BEFORE THE
STATE OF NEW YORK PUBLIC SERVICE COMMISSION

Proceeding on Motion of the Commission in Regard to Reforming the Energy Vision	**:** **:** **:** **:**	**Case No. 14-M-0101**

RATEMAKING AND UTILITY BUSINESS MODEL
COMMENTS OF THE EXELON COMPANIES

In response to the State of New York Public Service Commission ("Commission") July 28, 2015 *Notice Inviting Public Comment on Staff White Paper on Ratemaking and Utility Business Models*,[1] as issued in the above-docketed proceeding, Exelon Corporation – including its subsidiaries Constellation NewEnergy, Inc. ("CNE"), Exelon Microgrid, LLC, Constellation Energy Nuclear Group, LLC, Nine Mile Point Nuclear Station, LLC, R.E. Ginna Nuclear Power Plant, LLC, Exelon Generation Company, LLC, Baltimore Gas and Electric Company ("BGE"), Commonwealth Edison Company ("ComEd") and PECO Energy Company ("PECO") (collectively, "Exelon") – hereby submits its Comments.

INTRODUCTION

In its July 28, 2015, White Paper on Ratemaking and Utility Business Models, Staff recommends transformational reforms of utility rates and the ratemaking process. These recommendations include how utilities may recover their costs of service in furtherance of the Commission's vision for the future of the electric industry as part of the Reforming the Energy Vision ("REV") initiative.[2] This White Paper is a necessary, highly-anticipated next step in the

[1] *Proceeding on Motion of the Commission in Regard to Reforming the Energy Vision*, Case No. 14-M-0101, *Notice Inviting Public Comment on Staff White Paper on Ratemaking and Utility Business Models* (July 28, 2015).

[2] *Staff White Paper on Ratemaking and Utility Business Models*, Case No. 14-M-0101 (July 28, 2015) ("Ratemaking White Paper" or "White Paper").

REV process. Exelon looks forward to working with other stakeholders to ensure that this next phase results in achievable and sustainable reforms to utility business models, rate designs, and the ratemaking process that support the stated REV objectives, and are consistent with the Commission's and Exelon's REV principles.

As with Exelon's previous comments in the REV proceeding, the purpose of these Comments is to offer selective, constructive suggestions in response to the Ratemaking White Paper from the comparatively unique and balanced perspective of a stakeholder with extensive experience. Exelon operates utilities delivering electricity and natural gas to more than 7.8 million customers in central Maryland (BGE), northern Illinois (ComEd) and southeastern Pennsylvania (PECO), as well as participates in competitive retail and wholesale markets in 48 states, the District of Columbia and Canada. In addition, Exelon operates the nation's largest clean energy generation fleet, including 2,400 MW of zero carbon emitting base-load generation in New York. Exelon intends to remain engaged in the multiple, continuing REV workstreams, and provide additional comments on related issues, including process, incentives, rules, tariffs, and the New York utilities' Distributed System Implementation Plans ("DSIPs") to be submitted to the Commission in June of 2016.

COMMENTS

I. Introduction and Summary

A. Principles and Framework

The proposals contained in the Ratemaking White Paper reflect several foundational principles, as articulated by Staff and summarized below:

1. **Align earning opportunities with customer value** – changes to the regulatory paradigm must create the right incentives and opportunities for utilities to earn on activities that facilitate REV goals, including expansion of DER and third-party investment, and reduce overall customer bills.
2. **Maintain flexibility** – regulation should remain flexible enough to promote demonstration and other projects that enable adaptation as the market develops.
3. **Provide accurate and appropriate value signals** – rate design and value signals should provide the market and customers both the information and compensation necessary to support anticipated market activity and customer interest.
4. **Maintain a sound electric industry** – an operationally and financially sound electric industry requires forward-looking changes be grounded in the present and governed by the principle of gradualism.
5. **Shift balance of regulatory incentives to market incentives** – regulatory incentives should remain in place as long as they are needed and effective, although over time those incentives may be complemented by more valuable and efficient market-driven financial benefits.
6. **Achieve public policy objectives** – while the ratemaking principles and changes proposed in REV are reflective of the underlying public policy objectives, there remains an essential need for reliable, resilient, affordable, and clean energy service.[3]

Because of our common commitment to customer value, efficiency, and unbiased and objective evaluation of alternatives, many of the principles Staff identifies are consistent with Exelon's previously articulated REV principles:

REV Overarching Principles

- **GHG Alignment.** All REV activity must align with New York State and federal CO_2 and other GHG climate initiatives.
- **Reliability Standards.** All applicable New York State, regional and federal reliability requirements must be maintained.
- **Cost/Benefit.** A cost/benefit analysis should be completed for any proposed changes. This includes the overall costs/benefits for consumers and society; for REV Platform technology; and to evaluate DER investment versus traditional utility investment for individual project applications.
- **Generation Attributes.** Attributes monetized at the distribution level should receive similar consideration at the bulk power system level, and vice versa.

[3] *Id*., at 7-8.

- **Realistic & Reasoned Implementation Timetable.** The timetable should incorporate winter 2013/14 lessons learned and a longer-term transition to dynamic load management.

Wholesale Market Guiding Principles

- **Market Model Coordination.** The functioning of the Distributed System Platform ("DSP") provider should align with the NYISO wholesale market model.[4]

- **Clean Energy Base-Load Support**. Clean energy base-load resources are needed for long term reliability and environmental compliance, and must have the ability to realize adequate revenue recovery.

EDC Guiding Principles

- **Utility Role.** The EDC should fulfill the role of DSP provider.

- **Revenue Adequacy.** The EDC must have the ability to earn a fair return, maintain adequate cash flow, and secure long-term financial health.

- **Value of the Grid.** All users of the grid should pay their fair share.

- **Management Flexibility and Dynamic Efficiency.** The final model adopted must allow EDC management the ability to adjust to changing circumstances; support and encourage innovation; allow timely implementation of technological advances; promote continuous efficiency improvement; and support long-term value for customers.

- **Opportunities for Additional Revenue.** Where appropriate, EDCs must be provided opportunities to enhance revenue from bi-directional performance incentives or provision of adjacent services (services that the EDC is well positioned to provide and that are potentially competitive). These services include DER ownership under certain conditions.

Competitive Customer Choice Guiding Principles

- **Maintain and Protect Competitive Retail Model.** In any redesigned REV market, competitive customer choice must be maintained, and the market structure must support the ability to offer competitive services, including DER.

- **Protect Competitive Retail Model and ESCO Customer Engagement.** The REV must ensure that growth of competition is protected and not hindered by directly or

[4] The efficient wholesale market has brought billions of dollars of benefits to New York and the region and the future DSP and wholesale market structures should build on that synergistically. *See*, *Benefit-Cost Analysis Comments of the Exelon Companies*, Case No. 14-M-0101 (filed Aug. 21, 2015), at 4.

indirectly encouraging the perception that the EDC is the only "electric company," particularly in the eyes of residential and small C&I customers.

- **Customer Data.** Effective customer choice and product innovation requires accurate and timely data for appropriately licensed and authorized market participants.

In particular, Exelon's EDC Guiding Principles complement Staff's principles insofar as they both support the notion that whatever the business model, there are fundamental utility responsibilities that must continue to exist, including the operation of the grid in a reliable, resilient, safe, and affordable manner. Both Staff and Exelon, through these principles, build upon and enhance what can be offered beyond that essential baseline. Just as REV itself is premised on maintaining the grid as the necessary "platform" for innovation, Exelon emphasizes that the grid reforms must continue to complement and work within the existing larger, well-functioning competitive market structures, such as the Regional Greenhouse Gas Initiative ("RGGI") and New York State Independent System Operator ("NYISO") that send appropriate price signals to market participants and maintain reasonable rates for customers.

Additionally, both Staff's and Exelon's principles focus on activities and business models that encourage innovation and create value that is equitably distributed to customers. Exelon supports Staff's goal of aligning financial incentives and economic signals with REV objectives. Exelon also supports the development of innovative and cost-effective market solutions, with utilities facilitating those markets both in their system planning and in day-to-day operations. If the correct structures and price signals are in place to objectively incentivize achieving that value in a fair, accurate, unbiased, and transparent manner, then utilities and other market participants can be guided to the correct investment decisions and best solutions without sacrificing system reliability, since any analysis should fairly account for the use of and reliance of the grid by all market participants.

Exelon concurs with Staff's principle that all REV activity must align with public policy demands, and calls attention in particular to federal CO_2, regional, New York State, and other GHG climate initiatives and the values recognized by them.[5] As discussed later in these Comments, the Carbon Free Acquisition Rate ("CFAR") proposed in the White Paper is one method to account for the role carbon-free sources of generation play in maintaining these climate initiatives going forward. Regardless of the particular methods for evaluation, the ratemaking initiatives undertaken in this proceeding must recognize the continued need for clean base-load energy resources to ensure long-term reliability and environmental compliance. Thus, New York needs to maintain existing zero carbon emitting resources, allow for as needed economic growth of low-carbon resources, and protect against delivery-level reforms that undercut or distort the market's ability to provide sufficient clean energy resources for New York consumers.[6] As stated in Exelon's comments in the Large Scale Renewable ("LSR") docket, this Commission should expand this proceeding, or open a new proceeding, to holistically consider broad structural reforms to accomplish the State's clean energy goals.[7]

Exelon further agrees that any ratemaking changes must be consistent with the other important REV initiatives, including the development of a rigorous and unbiased benefit-cost

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5 *Id*., at 8; *see also*, *Benefit-Cost Analysis Comments of the Exelon Companies*, at 17-18.

6 Market structures must balance the value of existing zero carbon emitting resources critical to New York's ability to meet its self-established carbon reduction goals with the value of expanded DER. *See*, Magnarelli, Tom, *Given New Carbon Emissions Rules, Katko Says New York Can't Afford To Lose FitzPatrick Nuclear*, WSKG News, October 7, 2015, at http://wskgnews.org/post/given-new-carbon-emissions-rules-katko-says-new-york-cant-afford-lose-fitzpatrick-nuclear#stream/0 ("With the new laws that are out there with carbon emissions and new federal standards, they [NY State] need clean energy big time," Katko said. "... if they [NY State] lose any more of the nuclear power plants in New York state, there's no way possible that they [NY State] can comply with the carbon emissions standards." Rep. John Katko (R-NY)).

7 Policies, such as a Clean Energy Standard, are necessary in order to maintain the existing zero carbon generation fleet that will avoid over-dependence on emitting fossil fuel generation to the detriment of the State's climate initiatives. Continued operation of both legacy renewable generation assets and zero carbon emitting nuclear and hydro power plants is indispensable to New York State's ability to meet its approved Energy Plan and forthcoming Clean Air Act Section 111(d) compliance plan.

analysis ("BCA") framework and an approach to calculating the full value of distributed energy resources ("DER") and the net benefits to society.[8] These ongoing climate and REV initiatives are critical to the effort of establishing the proper price signals for market participants. Multiple, disparate approaches and values will frustrate the efficient achievement of the goals of REV, climate, and other initiatives.

The financial health of utilities is equally necessary to meet the goals of REV. Utilities rely on the regulatory compact; the provision of reliable service to all customers in exchange for the opportunity to earn a fair return on their investment. Without the ability of utilities to earn a fair return, maintain adequate cash flow, and secure long-term financial health, reliability and the essential functions utilities perform will suffer. The ability of utilities to take action or provide services is dependent on appropriate cost recovery. Staff's proposed business model and rate design reforms should be viewed as an optimization, and not an abrogation, of this basic regulatory compact.

Finally, Exelon appreciates Staff's recognition of how the complexities of REV generally, and of ratemaking in particular, affect the timing of reforms.[9] The practical realities of the pace of change, accounting for the operational complexity of the grid, the complexity involved in changes to ratemaking and business models, and lessons learned from events such as the winter of 2013/14 necessitate a realistic and reasoned implementation timetable. Exelon therefore agrees with Staff that "the critical task is to incentivize the near-term activities that will

[8] *Id*., at 5.

[9] *Id*., at 3-4.

promote the development of full-scale markets," while adhering to the principle of "gradualism."[10]

B. Utility Business Model Reforms

New York policymakers, through REV, articulate the imperatives for changes proposed to the State's electric utility industry; changes that will have rate design and operations (customer and grid) implications for the distribution utility business model. In fact, the utility business model is already changing in response to, and in anticipation of, a variety of factors including, but not limited to, flat-to-declining load growth, increasing deployment of DER (with corresponding implications for system infrastructure, load, rate structures, and cost-shifting among customers), growing demands by customers for dynamic rates and real time energy management, more stringent environmental mandates, cyber and physical security concerns, and more volatile weather conditions. Utilities must navigate this dynamic environment while still balancing adequate levels of investment in existing zero carbon emitting central station infrastructure with prioritizing investments for reliability and power quality, and considering impacts on customer affordability. REV thus requires a new paradigm for regulatory, business, and operating models, and the way utilities interface with customers.

Utilities will continue to build, maintain, and operate the grid to provide reliability, security and resiliency at reasonable cost. Simultaneously utilities are investing in foundational automation technologies to evolve to a new system where efficiencies derived from the grid can accommodate existing and new clean energy, central station and DER, and other value-added products and services. In addition to their roles as DSP providers, utilities are participating in deployment of DER to complement zero carbon emitting central-station resources and promote

[10] *Id.*, at 8, 11.

greater system efficiency and exploring other ways to increase customer value subject to continued cost recovery and long-term viability. As DSPs, utilities are expected to use their infrastructure to deliver energy to customers, maintaining affordable, universal service, and leverage enhanced technology to ensure grid reliability and resilience. Utilities will also increasingly leverage their core competencies and expertise to play a role in operating and participating in an integrated grid where choices for central and distributed generation and services expand to better serve the customer.

As part of REV, the Commission aims to change regulatory and market designs and incentive structures to align utility interests with the Commission's policy objectives. As a consequence, ratemaking in New York is expected to incrementally shift from a principally cost-of-service to an increasingly performance-based regulatory model as the utilities assume broader roles. The regulatory model that grows out of this proceeding must assure adequate cost recovery through a still-to-be-determined combination of base rates, performance incentives, and market-based earnings ("MBEs"), but still maintain affordability. The optimal model allows for fair allocation of benefits and costs, but provides for cost recovery of pilot and demonstration projects, enabling DER integration, and achieving the other REV policy objectives. For their part, utilities should incorporate REV principles in all aspects of the business model. This entails identifying the necessary investments and enhancements in both the electric grid and customer operating systems that allow for leveraging technology to increase efficiency, reliability, resiliency, and improve the customer experience. Ratemaking policy should therefore incentivize utilities to design and operate a system that optimizes DER integration. Such policies should also encourage an array of new products and services that meet the desires of customers, deliver value, and create efficiencies.

Exelon is generally supportive of these ratemaking and utility business model reform efforts, subject to the comments herein and further development of the REV initiative by the Commission. By shifting from a purely rate-based regulatory model to a more hybrid regulatory model, utilities will be best positioned for managing future growth and achieving reduced costs for customers. California, Maryland, Massachusetts, the District of Columbia and Hawaii have also initiated policy efforts aimed at reforming their energy markets, and other jurisdictions are expected to follow suit. That is not to say, however, that what is adopted in one jurisdiction is necessarily appropriate elsewhere.[11] But as with REV, Exelon has consistently supported efforts to most efficiently achieve the objectives of regulatory and market reform in a manner consistent with other policy initiatives at the regional and wholesale market levels.

II. Aligning Customer Value with Earnings Opportunities

A. The MBE Model

The evolution towards the new utility business model(s) will require certain regulatory policies to better align customer value with utility earning opportunities. Staff has already proffered a combination of financial incentives that include new MBE opportunities, adjustments to ratemaking, and target-based performance incentives.[12] Staff notes that increased MBEs will have the dual benefit of 1) encouraging utilities to support access to their systems by DER providers who can improve the economics of the system and add value to end-use customers, and 2) offsetting required base revenues derived from ratepayers.[13] Moreover, the utility as a platform presents opportunities for new utility services and associated revenues which will

[11] The Commission should remain fully cognizant of the experiences in other jurisdictions, such as Germany, Spain, Italy, California and Hawaii, where in some cases delivery costs to customers skyrocketed despite an environment where wholesale energy prices were depressed.

[12] *Id*., at 28.

[13] *Id*., at 9.

supplement existing rate-based utility revenues.[14] Staff suggests that a primary vehicle anticipated for utility MBEs will be platform service revenues ("PSRs") that utilities, in their capacity as DSP providers, will earn from market participants. The intent is that utilities will be able to diversify their business and protect against the concern of lost sales from, and potentially stranded investments in, conventional business units as more third-party investment enters the system.[15] Staff believes the eventual shift in balance from traditional regulatory incentives to MBE opportunities will complete the transition to a business and regulatory model where utility profits are more directly aligned with market activities that increase value to customers.[16]

While the market's incremental progression will determine the success of these incentives and full realization of the REV vision, Staff appropriately recognizes that there are unresolved issues. Specifically, certain aspects of the proposed incentives will require additional consideration in advance of wide-scale adoption, including:

- How MBE charges will be set in a manner that is "comparable and fair,"[17]
- How the role of the platform provider (*i.e.*, utility) will be defined versus what services will be open to third party providers on a competitive basis,[18]
- How the balance will be determined between what providers of services pay versus end-use customers,[19]
- How new revenue sources will be treated from a ratemaking and/or earnings sharing perspective,[20] and

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[14] *Id*., at 29.

[15] *Id*., at 30.

[16] *Id*., at 10.

[17] *Id*., at 36.

[18] *Id*., at 33.

[19] *Id*., at 33.

[20] *Id*., at 35.

- How best to align utility interests with policy goals when choosing the optimal trade-off between utility capital expenditures versus third-party DER versus utility operating expenditures.[21]

Resolving these issues will be particularly important to the success of the future utility business model. Exelon believes MBEs, used appropriately where value is added, are an important part of the future utility business model. However, MBEs should be integrated over time with the benefit of experience obtained in pilot programs that demonstrate the MBE programs are proven and reliable. In the meantime, while the above issues are still being resolved, MBEs should not be immediately relied upon as a one-for-one substitute for utility earnings derived from sustaining system reliability, as the Commission cannot rely on unproven MBE opportunities to fund essential grid functions. Similarly, the White Paper suggests a variety of performance incentives that would provide opportunities for utilities to earn additional revenue.[22] Exelon agrees with Staff that, where appropriate, utilities should be provided opportunities to enhance revenue from 1) performance incentives or 2) the provision of adjacent services, where the utility may be uniquely well-positioned to provide the means for such. Nevertheless, those performance incentives should be bilateral and symmetrical whenever possible. Formula rates (in reality, a form of performance incentive) are also worthy of consideration. Formula rates have been proven to provide a higher degree of financial certainty, regulatory streamlining, and, if designed correctly, customer protection.

[21] *Id*., at 40-43.

[22] *Id*., at 54-63.

B. The Utility/DSP Revenue Model

Exelon agrees with Staff that utilities are the entities to provide platform services optimally and efficiently.[23] Utilities should continue to utilize regulated assets for energy delivery, while facilitating non-regulated services that maximize the value of the grid in such a way that ensures all users pay their fair share, no customer pays more than their fair share, and achieves a balance between what service providers pay on the one hand and what end-users pay on the other.[24] Exelon agrees with Staff that "to achieve the benefits to customers that REV-enabled reform contemplates, utilities will need both mechanisms to recover the expenses they incur to support the developing market and opportunities to earn on them," and looks forward to seeing more complete details of Staff's proposals for recovery of utilities' costs and the mechanisms for providing a return on services that support the marketplace.

Exelon also believes it is critical that when evaluating ratemaking reforms the Commission should align ratemaking structures and incentives with other public policy objectives related to power delivery, such as reliability and resiliency. In particular, the Commission should consider additional, policy-driven metrics tied to critical objectives including carbon reduction and system reliability. When establishing these ratemaking structures and incentives, however, the Commission should not tie revenues necessary to fund core grid operations to outcomes that are highly dependent on customer preferences (participation in TOU rates, as one example).

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[23] *Id*., at 31.

[24] *Ratemaking White Paper*, at 33.

C. Public Policy Achievement

As the Commission stated in the Framework Order and Staff reiterated in the White Paper, despite technological change and opportunities for improvement through market mechanisms, electricity remains an essential service imbued with multiple public policy demands.[25] The societal benefit inherent in a reliable, resilient, affordable, and clean energy grid underscores the need to preserve the utility franchise. While the role of the utility may evolve to a more market-based model, there is an underlying need for the continuing ability of the utility to deliver a physical commodity across all classes of customers. Earnings opportunities should recognize both roles. To meet the system demands envisioned by REV, and evolve to the platform-enabling and service-based models that add value in the future, utilities must maintain investment in the physical grid. By making grid investments that increase resilience, flexibility and interoperability, utilities can be positioned to integrate DER, protect the environment through increased use of energy efficiency and clean energy, and undertake market enabling measures that integrate those resources in a manner that achieves both economic and environmental sustainability. The ratemaking principles and changes proposed by Staff should therefore continue to account for public policy goals, including, but not limited to, ensuring system reliability and security, protecting low-income customers, and supporting attainment of the State's environmental goals.[26]

Exelon supports Staff's reconciliation of public policy objectives with REV goals and initiatives, particularly with respect to energy efficiency and environmental objectives. Exelon believes that energy efficiency programs, when structured properly and implemented efficiently,

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[25] *Id.*, at 8.

[26] *Id*.

enable customers to get the maximum value for their energy dollars. This is particularly important for low-income customers. The White Paper recommends that utility-sponsored energy efficiency should transition from general resource acquisition to targeted and market-based approaches.[27] It is unlikely that these results could be achieved, especially in the short-term, without leadership by the utilities and without appropriate cost recovery, including a return on energy efficiency investment. With respect to alignment with environmental objectives, Exelon supports Staff's suggestion to consider any changes within the context of the State Energy Plan goals and future federal goals.[28] Meeting these stated goals will require maintenance of existing carbon-free clean energy resources, and a mechanism to attract new carbon-free clean energy resources. This requires a single market CO_2 price to retain and attract carbon free clean energy resources at the distribution and wholesale level, or consideration of the implementation of the CFAR outlined on page 65 of the White Paper. Regardless of the approach, the State must move quickly to appropriately value and implement a carbon methodology to align with New York's stated climate goals.

D. Earnings Impact Mechanisms, Scorecards and Outcomes

Staff makes several points and recommendations with respect to Earnings Impact Mechanisms ("EIMs"), scorecards, and outcomes.[29] For example, Staff proposes that existing safety, reliability, customer-service, and utility-specific performance mechanisms should be retained, and that Earnings Sharing Mechanisms ("ESMs") should be developed for peak reduction, energy efficiency, customer engagement and information access, affordability, and

[27] *Id.*, at 44, 48.

[28] *Id.*, at 51.

[29] *Id.* at 51-68.

interconnection.[30] Staff also proposes that scorecard measures should be developed for system utilization and efficiency, and a host of other objectives.[31] Exelon cautions that while it is a laudable goal to align economic interests with performance, successful use of performance metrics require clearly defined standards of measurement as well as deployment of advanced metering. Without these safeguards, customers could pay for changes that ultimately do not deliver REV promised customer benefits. As stated in Exelon's BCA comments, there is a need to "get it right," because failure to do so will lead to wasted capital, increased costs, and lost opportunities to deliver actual value.[32]

One proposed scorecard metric, Carbon Reduction, is worth noting in particular. Staff proposes that each utility be monitored for its CFAR. Specifically, this metric should reflect 1) carbon-free sources of generation sponsored by utilities, as well as third parties for the benefit of load within the utility footprint; and 2) energy efficiency penetration.[33] Exelon suggests this metric should include maintenance of all existing zero carbon emitting resources in New York, and not just limit this to utility-sponsored resources. Exelon agrees that the development of this measure is at least partially dependent on the issues pending in the Large Scale Renewables proceeding, but suggests that such a metric could provide support for appropriately valuing carbon-neutral resources, and incentivize the marketplace to utilize clean energy base-load resources for long-term reliability and environmental compliance.

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30 *Id*.

31 *Id*., at 63-66.

32 *Exelon BCA Comments*, at 19.

33 *Ratemaking White Paper*, at 65.

III. Rate Design

Exelon agrees with Staff that "efficient price signals and transparency are hallmarks of a successful market" and that "[r]ate design and compensation mechanisms that accomplish these will help to optimize the investment in and use of DER, thereby reducing total system costs and customer bills, not only for customers with DERs. Conversely, rates that are bundled and mask the underlying costs of service will not facilitate efficient decisions."[34] Exelon also agrees with Staff that there is a fundamental need to change the way utility distribution costs are currently being recovered from most of its customers as utilities face new and significant challenges due to declining electric sales growth, the need for increased investment, and new enabling technologies. Declining sales growth has occurred and customer self-generation is being increasingly adopted. There is a need for increased utility investment in delivery infrastructure due to customers' greater reliance on electricity (*e.g.*, internet, computers, cars), the desire to ensure greater reliability and resiliency (post-Superstorm Sandy and Hurricane Irene), general aging infrastructure, advanced metering deployment, higher levels of power quality needed for the digital economy, and a demand for increased grid cybersecurity. At the same time, new technologies and advanced metering enable more robust usage and allow customers to both generate and use electricity differently. For all of these reasons, electric utilities must revisit their traditional rate structures for delivery service (mainly distribution), especially for residential customers.

Distribution rates should be aligned with the underlying cost structure of the distribution network, and incentivize high performance. Without rate redesign, price signals in a post-REV environment will be distorted, and higher costs will need to be recovered over a smaller sales

[34] *Id.*, at 81.

base consisting disproportionately of customers without the means to invest in DER. Larger residential customers increasingly can avoid paying a large share of their cost of service under volumetric rates by adopting DER, even though most DER customers still need grid delivery services. This results in the need for greater cost recovery from non-DER customers. Therefore, non-DER customers will generally have to pay more than their fair share and/or utilities may under-recover their costs. Under recovery of distribution revenues may result in negative impacts on reliability and the ability to invest in new grid technologies due to credit rating impacts and higher costs for, and constraints on, capital. Rates designed around a higher proportion of demand charges ($/kW) and/or fixed customer charges ($/customer) would better reflect the distribution system cost structure and thereby ensure adequate cost recovery in a world of low or declining load growth. This new rate structure also would provide more efficient price signals for customers and DER for value provided and received, thereby encouraging economic DER integration and better aligning utility interests with public policy goals. As in any market, distribution system prices send signals and change the behavior of participants, and there are reliability and economic risks when those price signals lead to artificial subsidies – or uneconomic bypass – that create disparate impacts. We therefore support Staff's goal to move away from conventional distribution service rate design and to transition to efficient price signals for distribution services.

Exelon also supports the Staff proposal to consider demand-based distribution rates for all customer classes, not just commercial and industrial ("C/I") classes.[35] Demand-based delivery service rates already exist for most commercial and industrial customers, a customer

[35] In Illinois, ComEd has proposed a demand-based rate design for residential customers that allows for new uses of the grid while ensuring that related costs are borne by those who benefit from grid services. *See*, H.B. 3328/S.B. 1879, 99th Gen. Assem. (Il. 2015).

sector that over the past decade has experienced high migration, engaged customers, and innovative product offerings. Exelon agrees with Staff that adopting a rate design and compensation mechanism based on a more precise calculation of system value should greatly improve the proper valuation of DER.[36] This solution is consistent with the principle that the grid is the necessary, foundational platform for REV generally, and the expansion of DER in particular. There should be fair compensation for use of the grid by all customer classes. At the highest level, Exelon encourages the Commission to consider what has worked well for C/I customers in terms of demand-related charges and apply those lessons to all customer classes as advanced metering infrastructure is established. It is critical that compensation to maintain the grid is ensured, and that customers receive price signals that align distribution revenues with associated costs so that customers pay no more or less than their fair share. This new rate design will establish the foundation on which to value DER and the appropriate compensation level for their application.

Accordingly, Exelon suggests the Commission develop a rate design that allows for new uses of the grid, including the expansion of DER, while ensuring that related costs are borne by those who benefit from services.[37] Without new rate design, price signals will be distorted, and costs will need to be recovered over a smaller sales base consisting disproportionately of customers without the means to invest in DER. As Staff correctly recognizes, a demand-based rate design can leverage the capability of advanced meters, which are able to record energy demand in addition to consumption data. Exelon therefore agrees that "the introduction of advanced metering functionality will enable movement beyond the historical dispute between

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[36] *Id*., at 83.

[37] Most DER customers still need grid delivery services, as they both consume power from the grid on certain hours, and provide power to it in on other hours.

fixed customer charges and volumetric rates."[38] Exelon believes that this technology must be coupled with a demand-based rate design applicable to all customer classes to ensure that customers pay their fair share for use of the grid. The introduction and use of demand rates will provide customers with the potential for savings by reducing their demands on the distribution system, while ensuring more equitable cost sharing among participating and non-participating DER customers.

Staff proposes that changes to rate design may need to be gradual in order to mitigate potential impacts of sharp rate changes. In addition, Staff suggests that new rate structures may also have "opt-in" features that allow customers to choose between alternative rate designs.[39] Exelon understands the importance of carefully managing customer bill impacts, and the need for customer education regarding new rate structures. Phasing in a new rate design can be appropriate, for example, when the new structure is unfamiliar to customers, has significant potential budget impacts, or is designed to induce behavioral changes that take time to accomplish.

Exelon, however, opposes voluntary opt-in rate structures in cases where the rate change is designed to improve efficiency or to lower social costs. Efficient rates should reflect the costs and, where appropriate, the benefits of the subject use or behavior, accurately measured, and thereby send a correct, efficient price signal, and equitably allocate costs. Indeed, an existing rate structure requires replacement most urgently where it is *failing* to meet those goals – where it is not correctly designed and, as a result, is sending an inefficient price signal and imposing inefficient cross-subsidies and penalties. The new, efficient rate structure should apply to all

[38] *Id*., at 98.

[39] *Id.*, at 96-97.

similarly situated customers if it is to promote efficiency and equity. If the new rate structure requires customers to either "opt-in" to experience these new rates, or alternatively, allows customers to "opt-out" to avoid these new rates, it will allow customers to ignore the economically efficient price signal the new rate sends and perpetuates inefficient behaviors, inequitable subsidies, and social losses. Indeed, because the particular customers most likely to opt-in or opt-out to an alternative rate design are not random, such optional rate designs can actually exacerbate the problems of inaccurate price signals, subsidies and cost-shifting, and under-recovery of grid-related costs. Customers who have the greatest stake in the existing, inefficient rate structure will have the ability to avoid paying their fair share of grid costs. Furthermore, these social losses are often not evenly distributed. Larger customers, that can more easily and rapidly exploit opt-in/opt-out rates, can take advantage of them at the expense of other customers and/or utility shareholders.

Exelon, therefore, suggests the Commission adopt rate changes consistent with efficient price signals as they are identified and recognized. When rate impact concerns are legitimately raised those concerns can be addressed with phase-in periods rather than by optional opt-in or opt-out rates. Metering system investments, data gathering, scenario analysis and modeling, customer education, and consensus-building may be valuable tools to support this transition. During the transition period, Exelon believes that the same efficient price signals should be sent to all similarly situated customers, incrementally where appropriate, as opposed to being offered on a voluntary, opt-in or opt-out, basis. New, improved rate designs should send socially efficient price signals, not allow for their avoidance.

IV. Conclusion

Exelon appreciates this opportunity to submit to the Commission its Ratemaking and Utility Business Model Comments in support of the comprehensive ratemaking reforms critical to the success of the REV vision. Exelon will continue to remain actively engaged in the stakeholder process as the complex issues related to ratemaking and other REV initiatives are more fully explored.

Respectfully submitted,

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