BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Pacific Gas and Electric Company (U39E) for Approval of Demand Response Programs, Pilots, and Budgets for 2012-2014	Application 11-03-001 (Filed: March 1, 2011)
and Related Matters	Application 11-03-002 Application 11-03-003

COMMENTS OF THE CALIFORNIA INDEPENDENT SYSTEM OPERATOR CORPORATION ON THE ALTERNATE PROPOSED DECISION ADOPTING DEMAND RESPONSE ACTIVITIES AND BUDGETS FOR 2012 THROUGH 2014

The California Independent System Operator Corporation ("ISO") submits these comments regarding the Alternate Proposed Decision of Commissioner Ferron ("APD") adopting demand response activities and budgets for 2012 through 2014.[1] The ISO submits its comments pursuant to Rule 14.3 of the Commission's Rules of Practice and Procedure.

I. Introduction

The ISO agrees with many of the proposals contained in the APD and suggests certain minor revisions to the APD in these comments. In particular, the ISO believes that the APD appropriately describes the need for additional demand response as a flexible resource to meet the future energy needs of California and for integrating demand response into the wholesale energy markets. However, the ISO urges the Commission to promptly take action beyond that set forth in the APD, to explain its policy vision and outline the steps the Commission thinks necessary to significantly increase the development of demand response through the competitive market in order to align with the ADP's articulated policy that demand response should help integrate intermittent renewable resources.

Further, the Commission should extend the Aggregator Management Program ("AMP") contracts described in the APD for one year and should require that renegotiated AMP contracts be bid into the ISO market. The Commission should also expand policies stated in this APD that ensure the development of durable, generation-substitutable demand response resources that fulfill the spirit of the loading order and can be procured and planned on like other resource

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1 *[Alternate Proposed] Decision Adopting Demand Response Activities and Budgets for 2012 Through 2014*, issued on March 20, 2012, accessible on the Commission's website at http://docs.cpuc.ca.gov/efile/ALT/162146.pdf. The APD is an alternate proposed decision to the *[Proposed] Decision Adopting Demand Response Activities and Budgets for 2012 Through 2014*, issued on October 28, 2011 ("PD"), accessible on the Commission's website at http://docs.cpuc.ca.gov/word_pdf/AGENDA_DECISION/155437.pdf.

types. Lastly, the Commission should revise the APD to incorporate language from the original PD regarding allocation of demand response costs.

II. The APD Appropriately Describes the Need for Additional Demand Response to Meet California's Future Energy Needs

The ISO appreciates and agrees with the statements in the APD that demand response is more than just a tool for addressing emergency conditions and reducing peak load, but is also a flexible resource whose attributes can help pave the way to California's clean energy future by enabling the integration of large numbers of renewable resources into the markets operated by the ISO. For example, the APD states:

> The California Clean Energy Future plan expressly acknowledges that in addition to its historic role as an emergency and peak demand management tool, DR [demand response] will be able to provide a range of services that can support grid integration of large quantities of intermittent and variable renewable resources. The plan also articulates our collective commitment to integrating DR into the CAISO's wholesale energy markets.[2]
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> Looking ahead to our pursuit of SB 1X's requirement that the Utilities obtain 33% of the energy they deliver from renewable resources in 2020, we also expect that DR will likely be called upon to meet new needs beyond its historic role as an emergency resource and peak shaving tool. DR is ideally suited to support grid integration of renewable generation, much of which will be intermittent or variable.[3]

These statements in the APD are important for understanding and interpreting California's foundational loading order and for evaluating and approving future demand response programs.[4] The APD is consistent with the position of the ISO that the loading order does not simply promote *any type* of demand response that is deemed cost-effective, but, rather, that the loading

[2] APD at p. 13.

[3] *Id.* at pp. 76-77.

[4] As explained in the APD, "[f]or more than a decade, California's energy and air quality agencies have recognized the vital role of DR in meeting our shared responsibilities to provide clean, safe and reliable energy at reasonable rates. The foundational principal is . . . California's loading order policy, adopted by California energy agencies in the 2003 Energy Action Plan and reiterated in the Energy Action Plan II." *Id.* at pp. 11-12.

order promotes resources that can meet California's "growing energy needs."[5] As the APD makes clear, satisfying California's future energy needs through extremely use-limited demand response and emergency load shedding is not a satisfactory interpretation of the loading order.

III. The Commission Must Take Action to Explain Its Policy Vision and the Steps Necessary to Increase the Development of Demand Response Through the Competitive Market

The ISO appreciates the recognition in the APD that third-party demand response providers can supply the innovation needed to fulfill the goals of the loading order – specifically by providing new demand response innovations, products, and services that will help meet California's growing energy needs. However, as discussed below, the Commission should take more action than is envisioned in the APD to promote third-party supply of demand response.

The APD acknowledges that having third parties operating in the competitive market can deliver demand response products and services in ways that are "superior to the Utilities' abilities":[6]

> We noted however that "Acting expeditiously to allow end use customers or aggregators to bid DR resources directly in [CAISO's] markets . . . is consistent with our identification of DR as one of the state's preferred means of meeting growing energy needs."[7]
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> We think that third party aggregators can provide additional innovation and services to the market, yielding additional uncaptured potential benefits to DR in California.[8]
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> . . . .
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> As customers are being transitioned to other programs because of the termination of PeakChoice [the PeakChoice program operated by Pacific Gas and Electric

5 *Id.* at p. 15 (citation omitted).

6 *Id.* at p. 122.

7 *Id.* at p. 15 (citation omitted).

8 *Id.* at pp. 16-17.

> Company ("PG&E")] we encourage the MWs to be transitioned to third party contracts, when feasible, <u>because we envision that their ability to address customers' needs will be superior to the Utilities' abilities</u>.[9]
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> . . . .
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> The changing nature of the electrical grid, which we previously discussed, has generated additional requirements that call into question whether a utility-centric model for DR programs and services can meet current and future needs.[10]

As this discussion in the APD makes clear, the Commission questions the robustness of the utility-centric model and envisions greater customer benefits and demand response innovations can be provided through the competitive market rather than through the existing utility-centric delivery model. It would seem to follow from this discussion that issuing directives that promote the establishment of a competitive demand response market, such as requiring more competitive solicitations for demand response resources in the current application cycle, would be positive first steps. The APD, however, does not propose any such steps. Instead, the APD continues to promote significant investment in demand response almost exclusively through the utility-centric model, and encourages, but does not require, a transition to third-party supply of demand response, and then only in limited cases. Consequently, even though the Commission acknowledges the benefits of a competitive market for demand response, it does not take any definitive steps in the APD to evolve the existing utility-centric paradigm. The Commission defers any such steps to a future rulemaking.

In this regard, the Commission asserts in the APD that it must determine the future goals and policy objectives for demand response before it addresses competitive market issues:

> Dismantling of the utility-centric model, as suggested by some parties in this proceeding, requires thought and deliberation beyond the time provided in the current proceeding. Furthermore, the issues go beyond the three-year cycle of a DR Application and are more appropriately addressed in the DR rulemaking. <u>The</u>

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9 *Id.* at p. 122 (emphasis added).

10 *Id.* at pp. 188-89.

> Commission must determine the future goals and policy objectives for DR before addressing these issues. At this time, however, the most prudent path forward is to continue to gather information to develop a better record before making lasting changes to the current structure. We will address these issues in the DR rulemaking proceeding, R.07-01-041 or its successor.[11]

The APD does signal that the Commission holds a policy vision that demand response needs to be integrated into the ISO market.

> For the reasons discussed above, and consistent with our policy vision on integration into and direct participation of DR resources in the CAISO market, we deny PG&E's request for an RFP for new AMP contracts. Instead, we adopt the DR procurement model as proposed by the CAISO. The specifics of the DR procurement model will be further developed in the current DR Rulemaking proceeding, R.07-01-041, or its successor. We expect the Utilities to hold competitive solicitations for new PDR contracts as a part of their Resource Adequacy portfolio, once we have finalized the direct participation rules and implemented new Resource Adequacy rules for wholesale DR resources. We require the Utilities to work closely with CAISO, Commission Staff, and the Procurement Review Groups when developing the RFP requirements to meet future system needs, e.g., integration of renewable resources.[12]

The ISO is encouraged by this policy statement. However, because the above statement claims that the "Commission must determine the future goals and policy objectives for DR before addressing these [competitive market] issues," the ISO urges the Commission to establish and articulate its future goals and policy objectives for demand response to resolve these somewhat conflicting statements within the APD that recognize the benefits of the competitive market and direct participation, yet hold back from taking affirmative action until future goals and policy steps are determined.

In this and other application cycles, the Commission has authorized hundreds of millions of dollars be invested in demand response, yet it does not appear to have a clear or updated objective as how this significant investment helps project demand response along a particular path to achieve the Commission's energy policy goals. To shape and guide the demand response

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11 *Id.* at p. 190 (emphasis added).

12 *Id.* at pp. 187-88.

discussion, the ISO encourages the Commission to direct the Energy Division to draft a demand response paper that captures the Commission's preferred goals, policies, and principles for demand response as a priority resource. This paper could then be made available for discussion and comment by interested parties. The demand response paper should ultimately be reviewed and sanctioned by the Commission. For the engaged parties, such a paper would provide important guideposts for new proposals and programs that align with the Commission's demand response policy vision.

IV. The Commission Should Extend the AMP Contracts for One Year and Should Require that Renegotiated AMP Contracts Can Be Bid into the ISO Market

The ISO supports extension of the AMP contracts for one year while the Commission and interested parties complete and conclude the direct participation rules.[13] Thus, the ISO encourages the Commission to implement the direct participation phase in its demand response rulemaking proceeding (R.07-01-041) ("Demand Response Proceeding"), so that clear objectives for demand response can be set and third-party demand response providers can begin to competitively develop flexible, ISO-integrated demand response resources in earnest in 2013.

As to implementation of the direct participation phase, the ISO notes the following statement in the APD:

> Moreover, as we anticipate that we will expect the Utilities to rely more on competitive provision of DR services once we do open up Direct Participation, we find that it is prudent to maintain the presence of Third Party Aggregators during this transitional period.[14]

The Commission should clarify in the APD that, if PG&E elects to extend the current AMP contracts beyond 2012, any renegotiation between PG&E and the third-party demand response aggregator must ensure that the underlying demand response which is the subject of the AMP

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[13] *See id.* at p. 71.

[14] *Id.* at p. 72.

contracts can be bid directly into the ISO market. This clarification would be consistent with the following statements in the APD:

> [I]f PG&E elects to extend the current AMP contracts beyond 2012, it must renegotiate the terms of the contracts to improve their cost-effectiveness, increasing the TRC [Total Resource Cost] ratio to be cost effective as set forth in this decision.[15]
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> . . . .
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> As discussed above, we agree with the Applicants and parties that the Commission should preserve the DR resources from current and future AMP contracts because they can be bid into the CAISO market.[16]

V. The Commission Should Take Steps to Promote Durable Demand Response Products

The APD should direct the restart of phase 4 of the Demand Response Proceeding. Restarting phase 4 is necessary to permit the establishment of rules that will enable durable demand response products to be developed and offered to customers. Such durability is extremely important. As explained in the APD:

> While we regard DR as a substitute for generation and are pursuing efforts to ensure that it can compete on equal terms, we recognize that DR and generation are produced in fundamentally different ways. Power plants are long-lived physical assets, which can generally be expected to remain available even if idled or mothballed during periods of excess capacity. While DR resources require some investment in software and equipment, <u>they depend to a great degree upon investments in human capital and management decisions that are easily reversed. The shorter procurement timeframe for DR resources raises the specter of a stop-start-stop-start cycle that may discourage investment by participants and aggregators alike</u>. We wish to avoid such an outcome and intend instead to continue to develop dependable and sustainable DR resources that will be viable substitutes for generation as the reserve margin begins to close later in this decade.[17]

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15 *Id.* at p. 75.

16 *Id.* at p. 76.

17 *Id.* at pp. 72-73 (emphasis added).

The challenge presented by the type of stop-start-stop-start cycle described in the APD is that the ISO, as a system operator, must perform system planning, and resources do not readily fit into resource planning efforts and studies if they "cycle in and out" and if their performance is too uncertain over time they may not be sufficiently "reliable" for system planning purposes. The ISO performs resource planning with the expectation that the resource portfolios studied are reasonably durable, viable, and effective, and will be around for the following year or years. Thus, durability is a critical attribute that demand response must demonstrate, especially when California is considering thousands of megawatts of demand response to be in production by 2020 and it is to be one of the state's preferred means of meeting growing energy needs.

VI. The Commission Should Revise the APD to Incorporate Language from the PD Regarding Allocation of Demand Response Costs

The October 28, 2011 PD included an important point regarding allocation of demand response costs that has not been retained in the APD. Specifically, the PD explained in the following underlined language that issues regarding demand response cost allocation should be addressed in a consistent manner across the three investor-owned utilities ("IOUs") and are best handled in the Demand Response Proceeding:

> Moreover, until the Commission makes a final determination about the future structure of the DR market, changing the current cost recovery and rate design process for DR is not ripe for discussion. Normally, in order for the Commission to consider DACC and AReM's proposal to restructure rates, we would require additional data and fact finding studies that are best handled in rate design. <u>However, we agree that these issues should be considered in a consistent manner across all three utilities and thus are best handled in one proceeding, the DR Rulemaking, 07-01-041 or its successor</u>.[18]

[18] PD at p. 207 (emphasis added). The PD is accessible on the Commission's proceeding website at http://docs.cpuc.ca.gov/word_pdf/AGENDA_DECISION/155437.pdf.

The APD, by comparison, included all of this quoted language except for the underlined language.[19]

The ISO has stated in this proceeding that before a viable competitive demand response market can be established, the Commission must address the issue of how demand response costs will be allocated. If the IOUs are allowed to spread demand response program costs to all distribution service customers, but a demand response provider is only able to spread such costs to its participating customers, this creates an un-level and anti-competitive playing field.

Therefore, the ISO submits that the APD should be revised to incorporate the original underlined language from the PD that the APD had omitted. The principle of cost allocation is best handled consistently across all three utilities as cost allocation is not only a major policy issue but is also a challenge for the development of a competitive demand response market. The ISO believes it is inappropriate to address the principle of demand response cost allocation in separate and disparate general IOU rate case proceedings. This issue is too significant to not resolve head-on in a single proceeding.

VII. Statewide DR Marketing / Flex Alert Campaign Funding for 2012 is Appropriate

The ISO appreciates the Commission's attention to evaluating the funding amounts for the statewide demand response marketing and Flex Alert campaign. The ISO appreciates the APD's inclusion of additional funding levels for 2012, and believes that the additional funding will appropriately continue to provide critical public awareness about the need to conserve energy during periods when the system is highly stressed. The Flex Alert campaign and "Flex Your Power"™ brand is known and recognized by California energy users, and has served as an effective and valuable tool for the grid operator to seek load relief through statewide and regional energy conservation messaging when it is needed most.

[19] APD at p. 203.

The ISO also appreciates that the APD provides for consideration of statewide Marketing, Education & Outreach in its own proceeding, rather than relegating the matter to either the Energy Efficiency or Demand Response application proceedings. This procedural path will give these funding issues the attention they merit and will prevent them from being subsumed in the many other important issues to be resolved in the demand response and energy efficiency proceedings.

VIII. Conclusion

The ISO respectfully requests that the Commission consider the comments provided above in its determinations regarding the APD.

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Respectfully submitted,

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APPENDIX A

Appendix A to ISO Comments on
Alternative Proposed Decision of Commission Ferron
adopting demand response activities and budgets for 2012 through 2014

<u>Requested Modifications to the APD</u>

I. Issues Regarding Allocation of Demand Response Costs

Within **Section 10 [Cost Recovery]**, in the second paragraph at page 203, the ISO requests the following underlined additions:

> Moreover, until the Commission makes a final determination about the future structure of the DR market, changing the current cost recovery and rate design process for DR is not ripe for discussion. Normally, in order for the Commission to consider DACC and AReM's proposal to restructure rates, we would require additional data and fact finding studies that are best handled in rate design. <u>However, we agree that these issues should be considered in a consistent manner across all three utilities and thus are best handled in one proceeding, the DR Rulemaking, 07-01-041 or its successor</u>.