STATE OF CALIFORNIA

Public Utilities Commission
San Francisco

M e m o r a n d u m

Date: March 20, 2012

To: The Commission
(Meeting of March 22, 2012)

From: Lynn Sadler, Director
Office of Governmental Affairs (OGA) — Sacramento

Subject: **AB 2340 (Williams) – Distribution Grid: distributed generation.**
As introduced: February 24, 2012

LEGISLATIVE SUBCOMMITTEE RECOMMENDATION: OPPOSE

SUMMARY OF BILL:

This bill requires the California Public Utilities Commission (CPUC) to convene a proceeding by July 1, 2013 to establish rules by which developers of generating facilities would receive rate-based reimbursement for distribution system upgrades. The bill requires the rules to ensure that the distribution system upgrades are cost-effective.

SUMMARY OF SUPPORTING ARGUMENTS FOR RECOMMENDATION:

A position of 'Oppose' is recommended for the following reasons:

(1) The bill would reverse longstanding CPUC policy that makes developers of generating facilities responsible for their triggered costs of interconnecting to the distribution grid. In so doing, the bill potentially subsidizes one industry group, and eliminates ratepayer protection from excessive costs based on inefficient siting decisions made by for-profit business interests.

(2) The bill would prejudge a currently open CPUC proceeding that is examining, among other interconnection issues, cost responsibility policy and barriers to entry.

(3) The bill may result in program changes unintended by the author due to terms used in the draft language that are poorly defined.

SUMMARY OF SUGGESTED AMENDMENTS:

None.

DIVISION ANALYSIS (Energy Division):

This bill requires the CPUC to hold a formal proceeding, on or before July 1, 2013, to develop rules for ratepayer reimbursement of distribution grid upgrade costs to accommodate the interconnection of developers of generating facilities.

The major impact of this bill will be to reverse CPUC's direct cost assignment policy. It will have additional impacts on the CPUC's currently open interconnection proceeding.

The bill reverses longstanding Commission policy directly assigning distribution system upgrade costs to the triggering developer.

This bill reverses present CPUC cost responsibility policy that directly assigns the costs of distribution system upgrades necessary to interconnect a new generating facility to the generation developer.[1] Direct cost assignment ensures that ratepayers do not cross-subsidize a for-profit business for the costs that the business imposes on the distribution system. The policy further protects ratepayers from excessive costs based on inefficient siting of a generating facility, while at the same time incentivizing developers to choose cost-efficient locations for their projects. Finally, direct cost assignment guards against the subsidization of one industry group over another that is similarly situated.[2]

The location of a generating facility can have a dramatic impact on the cost of needed distribution system upgrades. For example, if there is significant load near the point of interconnection for the generating facility, system upgrades and associated system upgrade costs will generally be much lower than if there is no load near the new generation. Under the current CPUC policy the generator has a clear incentive to reduce the cost impacts of the interconnection. This bill would remove that incentive and could encourage developers to ignore distribution grid impacts when planning their own projects.

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[1] Resources seeking interconnection to the distribution system can queue under either IOU's Commission-jurisdictional interconnection tariff, Electric Rule 21 (Rule 21), or Federal Energy Regulatory Commission (FERC)-jurisdictional wholesale distribution access tariffs (WDAT or WDATs), depending on their QF status and commercial arrangement. The cost assignment policy for distribution upgrades is the same in Rule 21 and the WDATs.

[2] Notably, the Commission has maintained the direct cost assignment policy for distribution system upgrades triggered by interconnection since the early 1980s, when Rule 21 was first developed following the enactment of PURPA. The single exception is net energy metering (NEM) customer-generators, which are exempt from triggered distribution upgrade costs, pursuant to Public Utilities Code (PUC) section 2827 and Decision (D.) 02-03-057. In D.02-03-057, the Commission explained that the exemption for NEM projects was based on the fact that such primarily non-exporting generating facilities were unlikely to trigger distribution system upgrades.

The bill requires that the ratepayer-funded distribution system upgrades be "cost-effective," but this single constraint does not provide support for the policy reversal. The CPUC now regularly implements cost-effectiveness through procurement program pricing mechanisms and power purchase agreement terms. A direct cost assignment policy embedded in the interconnection process works in tandem with pricing mechanisms. Where distribution system upgrade costs are excessive, a project seeking to participate in a feed-in tariff, an auction based on lowest-price bids, or a program offering avoided-cost pricing likely will not be cost-effective. As a result, the developer will either seek other siting locations, or find other means of gaining efficiencies. Neither of those is an unreasonable marketplace outcome that justifies ratepayer support for a cost-inefficient siting decision. The bill does not provide support for its assertion that a new cost-effectiveness methodology for interconnection other than cost causation is warranted.

Several open CPUC proceedings are presently considering cost and other issues associated with distributed generation.

The CPUC is considering a number of issues associated with distribution level generating facilities within the following open CPUC proceedings:

In September 2011, the CPUC opened a proceeding to examine distribution level interconnection issues.[3] In Phase 1, CPUC staff led a significant reform of Rule 21's design in order to better accommodate today's volume of exporting generating facilities applying for interconnection on the distribution system. Cost responsibility issues and interconnection-related barriers to entry are specifically scoped into Phase 2 of R.11-09-011.

In addition, the CPUC's energy storage proceeding[4] is examining ways that energy storage can reduce the impact of generating facilities on the distribution system. A reduced impact will reduce distribution system upgrade costs for the developer.

Third, the CPUC's Resource Adequacy proceeding[5] will begin developing the rules for implementing a straw proposal of the California Independent System Operator straw proposal to provide Resource Adequacy Deliverability for Distributed Generation.[6] CAISO's proposal, which the CPUC supports at a staff level, will provide additional market signals about efficient siting.

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[3] Order Instituting Rulemaking (R.) 09-11-011.

[4] R.10-12-007.

[5] R.11-10-023.

[6] See http://www.caiso.com/informed/Pages/StakeholderProcesses/DeliverabilityforDistributedGeneration.aspx.

The bill offers no analysis of distribution system upgrade costs as a barrier to entry.

Given the present volume of queued distribution-level interconnection applicants, it is not clear that distribution system upgrade costs are the major barrier to entry for distributed generation. The volume of queued applicants is causing delays in the interconnection studies for all applicants. Exempting developers from distribution system upgrade costs does not cure that problem, and instead is likely to exacerbate it, by encouraging more applicants to join the queue.

Moreover, as noted above, cost responsibility issues are within the scope of R.11-09-011, Phase 2. As part of that scope, data on interconnection-related costs, including application fees and study deposits, interconnection facilities, and distribution system upgrades will be considered.

The CPUC has also issued requests for proposals from expert consultants to examine and present solutions to other potential barriers to entry, including advanced research on integration of generating facilities on the distribution system, continued examination of the technical screens in Rule 21, solar photovoltaic development potential under a range of cost scenarios, and a procurement cost limitation methodology. This technical expertise, analysis, and reports will be additional inputs to the CPUC's consideration of cost issues and barriers to entry within R.11-09-011.

Imprecise draft language in the bill is likely to lead to unintended outcomes.

The bill's draft language contains several imprecise phrases that are likely to lead to unintended outcomes:

- *"Wholesale distribution generation facilities"* are not defined. The author may intend to refer to non-NEM, system-side generating facilities. However, in the context of jurisdiction over interconnection, "wholesale" typically refers to rates subject to FERC jurisdiction, and are distinct from avoided-cost rates set by the state, which are state-jurisdictional. Certain of the CPUC's procurement programs incentivizing resources interconnecting to the distribution system[7] are limited to participants that sell at avoided cost rates as determined by the CPUC. As drafted, the bill would make such participants ineligible for ratepayer-funded infrastructure.

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[7] The Commission's programs for smaller resources (generally, 20 MW and under) include: the Small Generation Incentive Program (PUC section 379.6 and R.10-05-004), the renewable feed-in tariff (PUC section 399.20 and R.11-05-005), the Renewable Auction Mechanism (RAM) (D.10-12-048 and R.11-05-005), the utility solar PV program (D.10-09-016 and R.11-05-005), and a number of new contractual pathways for Qualifying Facilities (QFs) flowing from the QF Settlement (D.10-12-035).

- *"Wholesale distribution generation facilities constructed subsequent to the completion of interconnection studies"* is also not defined. It is not clear whether the author is referencing generating facilities or distribution system upgrades. The bill's language is vague as to whether the distribution system upgrades are those identified in course of the applicant's interconnection studies, or are identified by the utility separate from (but following the completion of) an applicant's interconnection studies.

- As drafted, the bill is silent on whether developers of generating facilities on the distribution system that may not be eligible for ratepayer-funded infrastructure are permitted to proceed. If the author's intent is to deny such opportunity, then the bill works counter to the CPUC's design of price-driven procurement programs, which allow market actors to find cost efficiencies. CPUC policy presently permits such risk-taking by developers, particularly where it does not have ratepayer impact.

As a result of such imprecise language, the bill is likely to have unintended outcomes, such as triggering a rush to file interconnection applications, exacerbation of the present queue problems, preferential treatment of otherwise similarly situated interconnection applicants (i.e., non-QFs versus QFs), and subsidization of one industry group over others.

PROGRAM BACKGROUND:

Since August 2011, the CPUC has led a significant reform effort to redesign Rule 21 to accommodate today's volume of exporting generating facilities applying for interconnection to the distribution system. The reform is occurring within a confidential settlement involving approximately 80 parties, including IOUs, the California ISO, ratepayer advocates, independent power producers, renewable energy advocates, best practices organizations, and state and federal agencies. By consensus of the settlement parties, the revised Rule 21 specifically retains the direct cost assignment for distribution system upgrades, and cost-related issues are recommended as within the scope of Phase 2.

The contents of the revised Rule 21 tariff are anticipated to be made public in a filing in R.11-09-011 on approximately March 19, 2012.

"Wholesale" generation facilities are generally subject to FERC jurisdiction rather than CPUC jurisdiction, but distribution facilities are generally subject to CPUC jurisdiction. Because of this ambiguity and possible conflict regarding jurisdiction, CPUC implementation of the bill could result in litigation, particularly over questions of jurisdiction and/or federal preemption. While the bill calls for the CPUC to refer to federal rules relating to transmission facilities that is not adequate to resolve the confusion that this bill has the potential to create. While the CPUC may be able to interpret and implement the bill in a way that avoids jurisdiction and preemption issues, this bill presents potentially serious legal issues and litigation risk.

FERC has jurisdiction over utility wholesale transmission lines. FERC has set out its cost assignment policy parameters for transmission resources in a series of orders, and the CAISO tariff, including Appendix Y, Generator Interconnection Procedure, is subject to FERC jurisdiction and approval. CAISO's TPP-GIP integration initiative proposes to revise the CAISO tariff to implement a shift toward limiting ratepayer reimbursement to policy-driven transmission resources. The TPP-GIP integration reforms are scheduled to be voted on by the Board of Governors at the March 2012 meeting.

LEGISLATIVE HISTORY:

None.

FISCAL IMPACT:

Major. This bill requires the Commission to convene a proceeding by July 1, 2013 to develop rules for reimbursement of distribution grid upgrade costs to developers of certain distribution-interconnected generating facilities. As this bill will establish new Commission policy and require the creation of new rules to implement the policy, it will require an additional full-time Administrative Law Judge I and an additional full-time Public Utilities Regulatory Analyst IV for two years over and above existing staffing. This bill will also require continued staffing for follow-on proceedings. The present and future additional work duties are described below.

The complexity of implementing this bill within the already complicated interconnection and procurement programs would require:

- One full-time Energy Division Public Utilities Regulatory Analyst IV to assemble data, analyze implementation options, and develop a staff proposal, and
- One full-time Administrative Law Judge I to conduct a regulatory proceeding of this complexity.
- One quarter-time equivalent Public Utility Counsel III to handle potential litigation over questions of jurisdiction and/or federal preemption.

As the proceeding required by this bill would be a new dimension to existing interconnection and procurement programs, it represents an expansion of work duties requiring additional resources.

Years 1-2: Analytical, regulatory, and legal proceeding work duties associated with the complexity of implementing the proceeding required by this bill include:

- Establish a precise definition of the ambiguous terms in the bill as written, including "wholesale distribution generation facilities" and "constructed subsequent to the completion of interconnection studies."

- Handle litigation over questions of jurisdiction and/or federal preemption.

- Assemble and analyze data as the basis for a precise definition of "cost-effective."

- Establish the methodology by which the definition of cost-effectiveness is applied, including the timing, the entity responsible for making a determination, confidentiality rules, and other provisions.

- Establish the dispute resolution provisions that may be available to a developer denied access to ratepayer-funded distribution system upgrades based on a finding of "not cost-effective."

- Conduct procedural communications, consideration of party views and evidence, and writing of rulings and proposed decisions.

Year 3+: Analytical, regulatory, and legal proceeding work duties associated with follow-up proceedings:

- Assemble and analyze updates to distribution system upgrade cost data to keep the cost-effectiveness methodology up-to-date.

- Apply the cost-effectiveness determination within the scope of an ongoing proceeding.

- Litigate appeals when a developer seeking ratepayer reimbursement fails a cost-effectiveness test as determined by the Commission.

- Handle ongoing litigation over questions of jurisdiction and/or federal preemption.

- Conduct procedural communications, consideration of party views and evidence, and writing of rulings and proposed decisions.

Existing Energy Division public utilities regulatory analysts are engaged in implementing the Commission's procurement programs and present interconnection activities. This bill creates new policy and therefore work duties that are not similar to present existing work duties. To implement this bill without additional staff resources would require redirecting staffing resources away from pre-existing programs implementing present Commission policy.

Existing Administrative Law Judges are fully occupied with proceedings already underway. The introduction of a new proceeding will require additional administrative law judge resources not presently available to be redirected.

Existing Public Utilities Counsel resources are not presently engaged in litigation over the jurisdictional and/or federal preemption questions raised by the bill. To the extent this bill may lead to new litigation, it will require additional counsel resources not presently available to be redirected.

STATUS:

AB 2340 is pending hearing in the Assembly Utilities and Commerce Committee.

SUPPORT/OPPOSITION:

None on file.

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BILL LANGUAGE:

BILL NUMBER: AB 2340 INTRODUCED
BILL TEXT

INTRODUCED BY Assembly Member Williams
(Coauthor: Assembly Member Blumenfield)

FEBRUARY 24, 2012

An act to add Section 379.9 to the Public Utilities Code, relating to electricity distribution.

LEGISLATIVE COUNSEL'S DIGEST

AB 2340, as introduced, Williams. Distribution grid: distributed generation.

Under existing law, the Public Utilities Commission (PUC) has regulatory authority over public utilities, including electrical corporations, as defined. Existing law requires the PUC to administer, until January 1, 2016, a self-generation incentive program for distributed generation resources to facilitate the integration of those resources into the electrical grid, improve efficiency and reliability of the distribution and transmission system, and reduce emissions of greenhouse gases, peak demand, and ratepayer costs.

This bill would require the PUC to convene a proceeding on or before July 1, 2013, to develop rules, as prescribed, for the reimbursement of distribution grid upgrade costs to developers of wholesale distribution generation facilities constructed subsequent to the completion of interconnection studies. The bill would require those costs to be included in each electrical corporation's rate base.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. Section 379.9 is added to the Public Utilities Code, to read:

379.9. The commission shall convene a proceeding on or before July 1, 2013, to develop rules for the reimbursement of distribution grid upgrade costs to developers of wholesale distribution generation facilities constructed subsequent to the completion of interconnection studies. Those costs shall be included in each electrical corporation's rate base. The rules shall ensure that distribution grid upgrades are cost-effective for ratepayers. The commission, in developing the rules, shall consider federal rules under which transmission grid upgrade costs are reimbursed.