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5 June 2007

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

RE: Initial Comments of Comverge, Inc. Regarding
Integrated Resource Planning Approval Process
Docket No. E-0000E-05-0431

Dear Madam or Sir,

This is to (1) request to be placed on the service list for this docket and (2) provide the response of Comverge, Inc. (Comverge) to the request for written comments of the Arizona Corporation Commission (Commission) regarding the Staff's 26 April 2007 Meeting Notice on the Commission's Resource Planning Workshops.

Comverge appreciates the opportunity to provide comments and to work with the Staff and other stakeholders on resource planning and competitive procurement issues.

If the Commission and any of its staff have any questions about this response please contact me.

Sincerely,

Dr. Eric C. Woychik
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On Behalf of Comverge, Inc.

Attachment

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Comverge, Inc.
Initial Comments Regarding
Integrated Resource Planning Approval Process
Docket No. E-0000E-05-0431

Introduction

This is in response to the Arizona Corporation Commission (Commission) Request for Meeting Notice ("Request") to schedule workshops on resource planning and request comments on a set of questions about resource planning and the Integrated Resource Planning Approval Process ("IRP Approval"). Comverge appreciates the opportunity to participate in the Commission's resource planning proceeding and for this opportunity to provide comments.

Comverge provides about 6,000 MW of Demand Response (DR) equipment in the U.S. and now has over 550 MW of 3rd party, fully-outsourced, pay-for-performance DR contracts in place with ISO New England, Nevada Power, Pacific Gas & Electric, Public Service New Mexico, Rocky Mountain Power, and San Diego Gas & Electric.

Overview of Comverge's Position

Comverge agrees with Arizona Public Service (APS) that the fundamental goal of resource planning is to provide reliable service at lowest cost, in light of overall resource portfolio risks and regulatory requirements. Comverge also agrees that Nevada's approach does indeed emphasize risk management and portfolio management. What is needed in Arizona is a similar approach that provides for clarity and consistency in the determination of the resources that are preferred and that should be selected.

The corollary need is to recognize the major benefits of Demand Side Resources (DSM), particularly when provided in fully-outsourced, long-term, pay-for-performance contracts. A problem with many resource planning approaches, however, is that they have limited time windows, such as to look only 3 years out, which is too short a time frame. DSM, benefits increase over time, as with supply resources, thus, the IRP process should extend at least 15 years out. These fully-outsourced contracts defer long-term needs for peaking capacity, transmission and distribution capacity, reduce congestion, increase reliability, reduce environmental mitigation, lower overall electricity prices, and provide market power mitigation. The difficulty is to provide a comprehensive summation of the benefits of DSM, particularly for DR and energy efficiency, as compared to supply-side resources. Undoubtedly, DR is an outstanding resource that reduces fuel risks, provides hedging, and lowers overall portfolio risk. Nevada Power's recent procurement to select a 126 MW DR contract using Comverge reflects these benefits.

IRP approval should enable a comparative preference for DSM, or a comprehensive apples-to-apples comparison of DSM to the full suite of supply-side resources that it defers, as well as recognition of its portfolio risk reduction benefits. California has used a "Loading Order" preference to accomplish this. North Carolina promotes DR and energy efficiency over supply-side resources, and requires compliance.

The difficulty is to provide an elegant mechanism that enables a proper comparison. Cost-effectiveness that incorporates the appropriate benefits and costs -- of generation, transmission, distribution, and environmental mitigation -- is quite complex to implement. Portfolio management and risk management methods are complex and somewhat expensive to implement. For these reasons, a loading order preference that recognizes the benefits of DSM may be preferred, particularly in resource plans that have few DSM resources to begin with. With this backdrop we respond to Staff's questions.

Staff's Specific Questions

First, what should be the primary objectives of a resource planning process? Comverge agrees with APS that the primary objective is to "identify the preferred resources that will be needed to meet anticipated customer needs in a reliable and cost-effective manner." The resource planning process should enable an objective, direct comparison of all resource options, including all major risks and uncertainties. A basic list of cost/benefit categories, including risks and uncertainties, bears detailed consideration, as the following costs/benefits, risks, and uncertainties should be central to the resource selection and procurement process:

- Resource installation, including siting, permitting, cooling, and land-use;
 - Total capital and variable costs for resource installation and operation, including for interconnection, transmission, distribution;
 - Environmental mitigation (NO_x, SO_x, CO₂, water, and land use);
- Fuel price and delivery costs, security risk, and volatility;
- Warranty, inspection, fixed and variable operations & maintenance costs;
- Comparable capacity delivery, including planned and forced outage rates;
- Performance risks, including cost responsibility for resource performance;
- Comparable dispatchability, ramp-rate, and operational flexibility;
- Local and regional stakeholder response (e.g., increased customer choice), including long-term labor impacts;
- Wholesale market price and market power mitigation impacts;
- Specific performance to provide stipulated capacity and energy results;
- Locational resource adequacy, to reduce congestion, reduce the use of reliability-must-run generation, and address voltage and reliability needs in load pockets.

Second, Comverge suggests that the Commission examine the problem of retail versus wholesale jurisdictions that results from reliance on regional transmission organizations. That problem is one of separating the transmission and wholesale functions from the retail resources and retail functions. Retail services, particularly DSM services, can defer transmission, generation, and distribution needs. In a regional transmission planning review DSM will usually not be considered, as it is a retail function, which then leaves this major resource expansion opportunity unaddressed. This suggests that the ACC should NOT rely on regional transmission entities to provide resource planning functions.

Third, should a Commission decision “accepting” or “approving” a plan (or part of a plan) be regarded as a finding of “prudence” in subsequent rate cases? The national trend appears to be that utility decisions on resource selection once approved by a Commission should not be second guessed. To do so is akin to voiding the sanctity of a contract. Two prudence scenarios seem relevant, cost overruns and failure of specific performance.

Resources approved at a defined costs that then face cost overruns, which utilities seek to recover, amount to reopening or renegotiating the contract, as the terms have changed. The just and reasonableness of the additional cost then suggests further analysis and approval is needed by a Commission as the contract (regulatory compact) has changed.

If a resource is expected to perform at a specific level after being approved by the Commission, failure to obtain specific performance suggests breach as the contract is not honored. Prudence may in this case be in question. This may occur if the projected capacity (MWs) does not show up over time as stipulated. Utility implemented DSM programs are noted for failing to perform – to provide the expected MWs of capacity and MWh of energy over time – thus, the Commission may view this as a prudence issue.

This suggests that prudence may be an issue if cost-overruns occur or if actual performance is out of line with stipulated performance. With respect to DR programs, Commissions have many times ignored the ongoing performance and costs of maintaining the capacity level previously stipulated. Comverge seeks to be on record that it seeks to ensure that the stipulated DR capacity promised is provided over the duration.

Accordingly, the Commission should accept or approve a resource plan or part of a plan given clearly stated specific performance, with a forewarning that this performance is stipulated. Deviations from stipulated specific performance would amount to lack of contractual performance and may be material enough to trigger prudence review.

Fourth, the specific information that should be included in ACC jurisdictional resources plans was previously listed above, in response to the first question, in terms of relevant cost/benefit categories. In addition, the Commission should ask that each of the resource options be assessed based on the following:

- Comparable forced outage rates;
- Impact on Loss-of-Load Probability (LOLP);
- Net-present-value of total benefits and costs;
- Cost per kW-year for capacity resources;
- Costs per kWh for energy resources.

Fifth, what time limits should apply to the Commission’s processing of a resource plan? If a resource plan is to be used for 3rd party procurement and for short-term and long-term utility self-build projects, it should be reviewed by the Commission and approved in a timely manner. The classic problem occurs when the utility and market circumstances change rapidly, particularly when circumstances require expedited treatment to ensure resource adequacy. This may suggest approval of part of a resource plan in a time frame less than 180 days. Absent a need to act sooner, the APS recommendation of review and approval in 180 days seems reasonable.

Sixth, how frequently should a utility file a resource plan? This depends on the pace of load growth, the level of specific knowledge about locational resource adequacy,

and the flexibility of the resources that are in place. This also depends on the types of resources that are being implemented. DR and energy efficiency can be installed quickly, without siting and environmental review, can avoid NIMBY issues¹, and can be used as soon as each incremental end-use device is installed. Supply-side resources, however, must be fully installed and complete before they can meet customer loads. With generation additions, new transmission and distribution capacity may also be needed before loads can be met. In either case, this suggests that the time frame for approval and installation of supply side resources is much longer than for DR and energy efficiency. Accordingly, it seems appropriate for utilities to file resource plans, or partial resource plans, whenever they need to, depending on the adequacy of the supply-demand balance and local resource adequacy.

Seventh, how can a resource planning process be developed that takes into account changes that occur between filings? The proposed use of action plans to identify steps to develop or procure needed resources may provide sufficient clarity to ensure local resource adequacy. Even with market changes, there are opportunities to reduce the use of older plants and to take advantage of other resources that may change the resource expansion path of a utility. This suggests that utilities file action plans on a quarterly or six month basis.

Eighth, should resource plans use a short term "action plan" to obtain more direct Commission direction? Comverge generally thinks this approach is wise, particularly to identify the types of resources that are most appropriate but as well to define the costs that current resources are causing on the system. That is, local resource adequacy should be reviewed and reported on by utilities on an ongoing basis. The short term "action plan" filed by the utilities may also include information about (i) redispatch to address transmission congestion and (ii) the use and cost of reliability must run units to provide voltage and security needs.

Ninth, what role should DSM play in the resource planning process? DR and energy efficiency are very beneficial under specific circumstances and should be integral to the resources planning process. The problem is that utilities are not usually fully aware of the amount of DSM that can be provided, how it can be provided, or the cost of various DSM resources.

This strongly suggests that utilities use an all sources Request for Proposal (RFP) process in order to assess the opportunities to procure DSM from 3rd party providers. Comverge is very interested to provide DR and energy efficiency to utilities in Arizona, particularly under fully-outsourced pay-for-performance contracts.

The opportunity also exists for Arizona utilities to procure DSM under a competitive RFP and still take ownership of DSM assets (equipment and installation), allowing these assets to be rate-based. At the same time Comverge is willing to take all the risks of marketing, customer acquisition, equipment installation and warranty, customer call center operation, project operations, and to be paid only for specific performance based on \$/kW provided.

With respect to the balance of benefits and costs, the Comverge fully-outsourced approach shifts most all of the risks onto itself, leaving far fewer risks on the utility and its customers. Specifically, Comverge is willing to bear the total amount of capital and variable costs, resource installation and operations, warranty and inspection, and to

¹ NIMBY is the "not in my back yard" problem that may hold up installation of supply side projects.

provide DR on a rapid, dispatchable, locational basis. DR does not require transmission or distribution, has no fuel price or deliver risks, has a very rapid ramp rate, is flexible in its use, reduces wholesale prices, and provides market power mitigation.

Finally, should risk management be factored into the decision making process? Risk management is critical for effective utility resource planning. As explained above, DSM can be provided in ways that dramatically reduce utility and related customer risks, most clearly through use of the all sources RFP process and use of 3rd party fully-outsourced, pay-for-performance contracting.

Conclusion

A flexible resource planning process is essential in Arizona given the current setting of mixed markets and regulation. The previously listed costs/benefits, risks, and uncertainties should be central to the resource selection and procurement process. Most importantly, comparability of resources in the selection process should be ensured, in order to enable apples-to-apples comparisons. Moreover, the resource selection process should specifically account for risks that the utility and its ratepayers will face, including performance risks after the selection process is complete. To avoid being pulled back into prudence question after the selection and approval process is complete specific performance should be fully defined, and appropriate incentives should be harnessed to ensure high performance. The use of 3rd party, fully-outsourced, pay-for-performance contracts will avoid future concerns about prudence, as payment is only forthcoming with verified performance. Furthermore, these DR contracts dramatically reduce overall risks and enhance a utility's resource portfolio, in part because fuel risk, transmission and distribution needs, and NYMBY issues are rendered moot. Finally, a loading order preference for DSM may be an appropriate policy for the Commission to adopt, in order to advance the use of DR and energy efficiency and to lower the overall risks of utility resource portfolios in the State. To accomplish this and provide profitability for Arizona utilities, all source bidding is recommended, to procure resources on a pay-for-performance basis, accompanied by a policy to allow for Commission approved DSM equipment and installation costs to be rate-based.