The Utility Business Model Going Forward: Policy, Perception, and Risk Considerations

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Characteristics of Ancien Regime

- Limited Upside Potential
- Asymmetric Downside Risks
  - E.g. Open Ended Obligation to Serve
- Absence of Meaningful Price Signals
- Limited Spectrum for Socializing/Privatizing Risks
- Bundled non-Discreet Services and Incentives
Critical Industry Changes

• Rapidly Changing Technology
• Changing Nature of Consumer Needs and Demands (e.g. varying reliability, back up, etc.)
• More Consumer Options
• More Diverse Resource Options (e.g. Distributed Generation)
• Greater Awareness of Externalities
Emergence of Competition and Unbundling

- Potential of Service Specific Focus:
  - Generation
    - micro/macra
    - renewable/non-renewable
    - capacity/energy
  - Transmission
  - Distribution
  - Energy sales
  - Metering and billing
  - Demand side services
    - demand response
    - energy efficiency
Customer Perceptions of Utility

- More Consistent with *Ancien Regime* than Current Reality
- Results in Undervaluing Core Services
Core vs. Non-Core Services

- Core: Transmission and Distribution
- Non-core: Everything else
- Who is Best Positioned to Perform/Manage Core Services?
- Who is Best Positioned to Perform/Manage non-Core Services?
Dangers of Mixing Core and non-Core Services
Erosion from Core Services Revenue Example: Net Metering

- Inefficient Pricing of Distributed Generation
- Treating More Costs as Fixed
- Diluting Efficient and “Green” Price Signals
- Socially Regressive Allocation of Revenue Responsibility
- Inefficient Resource Allocation
- Subsidizing Inefficiency
Misalignment of Risks and Rewards (Example: Smart Meters)

- Risks and Risk Allocation
- Technology Risks (Telephony Visits Electricity)
- Recovering Costs of Assets Whose Technological Obsolescence Occurs Prior to its Physical Demise
- Keeping Pace with Rapidly Changing Technology
- Lost Revenue Risks (Decoupling Sales and Revenues)
- Customer Resistance to Smart Meters
Risks and Risk Allocation cont’d

- Who is Best Equipped to Cope with Risks:
  - Utilities and Alternative Supplier Perspectives
  - Risk Minimization or Benefit Maximization
  - Regulatory Considerations (e.g. Depreciation Schedules) Recovery
  - Fear of Stranded Costs
  - Regulatory Pre-Approval
  - Symmetry Between Risk and Control (Socializing Risks)
  - Managers or Regulators Making Technology Choices
  - Agility in Responding to Change
  - Regulatory or Customer Focus
  - Best Positioned to Capture Supply Side Benefits?
  - Best Positioned to Capture Demand Side Benefits?
  - Best Positioned to Seize Innovation Opportunities?
Conclusion

- Greater Unbundling of Services
- Service Specific Focus
- Limit Utilities to Core Services
- Open Market for non-Core Services