

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Smart Grid Policy

Docket No. PL09-4-000

**SUPPLEMENTAL COMMENTS OF THE
ELECTRICITY CONSUMERS RESOURCE COUNCIL
("ELCON")**

The Electricity Consumers Resource Council ("ELCON") offers the following comments on FERC's May 19, 2009 Notice Requesting Supplemental Comments respecting the Proposed Policy Statement and Action Plan (the "Proposed Policy Statement") on the development of a national Smart Grid.¹ FERC now seeks input regarding rate recovery for smart grid investments in light of the announcement of two Smart Grid funding opportunities by the U.S. Department of Energy ("DOE") that may supply up to 50 percent of the funding for certain Smart Grid projects.

FERC must tread carefully here. Although DOE funding should be pursued to the fullest extent possible, nothing should distract FERC from its statutory obligation to ensure that utility investments are prudently incurred and have a net benefit to ratepayers. If implemented subject to thorough oversight, a two stage process consisting of conditional FERC approval – where the utility meets a burden of establishing that the proposed Smart Grid investment satisfies stringent criteria relating to the efficacy of the technology – followed by a FERC prudence review may represent the best compromise between competing considerations. This special procedure should be utilized only to the extent that it is essential to receive DOE funding – *i.e.*, where DOE funding is being sought and DOE has confirmed that a favorable FERC ruling is necessary to the

¹ 74 Fed. Reg. 23810 (May 21, 2009) ("Supplemental Notice").

release of funds – and would require careful regulatory oversight to protect against imprudent investment and abuse.

COMMENTS

In its initial comments in this docket, ELCON emphasized its support of FERC’s efforts to promote the development and, ultimately, implementation of Smart Grid technologies, which will, among other benefits, serve to enhance opportunities for demand response. At the same time, ELCON opposed FERC’s proposed Interim Rate Policy that would offer special incentive and expedited rate treatment to Smart Grid investments. In ELCON’s view, resolution of the major cybersecurity, connectivity and other technical hurdles to Smart Grid deployment and the implementation of final standards are prerequisites to any determination that Smart Grid investments are prudently incurred.

The current opportunities for DOE funding have added a further layer of complexity. It is in the interest of all parties to ensure that such funding is pursued to the fullest extent possible. But such funding will still leave ratepayers footing 50 percent or more of the cost of Smart Grid projects. In the request for supplemental comments, FERC further notes that the DOE funding documents issued under Section 1304 “instruct applications to . . . identif[y] all sources of project funds” and that the documents issued under Section 1306 “could be read as indicating a preference for [regulatory] approval.”² These conclusions are far from definitive. Nonetheless, ELCON agrees that FERC should take any necessary action to preserve opportunities for potential DOE funding, provided that it can do so in a fashion that fully preserves its Federal Power Act responsibilities, which must remain the prime consideration.

² Supplemental Notice at ¶¶ 5, 6.

In this regard, ELCON reiterates the opposition expressed in our initial comments to the Proposed Interim Rate Policy and our view that the special rate treatment that FERC proposed for Smart Grid investments would be contrary to the Federal Power Act. As ELCON stated previously, at this early juncture in the development of Smart Grid technologies, it would be premature to establish special incentives for Smart Grid investments before the substantial and complex technical issues have been resolved and comprehensive unified standards have been developed. When the time comes for substantial Smart Grid investments, rate recovery should be based on standard ratemaking procedures. Indeed, based on longstanding practice, the burden lies with FERC to explain why it is necessary to take the unorthodox step of authorizing single-issue ratemaking and special rate incentives. Prior experience indicates that these practices will lead to wasteful and unnecessary investment to the detriment of ratepayers.

In view of the current status of the DOE grant program, ELCON offers a path forward that could preserve the DOE funding opportunities while avoid special incentive ratemaking that would be inconsistent with the Federal Power Act. The following two-stage procedure should be utilized only to the extent that it is essential to receive DOE funding – *i.e.*, where DOE funding is being sought and DOE has confirmed that a favorable FERC ruling is necessary to the release of funds – and would require careful regulatory oversight to protect against imprudent investment and abuse. For example, it should not be applied to any Smart Grid investments ineligible for DOE matching funds; in that case, for the reasons stated in ELCON’s initial comments in this docket, normal rate-making procedures should apply.

Stage One: Conditional Review and Approval, Applying Stringent Smart Grid Criteria

First, FERC could establish specific, stringent criteria by which Smart Grid investments subject to DOE funding could be *conditionally* approved. Such criteria should establish

safeguards to ensure that any such Smart Grid investments have a net benefit to consumers.

As a key threshold criterion, cost recovery should only be considered if the investment meets all interoperability protocols and model standards that have been approved for the investment's functionality. DOE has proposed to make this a requirement of funding:

After the development and publication by the Institute of protocols and model standards for interoperability of smart grid devices and technologies, an investment that fails to incorporate any of such protocols or model standards [will not receive grants].³

As noted above, the FERC policy should not go beyond what is needed for DOE approval. When standards for a certain class of technologies are developed and published by NIST, Smart Grid devices and equipment that do not conform to NIST's standards should lose their interim approval status, if previously granted.

In terms of additional criteria that the utility must satisfy in order to obtain interim FERC approval, the Proposed Policy Statement provides a useful starting point:

1. Absence of adverse effect on “the reliability and security of the bulk-power system . . . by the deployment at issue,” requiring showings relating to:
 - “maintain[ing] compliance with Commission-approved reliability standards, such as the Critical Infrastructure Protection Reliability Standards, during and after the installation and activation of Smart Grid technologies so the reliability and security of the bulk-power system will not be jeopardized;”
 - “the integrity of data communicated (whether the data is correct);
 - “the authentication of the communications (whether the communication is between the intended Smart Grid device and an authorized device or person);”
 - “the prevention of unauthorized modifications to Smart Grid devices and the logging of all modifications made;”
 - “the physical protection of Smart Grid devices;” and

³ *Notice of Intent to Issue a Funding Opportunity Announcement For the Smart Grid Investment Grant Program*, Department of Energy, issued April 16, 2009, at p. 7.

- “the potential impact of unauthorized use of these Smart Grid devices on the bulk-power system.”
2. Minimization of “the possibility of stranded investment in Smart Grid equipment by designing for the ability to be upgraded,” looking to:
- “adher[ance] to the vision of a Smart Grid described in Title XIII of the EISA, including optimizing asset utilization and operating efficiency;”
 - “adher[ance] to the principles of the Gridwise Architecture Council Decision-Maker’s Interoperability Checklist;”
 - “reliance to the greatest extent practical on existing, widely adopted and open interoperability standards;” and
 - “where feasible, reliance on systems and firmware that can be securely upgraded readily and quickly.”
3. Sharing of “information with the Department of Energy Smart Grid Clearinghouse, provided for in the ARRA,” including:
- “any internal or third party evaluations, ratings, and/or reviews including all primary source material used in the evaluation;”
 - “detailed data and documentation explaining any improvement in the accurate measurement of demand response resources;”
 - “detailed data and documentation explaining the expansion of the quantity of demand response resources that resulted from the project and the resulting economic effects;
 - “detailed data and documentation for any improvements in the ability to integrate variable renewable generation resources;
 - “detailed data and documentation that shows any achievement of greater system efficiency through a reduction of transmission congestion and loop flow;
 - “detailed data and documentation showing how the information infrastructure supports DER such as plug-in electric vehicles; and
 - “detailed data and documentation that shows how the project resulted in enhanced utilization of energy storage.”⁴

⁴ Proposed Policy Statement at ¶¶ 47-50.

ELCON submits that these are the minimum criteria that should be applied for conditional approval of DOE funded Smart Grid investments and that utilities should bear the burden of making detailed showings respecting each of the criteria before conditional approval of a Smart Grid investment. FERC will then be in a position to make a threshold, interim finding that such investments have the potential to be prudently incurred, used and useful to customers, and of net benefit to ratepayers.

Stage Two: Prudence Review

Second, as a *quid pro quo* for such interim approval, any DOE funded Smart Grid investment conditionally approved subsequently should be subject to prudence review. Review of the prudence of incurred costs has long been included in the Commission's regulatory toolbox. As FERC has previously stated:

The Supreme Court of the United States early recognized that the determination of what is just compensation for a public utility involves consideration of the utility's conduct in incurring its costs.

...

...[W]e reiterate that managers of a utility have broad discretion in conducting their business affairs and in incurring costs necessary to provide services to their customers. In performing our duty to determine the prudence of specific costs, the appropriate test to be used is whether they are costs which a reasonable utility management (or that of another jurisdictional entity) would have made, in good faith, under the same circumstances, and at the relevant point in time. We note that while in hindsight it may be clear that a management decision was wrong, our task is to review the prudence of the utility's actions and the costs resulting therefrom based on the particular circumstances existing either at the time the challenged costs were actually incurred, or at the time the utility became committed to incur those expenses.⁵

Although the prudence analysis must evaluate a utility's decision on the basis of information available to the utility at the time when the costs are incurred, the utility has not reached that

⁵ *New England Power Company*, Opinion 231, 31 FERC ¶61,047, at 61,081-61,084 (1985).

stage when it applies for DOE funding. As the D.C. Circuit held in *City of New Orleans v. FERC*, FERC is entitled to defer its prudence review until “the rate-altering event occurs.”⁶ The risk that the utility bears “[u]ntil the final prudence determination is made . . . must be accepted as a tolerable incident of utility regulation.”⁷

As ELCON explained in detail in our initial comments, the concept of, regulation of, and technology for the Smart Grid are evolving rapidly. Prudence review, as proposed by ELCON, would permit FERC to take into account the state of Smart Grid technology and standards at the time the costs are incurred, thus ensuring that investments will result in a net benefit to consumers.

CONCLUSION

DOE funding of Smart Grid technology should be encouraged, but should not distract from full compliance with the Federal Power Act’s standards for rate recovery. Conditional FERC approval, where the utility meets a burden of establishing that the proposed Smart Grid investment satisfies stringent criteria relating to the efficacy of the technology, followed by a FERC prudence review, represents a reasonable compromise. If carefully implemented, such a two-stage process could enhance opportunities for access to DOE funding while providing adequate assurance that such Smart Grid investments are prudently incurred, are used and useful to customers, and have a net benefit to ratepayers. ELCON emphasizes, however, that this special procedure should be utilized only to the extent that it is essential to receive DOE funding – *i.e.*, where DOE funding is being sought and DOE has confirmed that a favorable FERC ruling is necessary to the release of funds – and would require careful regulatory oversight to protect against imprudent investment and abuse.

⁶ *City of New Orleans v. FERC*, 67 F.3d 947 (1995).

⁷ *Id.*

NOTICES AND COMMUNICATIONS

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Dated: June 2, 2009

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon each person designated on the official service list compiled by the Secretary of this proceeding.

Dated at Washington, D.C.: June 2, 2009

/s/ W. RICHARD BIDSTRUP
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