



On the radicality of New York's Reforming the Energy Vision



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ABSTRACT

In his article ‘The REVolution Yields to a More Familiar Path,’ Dr. Makhholm argues that the New York commission’s REV efforts are misguided because the traditional regulatory framework is efficient and well developed. Looking to the entire set of REV dockets, this article argues that the REV is attempting to overcome deeply entrenched incumbency advantages and is therefore both ‘radical’ and necessary to the successful transition to a clean, distributed energy infrastructure.

1. Introduction

In the words of its Public Service Commission, New York’s Reforming the Energy Vision (REV) aims to “enable the growth of a retail market and a modernized power system that is increasing clean, efficient, transactive and adaptable to integrating and optimizing resources in front of and behind the meter.”¹ The commission’s effort is attracting a lot of attention from both the trade press and interested parties,² and in his 2016 article on REV, Dr. Jeff D. Makhholm attempts to deflate some of this enthusiasm.³ He writes that REV’s “headline-grabbing rollout in 2014 of a ‘new regulatory model for the 21st century’ has yielded to a more traditional path for pursuing more efficient electricity distribution service in 2016.”⁴ He argues that the presently existing regulatory framework is sufficient to the task of regulating utilities and that more extensive (perhaps “radical”) reforms proposed under the REV are not needed. They are therefore misguided.

Dr. Makhholm seems to rely upon three main arguments. One argument is about the accounting method used to inventory a utility’s assets and determine its rate base.⁵ Since he dedicates the most space to this argument, it seems to be his primary one. His second and third

arguments are about the theoretical underpinnings motivating the REV reforms, the well-known capital expenditure bias and the information asymmetry.⁶ He believes that the traditional regulatory framework has recognized and adequately corrected for both of these so that the commission’s alleged foregrounding of them is naivety.⁷

In this response, I argue that the REV does represent radical reform, in the sense that the regulations break sharply from tradition, but for reasons other than those Dr. Makhholm thinks they do not. Of course, the chief concern is the successful transition to a clean energy economy, and whether REV is “radical” or “conservative” reform is of secondary importance. However, since hydrocarbon generation and infrastructure are deeply embedded in the presently existing regulatory framework, reforms as “radical” as REV are probably a necessary component of the transition.⁸

As prelude, the REV comprises about a dozen dockets, each with at least one major order and extensive utility regulatory filings under that order. These orders include: an order adopting a ratemaking and utility revenue model policy framework⁹; an order requiring utilities to develop a Distributed System Implementation Plan¹⁰; an order modifying the administration of utility low-income programs¹¹; an order adopting

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¹ (NYPSC, 2016g).

² Greentech Media has its own beat on REV. See, <https://www.greentechmedia.com/articles/tag/rev> (last visited April 11, 2017). The March 9, 2017, order on the Value of Distributed Energy Resources includes an Appendix summarizing the comments from 35 parties.

³ (Makhholm, 2016).

⁴ *Id.* at p. 55.

⁵ *Id.* at pp. 49–51.

⁶ *Id.* at pp. 52–53.

⁷ *Id.* at p. 55 (“REV raised conceptual economic problems (like information asymmetry and capital bias) that U.S. regulators had long ago recognized and tackled effectively enough to prevent them from being barriers to useful industry reform and the provision of efficient regulated services”).

⁸ See, (Astoria, 2017).

⁹ (NYPSC, 2016a).

¹⁰ (NYPSC, 2016f).

¹¹ (NYPSC, 2016h).

a clean energy standard¹²; an order establishing the requirements for community net metering¹³; an order establishing the requirements for community choice aggregation¹⁴; an order “resetting” the retail energy service provider market¹⁵; an order establishing a benefit cost analysis framework¹⁶; an order establishing a clean energy fund¹⁷; an order directing the development of a method for valuing distributed energy resources¹⁸; and an order authorizing utility administered energy efficiency portfolios.¹⁹ These dockets are highly integrated and should be taken together when evaluating REV.

2. Information asymmetry

Dr. Makhholm presents the commission as motivated by the well-known information asymmetry. He quotes three of the commission’s articulations on this asymmetry (all from the ratemaking docket) and also footnotes that the order mentions information asymmetry a dozen times.²⁰ “The problem with these statements,” he writes, “is that they treat regulation as a blank slate and ignore what U.S. regulators have done to address the problem.”²¹ The traditional solution to the information asymmetry, he notes, has been to “adopt methods to both heighten transparency and standardize the provision of publicly available and consistent financial and operating information for all regulated utilities” as well as to open the regulatory process to affected parties and judicial review under the Administrative Procedures Act.²² Since traditional ratemaking has long recognized and compensated for the information asymmetry, the commission’s foregrounding of it is out of touch with the effectiveness of the presently existing regulatory framework.

As traditionally formulated, the information asymmetry is the asymmetry in *financial* information *between* utilities and their regulators. However the commission might have stated the problem of information asymmetry at various places in the ratemaking order, a review of the other REV orders indicates that the traditional information asymmetry is not the asymmetry most concerning the commission. Rather, it is concerned about information about the flow of electrical power over the conductors, the condition of the substations, the timing and shape of the load curve, and other such data about the grid. In short, the commission is concerned about information about network or grid topology because it is necessary to develop distributed energy resource projects (DER). Further, the salient asymmetry is not the one between utilities and their regulators, but between the utility and the individuals, non-profits, and businesses wishing to develop DER projects.

The commission’s reconceptualization of the information asymmetry is evident in a large number of REV orders, and the Value of Distributed Energy Resources docket (VDER) provides a salient example.²³ The VDER docket aims to identify the various values which DERs provide to the grid. Some of these values are listed by the staff in its VDER report and include: distribution voltage support and ride-through; optimization of distribution operations; improvement of voltage quality and reduced system losses; deferred capacity upgrades; improved power system resiliency; participation in demand response programs; and reduced environmental impacts.²⁴ To identify and act

upon these values, DER providers must have access to information about grid topology.

For instance, DER can provide to the grid a demand reduction value (DRV) and a locational system relief value (LSRV). These values, however, depend upon the location of DER in the grid and the timing of their production. These values are both locationally and temporally dependent upon grid topology, but this information about grid topology was not at the time of the VDER order forthcoming from the utilities. While discussing DRV and LSRV, the commission writes, “[w]e are particularly concerned with utility efforts in this area. The utilities, in the first instance, have the most in-depth knowledge of their systems and have access to the planning and operation data necessary to perform such analysis. With unilateral access to the primary data and knowledge of the portions of their system where load relief would be more or less beneficial, they are gatekeepers of the information.”²⁵ The commission then takes seven pages to detail the numerous times it has required the utilities to provide such locational information and the various inadequacies of the utilities’ filings. It then orders a series of meeting and filing which will finally produce the needed information on grid topology.²⁶

In general, the information gap that must be bridged to facilitate the transition to DER is not between the utility and the regulator’s knowledge of its accounts, but between the utility’s knowledge about the grid and the individuals, communities, and businesses which desire to build distributed energy projects. Without it, non-utility entities (and their potential financiers) lack the information they need to build profitable distributed energy projects which optimize, rather than conflict with, the efficient and reliable operation of the grid. A utility’s hoarding of this information would be an insurmountable barrier to developing DER projects. The potential radicality of the REV, then, is not that it is trying to overcome the well-known information asymmetry, but its reconceptualization of that asymmetry from one about financial information to one about grid topology. The asymmetry concerning financial information takes place within the presently existing regulatory framework. The asymmetry regarding grid topology is necessary to overcome that framework and create a new one.

3. Capex bias and the *Hope* regulatory framework

In the United States, the system of utility accounting takes the utility’s depreciated capital expenditures as the “rate base” upon which capital’s constitutionally protected return on investment is calculated. This rather bizarre system of accounting is a *détente* arrived at during the first half the twentieth century between advocates of municipal ownership, capitalists, a managerial bureaucracy, and municipal and state governments. For instance, the 1907 bill which created New York’s first two utility commissions was a conservative reform championed by Governor Hughes and backed by then President Roosevelt. The misdeeds of the New York City utilities had created a socialist movement for municipal ownership which conservatives found unappealing. These Republican reformers aimed to tame the utilities enough to slacken this political movement.²⁷

That a utility’s capital expenditures should be identified as “public” and the foundation of the “rate base” was a four-decade process of legal politics.²⁸ As the railroads became politically and economically powerful, some states created railroad commissions charged with ensuring that rates were “just and reasonable.”²⁹ As the commissions promulgated rates, lawyers for the railroads challenged their constitutionality under the Fifth Amendment of the Constitution, which prohibits the

¹² (NYDPS, 2016i).

¹³ (NYPSC, 2015).

¹⁴ (NYPSC, 2016e).

¹⁵ (NYPSC, 2016d).

¹⁶ (NYDPS, 2016a).

¹⁷ (NYPSC, 2016b).

¹⁸ (NYPSC, 2017).

¹⁹ (NYPSC, 2016c).

²⁰ *REvolution Yields*, p. 52.

²¹ *Id.*

²² *Id.* p. 53.

²³ (NYPSC, 2017).

²⁴ (NYPSC Staff, 2016).

²⁵ (NYPSC, 2017) p. 112.

²⁶ *Id.* at p. 112–119

²⁷ (Sullivan, 1995). See esp., Chapter 12: The Triumph of Conservative Utility Reform, pp. 450–483.

²⁸ (Fried, 2001).

²⁹ Fried, at p. 305, fn 1.

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