Op-Ed

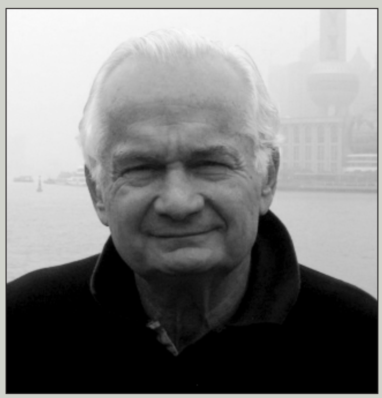
What Happened in Maryland

State case has national implications for grid modernization.

By William A. Mogel

Seemingly swimming upstream to a national policy, backed by $3.4 billion in federal funds from the *American Recovery and Reinvestment Act* incenting the smart grid[1], the Maryland Public Service Commission, in a unanimous 54-page decision, in *Baltimore Gas and Electric*, Case No. 9208 (June 22, 2010) denied recovery of $835 million in costs for deployment of smart grid initiatives. The PSC, in rejecting a surcharge proposed to be collected via a tracker, stated:

> Although we share… hopes and even enthusiasm, for the long run potential and importance … of the "smart grid"… [t]he Proposal asks BGE ratepayers to take significant financial and technological risks and to adapt to categorical changes in rate design, all in exchange for savings that are largely indirect, highly contingent and a long way off…
>
> The tracker virtually guarantees that the Company will recover from ratepayers the prudently incurred costs associated with the Proposal, a profit for its investors, and a portion of certain projected benefits, if they are realized. [W]ith the tracker in place, the Proposal is a "no-lose proposition" for the Company and its investors.



"The regulatory process should reward efforts to modernize the electric system."

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Despite the foregoing, the PSC invited the utility to submit an alternate proposal, keeping in mind the "core principle that utilities recover the cost of infrastructure investments through distribution rates." [Editor's note: The utility did so in July, and the PSC conditionally approved BGE's revised filing in August.]

National Implications

BGE raises several important questions. First, does this decision have national implications? The answer is yes. The costs associated with smart grid technology—some of which might not be proven fully—need to be reviewed by regulators by a standard that departs from strict application cost-of-service regulation. The PSC should've been willing to do this, especially when the utility made a showing of benefits including conservation, energy and capacity price mitigation, and avoided capital expenditures. According to BGE, the net-present value of the benefits was $1 billion.

One solution other than authorizing a pilot project is to require that the utilities' new technology expenditures are subject to annual prudence reviews. Thus, one of the main concerns of the PSC, that the risk of the smart grid was being shifted to ratepayers, would be answered. The risk would be to the utilities if the benefits didn't materialize as projected.

A second question: is *BGE* a rejection of the smart grid? Yes, in the short-term, the PSC only gave lip service to its enthusiasm for the smart grid, which has been described as follows:

> The smart grid promises increased flexibility and creates new possibilities for customers and utilities…
>
> Customers want to have better control of their electric usage and bills and … want to be able to choose their energy sources. Utilities need to provide reliable service while minimizing cost. Utilities also need to easily integrate wind and solar energy and to provide service for new uses as they emerge.[2]

The PSC, "while strongly supporting the overall goals of BGE's Proposal" concluded, "[T]he Company's business case raises serious doubts regarding whether the Proposal is…a cost-effective means of reducing consumption and peak demand of electricity in Maryland."

A final question is, did the PSC fairly consider all stakeholder interests in the regulatory process? It did not. In addition to ratepayers, whom it sought to protect from costs for *(Cont. on p. 12)*

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investments with only the possibility of future benefits, the PSC had an obligation to consider the impact of its decision on the regulated entity. Here, BGE like most utilities, was seeking to transform its operations, with the newest technologies, in order to ultimately benefit its customers. By rejecting the smart grid proposal, the PSC was ignoring application of national energy policy intended to encourage modernization of utilities and efficient use of electric power. Finally, the PSC ignored the role of utilities' shareholders and lenders. If investment and lending are to be stymied by regulation, the ability of a utility to raise capital to improve service to consumers will be impaired.

Grid Modernization

At the risk of unfairly labeling the PSC's strict adherence to cost-of-service regulation as Luddite, the regulatory process should reward efforts to modernize U.S. electric systems. More than 60 years ago, the U.S. Supreme Court recognized that ratemaking calls for certain "pragmatic adjustments" and that it is "not the theory but the impact of the rate order which counts."[3] Here, the impact of the PSC's decision is to delay implementation of a new technology that promises customer choice, efficiency and conservation.

Endnotes:

1. M. Troutman *Wall Street Journal* A.3 (July 26, 2010).
2. A. Kressener, *Smart Grid Flexibility*, 7 Energy Biz 56 (2010). It is estimated that of the 140 million electric meters in the United States, 40 million are "smart." *Wall Street Journal* R.7 (Sept. 13, 2010).
3. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602-603 (1944).