New York regulators take next step—Perry Sioshansi's Letter from America

Reforming the Energy Vision is gradually taking shape

Regulators at the New York Public Service Commission (NYPSC) launched the basic outline of an ambitious new regulatory framework called Reforming the Energy Vision (REV) following the devastation of superstorm Sandy. In mid-May 2016, they issued a new Order *Adopting a Ratemaking and Utility Revenue Model Policy Framework*, the details of which may be found at the NYPSC website.

The latest order addresses what steps are needed to align:

- the regulated distribution utility's business model and revenue streams in view of the rapidly changing competitive environment; and
- the rates that customers should pay for services derived in view of the evolving competitive forces, new offerings, new service needs and Commission's own policy goals.

REV, which was launched two years ago under the leadership of NYPSC chair, Audrey Zibelman, seeks to chart a new path for the regulation of New York's electric utilities, who like their counterparts everywhere, are entering new and uncharted territory.

As stated in NYPSC's original order:

"The confluence of cost, reliability, and environmental concerns […] lead to a conclusion that conventional utility and regulatory practices no longer represent the best approach to satisfying our responsibilities."

With this as the context, the NYPSC embarked on new approaches to regulating, especially the critical utility-owned monopoly distribution network. Among the REV's objectives were to facilitate the incorporation of distributed energy resources (DERs) in the distribution network.

In its major new order in early 2015, the NYPSC adopted a regulatory policy framework that described the need to reform the utility business model and to align ratemaking practices with evolving policy objectives. The centre-piece of the order was the establishment of a distributed system platform (DSP) structure by which:

- utilities will facilitate the growth of DERs;
- limited utility ownership of distributed resources to mitigate market-power concerns;
- required utilities to create distributed system implementation plans (DSIPs) outlining relevant system information and investment plans; and
- established interim energy efficiency targets.

The latest order represents the next step toward implementation of that vision. Needless to say, regulators across the US and beyond are examining NY's REV for useful insights to apply in their own jurisdictions, as appropriate.

By way of background, distribution utilities in the US – many of whom are still vertically integrated – tend to operate under so-called rate of return regulations. Basically, they are allowed to recover their costs through a reasonable return on the invested capital. In practice regulators periodically adjust customer tariffs so that regulated utilities can cover costs.

Whilst the simple mechanism worked reasonably well in the past, it has become apparent that it will no longer work in an environment when demand may be flat or falling due to energy efficiency, distributed generation and a host of new products and services including energy storage and peer-to-peer trading are being offered.

Moreover, NYPSC, like regulators elsewhere must increasingly recognise that many assumptions about the nature of business are no longer applicable in whole or part including the fact that:

- customer demand is largely outside the influence of the utility;
- economies of scale favour utility-scale investments;

- large expenditures to create redundancies are necessary to support reliability; and
- end-use customers are the only substantial source from which system costs – most critically the fixed costs of critical distribution networks – can be recovered.

By rejecting these outdated assumptions, NYPSC plans to begin to realign the revenue model of New York's utilities with desired outcomes. The Commission recognises that survival of the distribution utilities is critical to its vision of proactive customers in a changing business environment.

Mindful that a lot is at stake, the latest order proposes a gradual transition path with the following four main components:

- revenues tied to performance – The Commission has proposed establishing a new Earnings Adjustment Mechanism (EAM), New York's version of performance-based incentives, to better align utility financial incentives with priority near-term outcomes: system efficiency, energy efficiency, improved data access, and interconnection;
- new source of revenues – The Commission Platform Service Revenues (PSRs) by which utilities can earn revenues from operating and facilitating distribution-level markets;
- more granular rates – The Commission is intent to transition customers in New York toward more granular rates including time-based pricing options; and
- sharing customer data with DER providers – The Commission wants DER providers to have better access to customer data, with permission from the customers, of course.

Few would argue with the Commission's intent or its motivations. Yet the end result remains a rather complicated mix of the old style regulation plus new requirements to allow new services and service providers to find a footing on the grid's edge. For example, NYPSC has proposed the establishment of a scorecard tracking at least 10 measures of utility performance – consistent with REV's desired outcomes. Things get complicated in practice as the text below suggests:

In the near term, as the DSP market is being established, PSRs may come primarily from the utility's ability to develop non-wires alternatives to traditional infrastructure investments, but over time PSRs may be available. The NYPSC makes clear that PSRs are available to monopoly-related services, and may be approved by the PSC "in limited areas of competitive services" as stipulated by specific criteria in the Order.

Observing the merits of REV and NYPSC's objectives, the Rocky Mountain Institute, in an article in RMI Outlet dated 20 May 2016, wrote: "The NYPSC's recent order represents a major step forward in realizing the future of New York's electricity system. While New York is a national leader in comprehensive regulatory reform, many states are tackling similar questions at varying levels of scope and scale. The latest development in New York's REV proceeding provides insights for regulators, utilities, and stakeholders in states and localities that are facing similar challenges and opportunities in today's quickly evolving electricity system."

It remains to be seen how the proposed changes will be implemented in practice and whether they will lead to the intended outcomes. The key question in the face of rapid technological change is indeed how to regulate the emerging digital economy, if at all. While the case of Uber may seem obvious, the logic and types of regulations applied to regulated distribution utilities is much more convoluted and far less clear. For those looking for clarity or simplicity, the REV may prove disappointing.

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