VERMONT

DEPARTMENT OF PUBLIC SERVICE

MEMORANDUM

To:	**Vermont Public Utility Commission**
From:	**Ed McNamara, Director of Energy Policy and Planning**
Date:	**September 21, 2018**
Re:	**Case No. 17-5257-INV: Department comments in response to the Public Utility Commission's August 15, 2018 memorandum**

The Department of Public Service ("Department" or "PSD") appreciates the opportunity to provide comments to the Public Utility Commission ("PUC" or "Commission") addressing the following items as specified in the August 15, 2018 Memorandum: (1) any steps the Commission should take to improve the function of the standard-offer program; and (2) any recommendations the Commission should make to the Vermont General Assembly concerning the standard-offer program, including recommendations related to the exemption set forth at 30 V.S.A. § 8005a(k)(2)(B) and any issues arising from that exemption.

In general, the Department recommends phasing out the existing standard-offer program as soon as is practicable and enacting instead a requirement for an open and transparent utility procurement process that fits within the framework of the Renewable Energy Standard (RES). The Department recognizes that this would require legislative action; however, given the PUC's open-ended request for comments on the program, the Department believes that it is useful to put forward this proposal now. In addition, certain steps can also be taken to improve the function of the remaining standard-offer solicitation(s), which are also discussed below. Regarding the 30 V.S.A. § 8005a(k)(2)(B) exemption, the Department recommends ending the opportunity for

future exemptions from standard-offer obligations while grandfathering prior exemptions as long as renewability is demonstrated with the retirement of attributes.

I. STEPS THE COMMISSION SHOULD TAKE TO IMPROVE THE FUNCTION OF THE STANDARD-OFFER PROGRAM

Later in these comments, the Department recommends replacing the existing standard-offer program with a successor mechanism that would require utilities to conduct open and transparent procurements in the context of the RES and current and anticipated grid needs. The Department anticipates that such a transition would require some amount of time and that certain improvements could be made in that interim – however, there are very few that could be made without statutory change.

One potential change that could be made would be to require a refundable deposit for successful standard-offer bidders that is forfeited if a project withdraws prior to commissioning. VEPPI provided recommendations to this effect in Case Number 17-3935-INV; the PUC's March 16, 2018 order rejected this recommendation but stated that it "will revisit this issue before the 2019 RFP." The Department continues to support VEPPI's recommendations and recommends that the PUC implement these changes for the 2019 RFP. The Department includes VEPPI's October 20, 2017 comments as an attachment to this filing.

At the August 2, 2018 workshop, staff from the Lawrence Berkeley National Laboratory presented ideas regarding locational pricing. While the Department supports this concept it does not believe that the continuation of the standard-offer program in its current form is in the best interests of Vermont's ratepayers and instead inhibits progress toward the goals of the Comprehensive Energy Plan. Accordingly, the Department would not want to implement locational pricing for the standard-offer program at this point in time; instead, the locational

components could be integrated into the utilities' procurement under the program proposed by the Department or the concept could be further explored in the context of a future review of the net metering program.

II. RECOMMENDATIONS THE COMMISSION SHOULD MAKE TO THE VERMONT GENERAL ASSEMBLY CONCERNING THE STANDARD-OFFER PROGRAM

It would be prudent to undertake a review of any program reaching its 10-year anniversary; given the tectonic shifts in the electricity landscape in Vermont since that time and the administrative inefficiency associated with the standard offer program, it is timely to examine whether it is still able to adequately serve Vermont's energy policy goals.

In the nine years since the standard offer program was passed into law, sweeping changes have taken place in the electric sector. Cumulative capacity of net-metering applications grew from roughly 5 MW to close to 300 MW; standard-offer contracts grew from 0 to approximately 87 MW; Vermont's peak load has moved to after sunset for all months of the year; large areas of the state are either transmission- or distribution-constrained for additional generation; the region faces natural gas pipeline constraints resulting in higher fuel costs to gas-fired generators in the winter; and the variety and capabilities of various distributed energy resources have exploded (while their costs have simultaneously plummeted).

From a regulatory perspective, at the start of 2009, the only requirement related to renewable resources was the Sustainably Priced Energy Enterprise Development (SPEED) program, which required utilities to enter into long-term, stably priced contracts with renewable resources while allowing them to sell the RECs associated with those resources. In 2009, net-metering compensation was based on retail rates (most projects also received an up-front

capacity-based incentive from the Clean Energy Development Fund), and development was capped at 2% of utility peak demand in 1996. Today, there is no cap on the cumulative capacity of net-metering projects, and compensation is set using a complex process that attempts to set the appropriate pacing of new net-metered projects through compensation.

The standard-offer program aspect of the SPEED program was passed into law in 2009 and was designed to encourage the development of SPEED resources via a feed-in-tariff-like mechanism. Part of the underlying premise for the program in 2009 was the value that distributed generation brings to the distribution system. This point was explicitly made in Section 8005a(d)(2) which exempted from the statutory program cap those standard offer projects that "have sufficient benefits to the operation and management of the electric grid" and could "mitigate transmission and distribution constraints." As a result of aggressive energy efficiency and net-metering, load growth in Vermont is declining and distributed generation is, in some cases, imposing distribution costs rather than obviating the need for system upgrades. The location of utility-scale generation has operational and cost implications for the Vermont electric system; picking projects solely on price has the unintended and counter-intuitive consequence of actually increasing electricity costs. Given the importance of electrification in achieving the 90% renewable by 2050 goals contained in the Department's Comprehensive Plan, it is essential that the renewable generation requirements be met in as cost-effective a manner as possible.

A second area in which the standard offer program has also proven to have negative consequences is in the imposition of unnecessary costs associated with wheeling power from remote locations and out of the service territories of utilities that are hosting a disproportionate share of standard-offer generation. The PUC provided the following summary of the issue in Docket 8693:

> [T]he Standard-Offer program under 30 V.S.A. § 8005a has resulted in the development of much renewable generation. However, it has come to pass that many of the developed projects have not been sited near load, and that a disproportionately [sic] number of these projects are sited in the service territory of certain utilities (to date, GMP and VEC). In turn, this has resulted in higher costs to the interconnecting utilities and to the program as the power must be transmitted to load or must incur higher transmission costs because of the distribution of power to other utilities.[1]

The standard-offer program necessitates this wheeling because it involves a single, statewide entity to enter into contracts and assign the power and associated costs based on each utility's pro rata share of load. Based on information from the electric utilities, the wheeling costs to date total almost half a million dollars. Such costs from future standard offer projects would be obviated if the procurement was undertaken by the utilities rather than conducted through a state-wide process.

The standard-offer program is also administratively inefficient. The program requires the PUC, through VEPPI and with assistance from the Department, to establish avoided costs,[2] issue an RFP, make occasional changes to the generic power purchase agreement, and select winning bidders with whom to enter into contracts. This runs counter to the appropriate role of regulators – to provide oversight of the industry rather than make procurement decisions for the utilities.

The Renewable Energy Standard (RES) replaced the SPEED program and became effective in 2017. This has been an extremely significant regulatory change that has impacted the Vermont electricity industry. For the first time, utilities are required to retire Renewable Energy Credits (RECs) to demonstrate compliance, similar to every other renewable program in

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[1] Docket No. 8693, Order of 9/2/16 at 1.
[2] Note that the term "avoided costs" used in Section 8005a does not resemble how the term is used more generally in the industry.

the Northeast. Additionally, Tier II of the RES requires utilities to invest in distributed generation within Vermont, at a pace estimated to be 30 MW per year. And finally, Tier III of the RES changes the utilities' relationship with their customers – utilities are working more directly with customers to incentivize the transition to cleaner technologies in the heating and transportation sectors while more actively reviewing load management strategies.

While modifications within the purview of the Commission can be made to the existing program to improve its functioning, statutory changes would be required to truly begin to adapt the program to today's circumstances. Minor reforms do not get to the Department's root concerns with the standard-offer program – the lack of coordination with current statutory requirements and imposition of unnecessary costs. Effective reforms would require such fundamental changes to the structure of the standard-offer program that it would be more effective to instead terminate the existing standard-offer program and replace in wholesale fashion with a successor mechanism reflective of today's grid opportunities and challenges (which vary geographically across the state and by utility) as well as the current regulatory landscape (where the RES is the primary driver of the pace of distributed generation).

Successor Mechanism for a Transparent and Open Procurement Process

Any successor mechanism to the standard-offer program should retain the elements of the original program that have proven value. These include creating price transparency and benchmarking for renewable development in the state through the use of a market mechanism as well as enabling non-utility parties to participate in Vermont's renewable energy landscape via long-term financing mechanisms.

The goals codified in 30 V.S.A. § 8001 that provide high-level direction for the development and implementation of Vermont's renewable programs must also be factored into

any successor mechanism. These can be summarized as: 1) balance costs and benefits; 2) support the development of renewable energy along with its related economic development; 3) provide price stability; 4) develop markets for renewable and energy efficiency projects; 5) promote air and water quality; 6) contribute to reducing climate change and anticipating impacts to the state's economy that might be caused by federal regulation to attain those reductions; 7) support generation which is distributed throughout the grid; and 8) promote diverse technologies.

The Commission concluded in docket 18-0086-INV (biennial update of the net-metering program) that "the RES is the best standard for determining the amount of renewable energy necessary to meet state policy goals,"[3] and that up to 30 MW of new distributed generation resources will be needed annually to meet the current requirements of Tier II of the RES. Further, as the Commission stated in that docket,

> The Commission has been tasked with finding the balance between moving toward a carbon-free energy future, as outlined in the CEP and the RES, and doing so at a reasonable cost to ratepayers. . . . Thus, the question presented in this proceeding is not what economic incentives the Commission should set to promote the maximum amount of net-metering, but rather what incentives are necessary to meet the CEP and RES goals while protecting the interests of ratepayers.[4]

The challenge here, as in the net-metering biennial review, is fitting the net-metering, standard-offer, power purchase agreement, and utility-owned programs and options together neatly into Tier II while optimizing achievement of the other policy goals. Neither the existing net-metering framework (no explicit pacing guidance in statute) nor the standard-offer framework (very specific statutory pacing guidance) offer the utilities much flexibility or control

[3] Case No. 18-0086-INV, Order of 5/1/18 at 32.
[4] Case No. 18-0086-INV, Order of 5/1/18 at 31.

in design of their Tier II portfolios. The Commission has taken steps to bring net-metering compensation into alignment with its system values; a successor mechanism to the standard-offer program would endeavor the same: enabling distribution utilities greater flexibility in designing least-cost pathways to achieving their RES requirements while ensuring system benefits in the context of a rapidly changing electric sector and preserving the most successful and meaningful elements of the standard-offer program.

Below, the Department outlines some of the key elements it envisions in any successor mechanism to the standard-offer program.

PPAs would be between the electric utilities and individual renewable resources

Under this framework, distribution utilities would be responsible for issuing requests for proposals (RFPs), and would have the opportunity to collaborate with other utilities to issue joint RFPs. As utilities are in the best position to evaluate system needs and project impacts, the utilities would be responsible for selecting projects, with the oversight described below. Contracts, in the form of power purchase agreements (PPAs), would be made between individual utilities and projects, rather than the current standard-offer program paradigm under which the statewide facilitator enters into contracts with resources and allocates production and renewable energy credits from those projects to utilities on a pro rata basis. Using bilateral PPAs eliminates the unnecessary costs associated with wheeling and also allows utilities to procure resources specific to their system needs.

Individual project size would be dictated by the Tier II RES requirements – up to 5 MW – rather than the 2.2 MW limit set in the standard offer program. The amount procured would be a percentage of the Tier 2 RES requirements and would have to be procured from third parties through competitive solicitations. There would need to be further discussion regarding the

appropriate percentage to be procured, and should account for the fact that net metering resources are currently filling a significant percentage of some utilities' Tier 2 RES requirement.

Ensure Transparency, Accountability, Consistency, and Predictability

In the Department's proposed framework for a successor mechanism to the standard-offer program, statutory and/or regulatory guidance would be issued at the outset regarding a minimum set of common parameters for RFPs and contracts, including but not limited to contractual lengths (sufficient for project financing), minimum frequency of solicitations, and ability to solicit excess generation in advance of future years' obligations, eligible technologies, technology allocations, any exemptions for distribution utilities from various requirements related to size or other characteristics, etc. The Commission would exercise oversight over the content of RFPs prior to issuance, the selection of winning projects (for example, through a transparent mechanism that accounts for price and any other system benefits prioritized in the RFP), and the content of contracts. In addition, there would be a transparent review process associated with the resource selection process.

The Department recognizes that this would likely create additional, up-front work on the part of the utilities and there may be additional costs related to litigation in the first year or two of the process. However, given that this mechanism would last at least through 2032, these costs would be offset in the long run by the improved efficiencies. In addition, regular evaluation of the program's outcomes and effectiveness could be accomplished through existing statutory reporting obligations regarding the RES.

Ensure System Benefits, Policy Objectives, and Least-Cost Outcomes are Achieved

The RFP process and associated Commission review would allow utilities to consider and assign value to resource flexibility (i.e. valuation of production based on daily or seasonal

timing) as well as locational benefits (or costs) in their solicitations, along with emphasis on any other policy goals (such as prioritizing projects on preferred locations). This RFP process would provide utilities with sufficient flexibility to select specific types of resources that are best suited for their power supply and system needs – for example, a utility could prioritize a small wind resource with a different output profile than solar or the utility could select a solar project with associated storage. In addition, utilities should have flexibility within each RFP to describe available contractual options that bidders can propose as one element of the bid package.

Recommendations Related to the Exemption Set Forth at 30 V.S.A. 8005a(k)(2)(B)

Section 8005a(k)(2)(B) states:

> A retail electricity provider shall be exempt and wholly relieved from the requirements of this subdivision if, during the immediately preceding 12-month period ending October 31, the amount of renewable energy supplied to the provider by generation owned by or under contract to the provider, regardless of whether the provider owned the energy's environmental attributes, was not less than the amount of energy sold by the provider to its retail customers.

In 2017, the PUC approved exemptions pursuant to Section 8005a(k)(2)(B) for Swanton Electric Department and the City of Burlington Electric Department. In those orders, the PUC stated:

> We are concerned about the potential effects of recognizing this exemption, as well as any potential future exemptions for other Vermont electric distribution utilities that may similarly qualify under the statute. Each utility that qualifies for an exemption in a given year decreases the number of utilities, and therefore the number of ratepayers, among which to distribute a pro rata share of the costs of the standard-offer program. The result will place upward pressure on rates on a service-territory-specific basis with fewer ratepayers subsidizing the costs of this program. However, the statute grants a qualified utility this exemption. [5]

[5] Docket 8863, Order of 1/13/17 at 3.

On February 8, 2017, the PUC provided a letter to the Chairs of the Senate Natural Resources & Energy, Senate Finance, and House Energy and Technology Committees addressing the exemption and stated: "This exemption, although provided for by law, has policy implications that will increase the compliance costs of the standard-offer program for the remaining utilities and could, if expanded to other utilities; undermine the operation of the broader program."

Act 53 imposed a moratorium on new utilities receiving an exemption under Section 8005a(k)(2)(B) and also required:

> On or before December 15, 2018, the Public Utility Commission (Commission) shall submit a written report providing its recommendations related to the exemption set forth at 30 V.S.A. § 8005a(k)(2)(B) and any issues arising from that exemption, including the effect of the exemption on the State's achievement of the renewable energy goals set forth in 30 V.S.A. § 8001.

With respect to the effect of the exemption on Vermont's renewable energy goals, the primary negative impact is associated with goal 8001(a)(7): "Providing support and incentives to locate renewable energy plants of small and moderate size in a manner that is distributed across the State's electric grid . . . ." The exemption reduces the need for qualifying utilities to support distributed resources. However, the Department also notes that there are competing renewable goals that focus on affordability and it could be argued that the exemption appropriately supports the goal related to affordability.

As passed in Act 53 of 2017, only utilities that have previously qualified for an exemption can continue be exempt from the entire standard-offer program for 2018 and 2019; utilities that have not previously qualified for an exemption are not eligible in 2018 and 2019.

The Department views the future of exemptions for the remainder of the Program as having three possible outcomes:

1. Remove the moratorium and allow any utility, regardless of their exemption history, to apply;
2. Eliminate exemptions for all utilities, both historically and going forward; or
3. Implement a hybrid approach that would continue exemptions for previously exempt utilities on projects built in or before 2019, but not allow any exemptions on post-2019 projects to any utility.

The Department recommends moving forward with the hybrid approach. As the PUC noted in its letter to the legislature, the continuation of exemptions from any utility is not a sustainable path, as it is conceivable for all utilities to be eligible for exemption in which case there would be no offtakers of the power and the contracts could go into default. Conversely, to entirely eliminate exemptions for all utilities would put too much regulatory uncertainty on the previously exempt utilities. Those utilities have made power supply decisions based on an assumption that they would continue to be exempt; while rules can always change, there are equity issues associated with changing utilities' allocation of power from existing standard-offer projects. The Department believes that middle-ground can be achieved with a hybrid approach.

One of the primary goals of the statue was to stimulate economic development of small in-state renewables by offering long-term fixed price contracts, and in effect requiring the utilities to support renewable development. While utilities that have previously been exempt may have made significant efforts to source their energy from renewable generation (which includes large out-of-state generators that may not include the renewable attributes), this should not entirely relieve them of their obligation to support small in-state development. Utilities that have

previously qualified for an exemption, and continue to meet the requirements, should be grandfathered and continue to receive an exemption on all projects built prior to 2020. Exemptions on new projects should cease in 2020, but previously exempt utilities that continue to meet the exemption criterion should not be allocated a share of pre-2020 standard-offer projects.

However, the Department also recommends that the exemption requirements be adjusted to reflect the new regulatory paradigm such that grandfathered utilities can only continue to be exempt if these new requirements are met. Exemption requests currently do not require the retirement of RECs, but instead a utility is exempt "if, during the immediately preceding 12-month period ending October 31, the amount of renewable energy supplied to the provider by generation owned by or under contract to the provider, regardless of whether the provider owned the energy's environmental attributes, was not less than the amount of energy sold by the provider to its retail customers." (30 V.S.A. §8005a(k)(2)(B)) In other words, a utility can sell the RECs associated with the renewable energy used to achieve exemption, and at the end of the year, the utility cannot make any claims of renewability. With the Renewable Energy Standard and the associated requirement for annual compliance filings, it follows that utilities should be required to demonstrate 100% renewability for standard-offer exemption with the retirement of RECs in NEPOOL GIS.

Conclusion

The Department appreciates the opportunity to comment in this docket, and looks forward to reviewing comments filed by other stakeholders.

Attachment list

Attachment A – VEPP Inc.'s comments of Oct. 20, 2017 in Case 17-3935-INV