SUBMISSION OF INDIANA INDUSTRIAL ENERGY CONSUMERS, INC.
TO THE
INDIANA UTILITY REGULATORY COMMISSION

# INDIEC'S COMMENTS REGARDING THE COMMISSION'S BACKUP, MAINTENANCE, AND SUPPLEMENTAL POWER RATE REVIEW CONDUCTED PURSUANT TO INDIANA CODE § 8-1-2.4-4(H) and GAO 2017-3

April 20, 2018

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Indiana Industrial Energy Consumers, Inc. ("INDIEC") makes this submission to the Indiana Utility Regulatory Commission ("IURC or "Commission") in response to the March 16, 2018 submissions of the electric utilities regarding their provision of backup, maintenance, and supplemental power to customers served by cogeneration, small hydro, and alternative energy production facilities, or private generation projects, (collectively "private energy projects").

Consistent with explicit state and federal policy, INDIEC has a strong interest in promoting the development of efficient, cost-effective, private energy projects to serve the energy needs of large industrial customers. This submission will, therefore, address both specific issues with the electric utilities' tariff structures, which impede the statewide implementation of that policy, and offer suggestions that would better align existing structures with state and federal policy on private energy projects.

## Executive Summary

Indiana industrial and manufacturing customers once enjoyed the economic advantage of low-cost energy within the State. That advantage made manufacturing a vital component of the state's economic health. Even today, manufacturing accounts for about one in six jobs within Indiana, employs over half-a-million Hoosiers, and pays $31 Billion in wages.[1]

Nevertheless, the economic advantage of low-cost energy has eroded in the course of the last fifteen years. Whereas in 2003 Indiana had the 5th lowest industrial electricity prices in the nation, at the close of 2017 Indiana's industrial electricity prices had slipped to the 31st lowest.[2] The trend in rising energy costs is expected to continue as older, largely depreciated, plants are retired and new units are brought into service.

[1] Indiana Dept. of Workforce Development, *Indiana Economic Analysis Report: Program Year 2016* (October 2017) at 7.
[2] U.S. Energy Information Administration, *Electricity Data Browser*, Table 5.6: Average Retail Price of Electricity to Ultimate Customers by End-Use Sector, by State.

Reasoned and decisive steps to counteract, or at least mitigate, the trend in rising prices must be taken not simply to promote continued manufacturing growth in Indiana, but also to preserve the existing manufacturing base. The deployment of private energy projects is one means by which customers can mitigate their own costs, but it can also help reduce costs for all ratepayers by reducing the need for incremental investment by utilities in new plant. Accordingly, one step available to the Commission to help mitigate the rising cost trend is to take action to further the State's explicit policy encouraging the development of private energy projects.

That policy and the Commission's role in its implementation are clear. Indiana Code §8-1-2.4-1 declares that: "It is the policy of this state to encourage the development of alternative energy production facilities, cogeneration facilities, and small hydro facilities in order to conserve our finite and expansive energy resources and to provide for their most efficient utilization." Likewise, Indiana Code §8-1-2.4-3 mandates that the Commission "shall encourage the participation of utilities in alternative energy production facilities, cogeneration facilities, small hydro facilities, and private generation projects."

In order to further the policy encouraging private energy projects, however, the Commission must ensure rates for standby service[3] are cost-based and non-discriminatory to those customers who utilize such projects. A review of the electric utilities' responses to the Commission's request for information indicates that much can be done to better align standby service rates with those basic ratemaking principles.

[3] As used throughout, the term "standby service" refers to both backup power which is the provision of energy and capacity as a replacement for that ordinarily produced by a customer's private energy project facility during an unplanned or forced outage of that equipment, and maintenance power which is the provision of energy and capacity when a private energy project unit undergoes a scheduled outage, such as for maintenance and upkeep.

Establishing rates that reflect the actual use of the system by customers with private energy projects and which do not penalize a customer for using a private energy project when it calls for standby service is a necessary prerequisite to make such projects cost-effective. Promoting such rates will encourage investment in private energy projects to the benefit of all. Conversely, failing to do so will hinder the development of private energy projects contrary to explicit State policy and impose unnecessary costs on all ratepayers.

## I. Why Private Energy Projects and Proper Standby Service Rates?

Longstanding Indiana and federal policy encourages the development of private energy projects[4], and does so with good reason. Such projects can be tailored to meet the specific needs of a customer and are highly reliable and highly efficient; and the proximity of private energy projects to the facility utilizing the generation reduces grid congestion. Moreover, by reducing the needed capacity required to serve customers within a specific service territory, private energy projects reduce the incremental investment in generation that must be made by a public utility. For public utilities operating as regulated monopolies such as those in Indiana, this reduces the overall plant on which the utility earns a return of and on, thereby reducing the overall cost to all ratepayers.

Actual investment in private energy projects, however, requires that numerous prerequisites be met. Among these are a cooperative relationship with the energy utility serving the territory in which the facility is to be located and standby rates that do not penalize a customer with a private energy project when it requires standby services and thereby impose undue risk and make operation of such a facility economically unviable. Indeed, if price signals

[4] *See, e.g.*, Indiana Code §8-1-2.4-1; §8-1-37-4(a); 16 U.S.C. §796(17(A) and 16 U.S.C. §824a-3.

fail to differentiate between a customer with a private energy project and a customer without such a project there is no economic incentive to invest the resources to pursue the private energy project in the first instance.

Likewise, rates that fail to properly account for the limited costs associated with a private energy project customer on the system are discriminatory. Adherence to cost-based ratemaking ultimately mandates that private energy project customers be obligated to pay only for the system resources dedicated to their use. If, however, standby service rates are out of alignment with cost-based principles and customers are required to pay more for such services than they should, they are subsidizing other customers and paying discriminatory rates.

Setting proper standby rates, accordingly, is necessary not only to adhere to both State and federal law, but also to promote and encourage investment in private energy projects consistent with long-standing legislative policy at the State and federal level.

## II. Creating Cost-Based Standby Rates

Establishing cost of service based standby rates begins with the recognition that customers operating private energy projects are different in their usage patterns than full requirements customers. Unlike a full requirements customer who imposes load on the system throughout the entire year, a customer with a reliable private energy project requires standby services only during the course of an unplanned outage of the generation unit (back-up service) or during scheduled repairs and servicing of the generation unit itself (maintenance service). The load on the system necessary to serve a customer with a private energy project thus amounts to only a fraction of the load of a full requirements customer. A cost-based rate for standby service should recognize this distinction both in cost allocation and rate design.

As a matter of cost allocation, a customer using a private energy project should only be allocated those costs it actually imposes on the system. This means, from the standpoint of capacity, that customers with private energy projects should only be allocated the amount of reserve capacity necessary to meet the needs of the class of customers using private energy projects at system coincident peak. FERC rules, in fact, expressly prohibit the establishment of standby rates, absent evidence to the contrary, based on the assumption that outages by all private energy projects served by a utility will occur simultaneously and/or on the system peak; and expressly require consideration of the ability of customers utilizing such projects to schedule outages in coordination with the utility's planned outages.[5] This means that standby rates, absent compelling evidence, cannot be structured on the assumption that the utility must make an investment in capacity equal to that of the amount of capacity needed for the entire private energy project class at the time of system coincident peak.[6]

Given that private energy project customers do not impose full requirements load on the system year round, the amount of capacity dedicated to their service should reflect a level of capacity less than the amount required to serve an equivalently sized full requirements customer. Instead, the private energy project class should only be allocated the amount of capacity that can reasonably be expected to meet it needs at the time of system coincident peak. That allocation should reflect a realistic assessment of the private energy project resources' expected outage rates. In other words, the allocation should reflect the reliability of private energy projects and the ability of customers with such projects to time planned outages and operational loads in order to avoid calling for standby service during utility system peaks.

[5] *See* 18 CFR Ch. I, §292.305(c).
[6] To assume otherwise would, in fact, lead to the unnecessary investment in excess capacity by the utility and foster inefficient investment decisions.

The distinction between full requirements customers and those utilizing private energy projects, as well as the flexibility of customers with private energy projects to tailor their operations, should be further reflected in the amount of costs allocated to private energy project customers. Standby rates, accordingly, should only reflect cost recovery for any incremental reserve capacity maintained by the utility to serve the load of private energy project customers. In short, standby rates should not, indeed cannot, treat customers with private energy projects as though they were full requirements customers.[7]

Following the basic ratemaking principles outlined above, nearly all the standby service tariffs submitted by the utilities fail in some respect to reflect the basic distinction between a full requirements customer and a customer with a private energy project that supplies all, or part, of the customer's load. The default to full service rates, the inclusion of demand ratchets, and maintenance power rates that do not reflect the ability of the utility and customer to coordinate outages all reflect rates that deviate from cost of service principles and discriminate against customers utilizing generation from private energy projects.

For example, rather than creating a truly distinct rate for standby services, many tariffs reflect standby rates that effectively default to the base rate under which the customer is served as though they were a full requirements customer. Even among those tariffs that include some reduction in demand charges, the reduction is not significant or clearly tied to the expected

[7] Generally, utility power provided to a customer with a private energy project that, under normal operating conditions, does not supply all of the energy needs of the customer (supplemental power) is appropriately allocated and priced as though it were being provided to a full-requirements customer. This general rule is subject to two important caveats. First, to the extent a customer with a private energy project is able to reduce the net demand of its operational load during a generation outage or derate down to the level of the demand of its supplemental load, there should be no charge for standby service as its load does not differ from ordinary operating conditions. Second, in the case of a customer who takes some amount of standby service in excess of its supplemental load during an outage, the standby service should not affect the ratchet for the supplemental power, as the costs associated with the standby service are already recovered through the standby service rate.

outage rate of the private energy project. Nor does there appear to be a significant recognition that the need for maintenance power can be timed to coincide with non-coincident peak periods, justifying a lower rate for such power.

These failings unreasonably penalize a private energy project customer by imposing system costs on the customer that they did not cause and that the utility is not obligated to incur. Similarly, several utilities impose demand ratchets on private energy project customers when they rely on standby services. In doing so, the utility penalizes the customer in a manner that is inconsistent with the limited costs the customer imposes on the system, by carrying over, in some cases for an extended period, a level of demand that a private energy project customer ordinarily does not utilize.

In both instances, the distorted rates send inaccurate price signals to customers. Specifically, they discourage investment in private energy projects by obscuring the economic benefits of those projects and thereby encourage reliance on the monopoly service provider. If customers fail to see any differentiation in treatment between operating with a private energy project and operating without, there is little economic incentive to make the investments needed to pursue the project. This promotes inefficient and excessive investment by utilities and imposes significant added costs, through additional utility owned generation investment, on all ratepayers.

Several of the tariffs submitted by the energy utilities also fail to recognize that since PURPA was initially enacted, there have been significant changes in electricity markets. With the emergence of competitive regional markets in which capacity and energy are available for purchase through RTOs such as MISO and PJM, the need for a given monopoly utility to impose costs associated with additional, utility owned, capacity on a private energy project customer can

be significantly reduced, or even eliminated, if the customer has the option to buy such capacity at the market price rather than relying on utility resources to meet its needs during an outage. For a customer with a private energy project willing to operate with some degree of interruptibility, a tariff structured to allow a buy through option provides the customer greater choice and flexibility; allowing it to choose to reduce its consumption, buy through at market rates, or incur costs imposed by the utility depending on the existing economic signals and the customer's operational needs at the time of the outage. The expansion of customer flexibility to meet its own needs based on its own assessment of its operations should be encouraged as it serves as the best method of maximizing the efficient use of all resources.

## III. The Consequences of Non-Cost Based Standby Rates

As illustrated above, non-cost based standby rates send inaccurate price signals to consumers and discourage active investment in private energy projects as a resource. In part this can be seen through the low take up rate of private energy projects reported by the responding utilities. Based on the utilities own reporting, less than a dozen large customers take advantage of the suites of tariffs offered by the five investor owned utilities, with one investor owned utility reporting that it has no such customers.[8] IMPA reports that no member currently has a tariff which is purposefully designed to provide standby services to a cogeneration or renewable generation facility. The investment in private energy projects is, in addition, spread unequally throughout the State. Investment in private energy projects, however, should not depend on the

[8] Duke reports "two customers" who utilize the services offered by the company without specifying the size of those customers. I&M identifies two customers served under the company's "other sources of energy provision" or by special contract. All other I&M customers identified in its response are served by tariffs that limit the capacity of the private energy projects to 1MW or less. NIPSCO has "six (6) large industrial customers" served by Rider 776. Vectren identifies one customer served by its Rate BAMP. IPL reports it "has not provided nor is it currently providing" service under its private energy project riders.

service territory in which the customer's facility is located. All customers should have access to cost-based standby rates. Without them, investment in private energy projects will continue to be unequal, bringing its benefits in some sections of the State while impeding its growth in other areas.

Suppressed investment in private energy projects does have consequences. As noted above, private energy projects have been encouraged precisely because they offer a reliable, efficient, and economic generation resource. Further, investment in private energy projects can reduce the overall burden on all ratepayers by reducing total utility investment in its own generation resources. Failing to create cost-based standby rates plays a significant role in a company's decision not to proceed with investment in a private energy project. The inappropriate price signals sent by non-cost based standby rates discourages such investment and runs counter to established state policy.

At a time when new generation investment is necessary as existing plants age and are retired, private energy projects can play a key role in reducing utility investment in expensive generation resources. To encourage private energy projects, as is required by statute, the Commission should take reasoned and concrete steps to fulfill the statutory mandate that standby services be provided at non-discriminatory rates.

## IV. Policy Suggestions

In order to promote the development of reasonable and non-discriminatory standby rates, INDIEC recommends the Commission take the following steps.

- **Require revisions to existing standby rates to reflect cost-based principles**
    - Although each utility has unique characteristics, standby rates should reflect certain "best practices" in order to meet the non-discriminatory standard. These include charges based on the actual cost to serve a private energy project customer that reflect the expected outage rate of the facility serving the customer and the ability of a customer to schedule certain outages with the utility to avoid coincident peaks. Most importantly, such rates should not simply co-opt rates and tariff structures designed for full-requirements customers. Due consideration should also be given to reflect changing market forces that allow for capacity and energy to be purchased in competitive regional markets.
- **Mandate that such revisions be adopted uniformly across the State**
    - Failure to implement revisions to standby tariffs in all service territories picks winners and losers, placing customers in some service territories at a disadvantage simply due to location. Non-discriminatory standby rates, which reflect "best practices", should be available to customers in all service territories.
- **Recognize the benefits of increased use of private energy projects**
    - Unquestionably, Indiana is entering a build cycle as old plants are retired or significantly upgraded, and new plants constructed. In assessing the need for new generation, as well as its sizing, the Commission should take into account the

benefits of increased deployment of private energy projects in the IRP process and in other proceedings.

## V. Conclusion

A necessary step to encouraging the use of private energy projects as a resource is the development of cost based standby rates that send accurate price signals to customers utilizing or investigating such projects. The Commission, in reviewing the material submitted by the energy utilities, should be skeptical of standby service rates that mirror, or closely mimic, rates for full requirements customers and which unduly penalize private energy project customers by allocating costs far in excess of those that such customers impose on the system.

The deployment of private energy projects offers significant benefits to Indiana, including the potential to partially counteract a rising cost environment. The Commission should, accordingly, take appropriate and measured steps to further State and federal policy which recognizes those benefits and encourages the expansion of private energy projects.

Respectfully submitted,

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