

Electric Utility Perspective on Distributed Energy Resources

1. Do what's good for consumers. In today's rate environment, we need to do everything we can to control future rate increases. This means allocating capital to its highest and best uses (i.e., to infrastructure and supply projects which will be most cost-effective). Where DER projects are concerned, we need to make sure that benefits exceed costs, and that benefit/cost ratios are competitive with those available from the best T and D projects. (Note: utilities in the mid-Atlantic are restructured, so they generally do not own generation.)
2. Focus on getting DER incentives right. Today, most utilities in the mid-Atlantic region make nothing on distributed energy resource (DER) projects (e.g., targeted efficiency, demand-side management, distributed generation). The best they can hope for is to recover their costs – eventually. Policies that allow utilities to rate base DER investments and recover costs and earnings timely in rates will go a long way toward encouraging them to develop more DER. Beyond this, incentives should be designed to encourage the development of cost-effective DER. This means measuring benefits and costs in a reliable way, and designing incentives so that more cost-effective projects earn more than less cost-effective projects. EEI, working with National Economic Research Associates, has developed a number of conceptual approaches to incentives design. These are documented in the monograph, *Distributed Resources: Incentives*, available from Eric Ackerman at EEI. (202 508 5528) Incentive models A, B and C, particularly, are designed to encourage efficient development.
3. Policies based on mandates are not in consumers' long-term interest. The alternative to an incentives-based strategy is develop DER pursuant to policy mandates. This may be a temptation, but experience shows that mandates do not elicit efficient development. This is a fundamental lesson of the Public Utility Regulatory Policies Act of 1978; namely, that the mandatory purchase obligation led to the development of “PURPA Machines” whose purpose was to take advantage of the PURPA mandate, not maximize energy efficiency. We should focus on providing incentives for efficient development, then let utilities and third party suppliers see how much cost-effective DER they can find. Remember that DER which is not cost-effective will exacerbate rate increases, not mitigate them. This is the risk we run with mandates.
4. Addressing the “throughput” issue is an important aspect of getting the incentives right. The negative earnings impact which DER can have is a clear disincentive, and should be addressed as part of any DER strategy. (DER will hurt earnings if fixed costs are recovered through kWh-based rate designs, because as kWh send out declines, the utility's revenues will fall faster than its costs.) Decoupling is only one option for addressing this issue, and may have significant disadvantages relative to other options such as developing more accurate standby rates, using contract-based

rates to recover distribution costs, reforming rates to reduce reliance of kWh-based designs, or implementing more targeted / specific lost revenue recovery mechanisms. It's important to address the throughput issue holistically, taking account of the full range of options for dealing with the issue, and giving careful consideration to the impact of a given option on the full range of rate-related impacts. (Note: the pros and cons of decoupling are elaborated in *Distributed Resources: Incentives*, above.)

5. There are several opportunities for valuable DER-related coordination within the mid-Atlantic region. The first involves the development of best practices for measuring the benefits and costs of DER, and allocating costs to customers. This is important because the benefits of DER projects may flow to electricity consumers outside the state in which the DER project is located, so equitable cost allocation would benefit from a regional approach. A second opportunity involves coordinating DER pilot programs so that results can be shared within the region, and states can avoid replicating the same kinds of pilot in multiple jurisdictions. A third opportunity involves the development of a model, or template, for addressing the new PURPA standard involving time-based metering and communications. The issues and uncertainties in deciding whether, and what kind, of advanced metering infrastructure to deploy are substantially the same for all states within the mid-Atlantic region - even if the answer may be different for different utilities with different mixes of customers. Moving toward more uniform decision processes would save money and increase regulatory certainty for utilities operating in multiple jurisdictions in the region.