technology of both DER and the grid has advanced and will continue to advance.

For example, solar costs have come down significantly and solar is now a mainstream generation resource. This applies for private residential and commercial solar resources as well as more cost-effective solar resources such as community solar and universal solar. Even in unexpected locations like the Upper Peninsula of Michigan, distributed energy resource caps are being reached. The Upper Peninsula Power Company recently reached its legislatively-determined net metering cap for small solar

installations and Thumb Electric Cooperative is also nearing its net metering cap. The time is past for the need to stimulate solar development through cost-shifting rate design.

Technological advancements in the grid such as advanced meters and sensors are also enhancing the customer experience for all customers including DER-participating customers. To bring enhanced grid benefits to customers, now is the time to unlock the benefits of planning, building, and operating the grid as a platform by incenting investment in grid infrastructure rather than discouraging it by perpetuating the cost shift.

Like customers in the aggregate, customers that are contemplating the installation of private DER also benefit from knowing the rules of the game before making their decision. Timely rate design resolution will provide guidance to customers that desire to own private DER, while avoiding the need for states to hurriedly respond later when significant grandfathering issues may need to be unwound.

Based on the foregoing observations, the time to address alternative rate design issues is now. The timely clarification of solutions will serve customers well. Deferring the identification of a rate design solution while waiting for penetration to increase will only make the negative impact on that state's customers more significant. The finalized NARUC manual will equip the states with a beneficial tool to address these important rate design issues.