

BEFORE THE PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

-----In the Matter of----- )  
 )  
PUBLIC UTILITIES COMMISSION )  
 )  
Instituting a Proceeding to )  
Investigate Distributed Generation )  
in Hawaii. )  
\_\_\_\_\_ )

DOCKET NO. 03-0371

ORDER NO. 22375

Filed April 6, 2006  
At 11 o'clock A.M.

Karen Digest.  
Chief Clerk of the Commission

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ORDER

By this Order, the commission grants in part and denies in part the Motion for Clarification and/or Partial Reconsideration of Decision and Order No. 22248, filed on March 1, 2006 (the "Motion for Clarification"), by HAWAIIAN ELECTRIC COMPANY, INC. ("HECO"), HAWAII ELECTRIC LIGHT COMPANY, INC. ("HELCO"), and MAUI ELECTRIC COMPANY, LIMITED ("MECO") (collectively, the "HECO Utilities" or "Companies").<sup>1</sup> In Decision and Order No. 22248, the commission anticipated that there may be a need in the future to further refine and detail certain requirements established and described in Decision and Order No. 22248, as may be required by specific circumstances involving distributed generation projects to be considered by the commission. Nonetheless, as the commission understands the need

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<sup>1</sup>The Parties of record in this investigative proceeding are: the HECO Utilities, KAUAI ISLAND UTILITY COOPERATIVE ("KIUC"), the DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS, DIVISION OF CONSUMER ADVOCACY ("Consumer Advocate"), LIFE OF THE LAND ("LOL"), HAWAII RENEWABLE ENERGY ALLIANCE ("HREA"), HESS MICROGEN, LLC, and the COUNTY OF MAUI. The COUNTY OF KAUAI is the sole Participant.

for certain points to be clarified prior to the consideration of applications for specific projects, the commission herein partially grants and partially denies the motion to the extent it requests clarification of certain portions of Decision and Order No. 22248, and denies the motion to the extent it requests any reconsideration of Decision and Order No. 22248.

I.

Background

On January 27, 2006, the commission issued Decision and Order No. 22248, "set[ting] forth certain policies and principles for the deployment of distributed generation in Hawaii and certain guidelines and requirements for distributed generation, some of which will be further defined by tariff as approved by the commission."<sup>2</sup>

On March 1, 2006, the HECO Utilities filed their Motion for Clarification and/or Partial Reconsideration of Decision and Order No. 22248, with copies served on the other parties and Participant.<sup>3</sup> The HECO Utilities also requested a hearing on

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<sup>2</sup>Decision and Order No. 22248, filed on January 27, 2006, at 1.

<sup>3</sup>HECO Utilities' Motion for Clarification and/or Partial Reconsideration of Decision and Order No. 22248, Memorandum in Support of Motion ("Memorandum"), Affidavit of Scott Seu, Affidavit of Timothy Hill, and Certificate of Service, filed on March 1, 2006 (collectively, "Motion for Clarification"). See also HECO Utilities' letter, dated March 6, 2006, with enclosure.

On February 8, 2006, the HECO Utilities filed a "Motion for Enlargement of Time to File [a] Motion for Clarification and/or Motion for Reconsideration of Decision and Order No. 22248." The HECO Utilities requested an enlargement of time until March 1, 2006, to file a motion for clarification and/or reconsideration,

their Motion for Clarification, in accordance with Hawaii Administrative Rules ("HAR") § 6-61-41(f), or in the alternative, oral argument consistent with HAR § 6-61-142. On March 7, 2006, the commission: (1) set a deadline of March 22, 2006, for the other parties and Participant to file responses, if any, to the HECO Utilities' Motion for Clarification; and (2) denied the HECO Utilities' request for a hearing either to provide additional evidence or oral argument, subject to reconsideration upon the commission's own motion.<sup>4</sup>

Timely responses were filed by HREA on March 20, 2006, and the Consumer Advocate on March 22, 2006.<sup>5</sup>

This Order addresses the HECO Utilities' Motion for Clarification.<sup>6</sup>

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if any. On February 13, 2006, the commission granted the HECO Utilities' request for an enlargement of time until March 1, 2006, to file a motion for clarification and/or reconsideration of Decision and Order No. 22248. See Order No. 22283, filed on February 13, 2006.

<sup>4</sup>See Order No. 22310, filed on March 7, 2006.

<sup>5</sup>HREA's Response to HECO's Motion for Clarification; and Certificate of Service, filed on March 20, 2006 (collectively, "HREA's Response"); and Consumer Advocate's Comments on HECO's Motion for Clarification; and Certificate of Service, filed on March 22, 2006 (collectively, "Consumer Advocate's Response").

<sup>6</sup>The Consumer Advocate agrees with the HECO Utilities' assessment that the requested relief can be accommodated within the "four corners" of Decision and Order No. 22248. See Consumer Advocate's Response, at 2; see also HECO Utilities' Motion for Clarification and/or Partial Reconsideration of Decision and Order No. 22248, at 2.

II.

Discussion

Hawaii Administrative Rules ("HAR") chapter 6-61, subchapter 14, governs the filing of motions seeking any change in a commission decision or order. HAR § 6-61-137 of subchapter 14, provides:

§6-61-137 Motion for reconsideration or rehearing. A motion seeking any change in a decision, order, or requirement of the commission should clearly specify whether the prayer is for reconsideration, rehearing, further hearing, or modification, suspension, vacation, or a combination thereof. The motion shall . . . set[] forth specifically the grounds on which the movant considers the decision or order unreasonable, unlawful, or erroneous.

HAR § 6-61-137.

In general, the HECO Utilities seek clarification and/or reconsideration of: (1) the conditions applicable to regulated utility ownership of customer-sited distributed generation; and (2) the applicability of Decision and Order No. 22248 to renewable forms of distributed generation. In brief, the HECO Utilities assert:

. . . . D&O 22248 provides only limited guidance as to how the Commission intends to apply the three conditions for utility ownership of customer-sited DG, and whether it intends to differentiate in its application of the conditions based on fundamental factors that are not extensively discussed in the decision, such as the DG application at issue, or the size of the DG installation relative to the utility system. Thus, if the Commission deems the requested relief to go beyond the conditions specified in the D&O, the Companies respectfully request, in the alternative, that the Commission reconsider the

scope of the conditions, and allow the utilities to proceed on the basis outlined in [their] motion . . . . .

HECO Utilities' Motion for Clarification, at 2.

. . . . . The Companies do not request reconsideration of any of the listed actions [in Decision and Order No. 22248], and will attempt to implement the actions required by the D&O in the time frame contemplated. The Companies do request, however, a minor clarification as to the potential applicability of standby rates to renewable DG, . . . and have provided comments regarding the feasibility of acquiring peaking dispatch rights in interconnection agreements[.]

. . . . . The Companies do have some concerns regarding the balance of interests under the Commission's DG competition policy, but are not requesting reconsideration of the basic policies or conditions established in the D&O . . . . . Rather, the Companies request clarification as to the scope and applicability of the three conditions (or in the alternative, partial reconsideration of the conditions)[.]

HECO Utilities' Memorandum, at 2 (emphasis in original). See also id. at 2 - 27.

A.

Ownership of Distributed Generation

Section II.B of Decision and Order No. 22248, relating to the ownership of distributed generation, concludes in part:

If the utility wishes to sell distributed generation services as a regulated utility, the utility must show, in an application filed with the commission, the following:

- (a) the distributed generation resolves a legitimate system need;
- (b) the distributed generation proposed by the utility is the least cost alternative to meet that need; and

- (c) in an open and competitive process acceptable to the commission, the customer-generator was unable to find another entity ready and able to supply the proposed distributed generation service at a price and quality comparable to the utility's offering.

The commission may establish further detailed guidelines on the foregoing application requirements by rule or order, if circumstances indicate that these requirements are insufficient to achieve the goals described in this Decision and Order.

By establishing the preceding conditions to utility participation in the distributed generation market, the commission seeks to allow utility participation to address immediate system needs when required in a manner that minimizes the possibility that utility participation will impede entry of new competitors in the immediate and longer term.

Decision and Order No. 22248, at 22 - 23 (emphasis added). See also id. at 20 and 46, Ordering Paragraph No. 2. As noted above, the commission anticipated that there may be a need in the future to further refine and detail these application requirements as may be required by specific circumstances and projects to be considered by the commission.

The HECO Utilities seek clarification as to how requirements (a), (b), and (c) will be administered, to confirm that their understanding of the decision is consistent with the commission's understanding.<sup>7</sup> As the commission understands the need for certain matters to be clarified prior to the consideration of applications for specific projects, the

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<sup>7</sup>HREA, in response, reiterates its general opposition to the "installation and operation of utility-owned, renewable DG on customer-sites." HREA's Response, at 3.

commission herein clarifies certain portions of Decision and Order No. 22248.

1.

Requirement (a): Legitimate System Need

a.

Benefits of Distributed Generation  
Identified in Decision and Order No. 22248

The HECO Utilities note that while Decision and Order No. 22248 does not explicitly define "legitimate system need," they explain that Section II.C (at 23-25) of the decision cites to a number of benefits of distributed generation, including:

1. Additional electrical generation capacity;
2. Deferring the need to deploy certain facilities such as lines and transformers, on the transmission system and distribution system, which may be needed to avoid overloads, under contingency and projected peak conditions;
3. Reducing system transmission and distribution line losses and providing voltage support;
4. Improving system energy efficiency; and
5. Increasing the use of renewable energy technologies in order to reduce the burning of fossil fuels and to meet renewable energy portfolio standard ("RPS") requirements.

The HECO Utilities state that "[e]ach of these is a legitimate need from the utility system perspective[, and] . . .

request that the Commission confirm this interpretation of system need."<sup>8</sup>

The Consumer Advocate supports the HECO Utilities' request in this regard and agrees that the identified benefits may support a finding that utility-owned customer sited distributed generation fulfills a system need. Nonetheless, the Consumer Advocate states that "the Commission should only provide the confirmation requested by the [HECO Utilities] that the above may support a finding that the utility-owned customer sited DG project fulfills a 'system need' and reiterate the utility's responsibility to demonstrate that the proposed project meets this criteria."<sup>9</sup> The Consumer Advocate reasons that the evaluation as to whether a specific proposed utility-owned distributed generation project meets the system need criteria must be based on the specific information contained in the application seeking the commission's approval to proceed with the project.

HREA contends that:

1. In reply to the HECO Utilities' argument that providing additional electrical generation capacity should qualify as a legitimate system need, HREA believes that the commission "means providing additional electrical generation capacity when and where it is needed on the system to meet system needs[,]" which is a public utility's primary role.<sup>10</sup> Conversely,

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<sup>8</sup>HECO Utilities' Memorandum, at 3 - 4.

<sup>9</sup>Consumer Advocate's Response, at 3 - 4.

<sup>10</sup>HREA's Response, at 3.

the utility's provisioning of "energy services, including [distributed generation], for a specific customer on the customer-side of the meter is not. Provision of such services is the role of a private utility[.]"<sup>11</sup>

2. Increasing the use of renewable energy technologies in order to reduce the burning of fossil fuels and to meet RPS requirements is a legitimate system need in situations where the renewable capacity is "firm" and utilized to meet peak loads. Conversely, the "purchase of as-available renewable power to meet RPS as a legal need, thus avoiding potential fines, [does] not meet[] a legitimate system need."<sup>12</sup>

The commission finds that the HECO Utilities' broad paraphrasing of the identified benefits of distributed generation into "providing additional electrical generation capacity" is much too expansive, and was not described as such in Section II.C of Decision and Order No. 22248. If the HECO Utilities' interpretation is adopted, any distributed generation project would qualify as satisfying a legitimate system need.

Having considered the request of the HECO Utilities, and the positions taken by the Consumer Advocate and HREA, the commission clarifies and confirms that "legitimate system need" as used in Decision and Order No. 22248 may include the benefits of distributed generation as described in Section II.C of Decision and Order No. 22248, and may support a finding that

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<sup>11</sup>HREA's Response, at 3.

<sup>12</sup>HREA's Response, at 3.

utility-owned customer-sited distributed generation fulfills a legitimate system need.

The commission, however, agrees with the Consumer Advocate that the utility has a responsibility to demonstrate that the proposed project meets all applicable criteria. The evaluation as to whether a specific proposed utility-owned distributed generation project meets the legitimate system need criteria must be based on the specific information contained in the application for commission approval to proceed with the project. Accordingly, the applicability of any one or more of the benefits of distributed generation identified in Section II.C of Decision and Order No. 22248 should not in and of itself be construed as a guarantee of a finding of a legitimate system need.

b.

Portfolio Perspective

The HECO Utilities also "request clarification as to whether a portfolio perspective may be used when judging whether broader system needs, such as for generating capacity or for renewable energy, are being 'resolved' by a DG project."<sup>13</sup> As they explain:

A portfolio approach, wherein a DG project is considered in an aggregated fashion with other DG systems, and other supply-side and demand-side resource options, is more appropriate when considering such system needs. This is because, with few exceptions, from a capacity planning

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<sup>13</sup>HECO Utilities' Memorandum, at 4.

perspective, no single DG project will provide meaningful contribution to deferring the need for additional central station generation. Similarly, an individual renewable DG project such as a 100 kW photovoltaic ('PV') system will not have a noticeable effect on meeting RPS targets.

HECO Utilities' Memorandum, at 4.

The Consumer Advocate concurs with the HECO Utilities' concern, noting that "it may be appropriate to consider DG projects considered in an aggregated fashion when considering such system needs are met as well as when determining whether a project is cost-effective and the 'lowest reasonable cost' solution."<sup>14</sup>

Having considered the request of the HECO Utilities and the position taken by the Consumer Advocate, the commission clarifies and confirms that a portfolio perspective may be used to help support a finding that utility-owned customer-sited distributed generation projects fulfill a legitimate system need. The commission reiterates, however, that the utility has a responsibility to demonstrate that the proposed project or projects meet all applicable criteria. The evaluation as to whether a specific proposed utility-owned distributed generation project meets the legitimate system need criteria must be based on the specific information contained in the application for commission approval to proceed with the project.

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<sup>14</sup>Consumer Advocate's Response, at 7.

2.

Requirement (b): Least Cost Alternative

The HECO Utilities seek clarification that the term "least cost" in requirement (b) means the same as "lowest reasonable cost," as used in Section II(A) of the commission's Integrated Resource Planning ("IRP") Framework, dated May 22, 1992:

II. Introduction

A. Goal of Integrated Resource Planning

The goal of integrated resource planning is the identification of the resources or the mix of resources for meeting near and long term consumer energy needs in an efficient and reliable manner at the lowest reasonable cost.

Section II(A) of the IRP Framework, dated May 22, 1992, at 3 (emphasis added).

The HECO Utilities explain:

A 'lowest reasonable cost' standard would allow greater flexibility and provide a broader means to consider resource options that may provide additional value to the system or customer, as is the case with DG. A DG option may not be the 'lowest cost' alternative in the strict sense of the wording, but may be preferred for other attributes and value that it delivers to the host customer, the system, and/or other ratepayers (e.g., any of the various benefits of DG described in Section II.C. of the D&O). As in other matters or projects for which the regulated utility seeks Commission approval, the burden would be on the utility to show that its DG expenditures are prudent, reasonable, and in the interests of ratepayers.

Finally, . . . if a resource portfolio perspective can be taken in considering a DG project and its use to meet a system need, then

that perspective should also be allowed in considering the project's cost-effectiveness.

HECO Utilities' Memorandum, at 5.

The Consumer Advocate supports the HECO Utilities' request and "believes that the Commission intended to utilize 'lowest reasonable cost,' as opposed to 'least cost' as the planning standard criteria for evaluating utility ownership of customer-sited DG."<sup>15</sup>

HREA agrees that clarification of the term "least cost" is needed, but it does not believe that the HECO Utilities' interpretation is necessarily correct. In HREA's view, the term "least cost" must meet the commission's stated goal of ensuring that distributed generation that is not cost-effective does not enter the utility's system.

The request of the HECO Utilities that the commission clarify the meaning of "least cost" to mean "lowest reasonable cost" as used in Decision and Order No. 22248 is reasonable. The term "lowest reasonable cost" is consistent with the standard used in the IRP Framework and the commission agrees that it would allow greater consideration of resource options that may provide additional value to the system, but may not strictly qualify as the least cost option in monetary terms. The commission agrees with HREA that the commission should not accept a proposal that is not cost-effective. The commission believes that the utility's obligation, set forth in Section II.B of Decision and Order No. 22248, to show that "in an open and competitive process

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<sup>15</sup>Consumer Advocate's Response, at 4.

acceptable to the commission, the customer-generator was unable to find another entity ready and able to supply the proposed distributed generation service at a price and quality comparable to the utility's offering" will, in conjunction with the "lowest reasonable cost" standard, satisfy the requirement of cost-effectiveness.

Having considered the request of the HECO Utilities and the positions taken by the Consumer Advocate and HREA, the commission clarifies and confirms that "least cost" as used in Decision and Order No. 22248 means "lowest reasonable cost."

3.

Requirement (c): Open and Competitive Process

The HECO Utilities seek clarification on the possible non-applicability of requirement (c) in certain instances.

a.

Distributed Generation Primarily Driven by Utility Need

The HECO Utilities contend that if a customer-sited distributed generation project is primarily driven by a utility system need, and the customer would not otherwise have installed distributed generation, requirement (c) should not apply. In general, they explain that, in such a situation:

. . . The customer may have no desire or ability to own, operate, and maintain the DG unit, and the utility, to the extent it is relying on the unit to meet a critical system need, should be allowed to directly own and operate the DG system. In such circumstances, the utility could

competitively procure the unit, but the customer would not be expected to be involved in that process.

HECO Utilities' Memorandum, at 6.

The HECO Utilities specifically assert that requirement (c) should not apply to HECO's current efforts to add capacity to its Oahu system by installing utility *peaking* distributed generation units. In this regard, HECO notes that: (1) in 2005, it installed 14.8 MW of distributed generation at three (3) HECO sites; (2) it is evaluating additional sites, both utility and customer-owned, to install more distributed generation in 2006 and beyond; and (3) it has been in discussions with the Department of Defense ("DOD") about the possible installation of HECO-owned distributed generation on Oahu military bases to serve system capacity needs, and "[i]t would be inappropriate to require the DOD to oversee the procurement process for what ultimately is a utility resource, not a customer resource."<sup>16</sup>

In addition, the HECO Utilities suggest that requirement (c) may not apply (or may not apply to the same extent) to certain other types of customer-sited distributed generation. For example, they explain that in the future they may choose to offer emergency generator service to its customers, by tariff or contract. Hence, the HECO Utilities seek

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<sup>16</sup>HECO Utilities' Memorandum, at 7. See also Affidavit of Scott Seu. Ultimately, the HECO Utilities contend that distributed generation facilities sited on military bases should not be subject to the competitive procurement requirement at all, reasoning that military security and reliability concerns, together with federal contracting policies, "should take priority over any general policy the Commission has to encourage competition for customer-sited generation." Id. at 7.

clarification from the commission that the customers using such a tariff service are not expected to first seek to competitively procure the emergency generator from third-parties, as presently envisioned under requirement (c).<sup>17</sup>

The Consumer Advocate counters that: (1) commission action on whether to exempt requirements (a), (b), or (c) for a specific distributed generation project should be based on the specific facts supporting the proposed project, with the burden on the utility to justify the reasonableness of any requested exemption; and (2) the commission, in Docket No. 03-0371, should refrain from granting on a generic basis any exemptions to requirements (a), (b), or (c).

HREA contends that the commission should not, by this Order, necessarily bind itself by accepting the HECO Utilities' contention that requirement (c) should not apply in situations where a customer-sited distributed generation project is primarily driven by a utility system need, while providing only ancillary benefits to the customer. Rather, HREA states that the commission "should wait to rule on the transaction HECO is sketching out in its memorandum until HECO files a complete and substantiated application."<sup>18</sup>

It would be premature to establish a generic exemption as requested by the HECO Utilities for situations where a distributed generation project is primarily driven by a utility

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<sup>17</sup>See HECO Utilities' Memorandum, Section III.B, Further Distinctions Should Be Made Between The Types of DG Application, at 17 - 19.

<sup>18</sup>HREA's Response, at 4.

system need. The commission agrees with the Consumer Advocate that any commission action to exempt requirement (c) or to determine the applicability of these requirements to a specific distributed generation project should be based on the specific facts supporting the proposed project, with the burden on the utility to justify the reasonableness of any requested exemption.

Moreover, in situations where a distributed generation project is truly primarily driven by a utility system need, and the customer has no rational or reasonable business reason to own, operate, or maintain a distributed generation unit on its property, the utility would obviously be required to compensate the customer to induce it to allow the utility to install a distributed generation unit on the customer's property. In such situations, it would probably be more appropriate for the utility to obtain an easement, lease, or license of the customer's property or a portion thereof, and thereby own and operate a distributed generation facility on utility property. As discussed in Decision and Order No. 22248, at 15, "there is no dispute that the utility should be authorized to procure and operate distributed generation for utility purposes on utility property[.]"<sup>19</sup>

b.

Application to Projects Currently Being Considered

The HECO Utilities also seek clarification that requirement (c) will not retroactively apply to the utility-owned

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<sup>19</sup>Decision and Order No. 22248, at 15.

combined heat and power ("CHP") facility being considered for Castle & Cooke Resorts' ("C&C Resorts") Manele Bay Hotel on the island of Lanai.<sup>20</sup> In Docket No. 03-0261, the commission approved, subject to one (1) revision, a service contract between MECO and C&C Resorts, dated August 20, 2003 ("Service Contract").<sup>21</sup> The HECO Utilities, in seeking clarification with

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<sup>20</sup>See In re Maui Elec. Co., Ltd., Docket No. 03-0261.

<sup>21</sup>See Decision and Order No. 20811, filed on February 24, 2004. The Service Contract consists of three parts: (1) a \$250,000 annual discount for electric utility service to the Manele Bay Hotel for three (3) years, scheduled to expire on February 24, 2007; (2) an arrangement to implement ten (10) energy conservation measures; and (3) consideration of a MECO-owned CHP facility at the Manele Bay Hotel with a new rate for energy supplied by the CHCP system that results in a lower electric bill than MECO's current rates. C&C Resorts is not obligated to undertake the CHP project with MECO, and instead, could choose to undertake a similar CHP project with a third-party. The commission found reasonable and consistent with the public interest the first two (2) parts of the Service Contract. Id. at 3 - 7 (Section II(A) and (B)). Concomitantly, the commission made no ruling with respect to the reasonableness of the third part of the Service Contract, i.e., MECO's proposed CHP project:

The third part of the service contract is that the MECO and C&C Resorts will pursue the possible installation of a MECO-owned CHP facility at the Manele Bay Hotel, including providing energy at a lower rate for C&C Resorts than the rate charged other customers in the same customer class. MECO states that it will seek commission approval of its CHP agreement with C&C Resorts under a separate application. MECO also states that no negotiations have begun regarding the possible CHP facility and that C&C Resorts is not obligated to install MECO's proposed CHP project at the Manele Bay Hotel site. Therefore, the commission finds that it need not make a determination as to the reasonableness of MECO's proposed CHP project at this time and further notes that the commission has not ruled on HECO's CHP program application in Docket No. 03-0366 and the commission's own investigation into distributed generation in Hawaii, Docket No. 03-0371.

Id. at 7 - 8 (Section II(C)).

respect to the CHP project at the Manele Bay Hotel, essentially reason:

The Service Contract does not obligate C&C Resorts to implement a CHP project at the Manele Bay Hotel with MECO. Nonetheless, D&O 20811 recognizes the harmful impacts to MECO's Lanai ratepayers that would occur if C&C Resorts were to self-generate or otherwise implement non-utility DG. C&C Resorts also recognizes these potential impacts, and to the extent that its other Lanai accounts and the accounts of many of its employees who live on Lanai might be negatively impacted, prefers a MECO CHP system. (See Affidavit of Timothy Hill, which is attached hereto.) For this reason, the criterion governing customer consideration of non-utility DG options should not apply to Lanai.

HECO Utilities' Memorandum, at 9 - 10 (footnote and text therein omitted) (emphasis added).<sup>22</sup>

HREA opposes the HECO Utilities' position that Decision and Order No. 22248 should not retroactively apply to the MECO-owned CHP facility for the Manele Bay Hotel. Instead, HREA encourages MECO (and Castle and Cooke) to explore the installation of a non-CHP "renewable solution" on Lanai.

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Moreover, Paragraph 14 of the Service Contract states:

Commission Jurisdiction. As required by MECO's Rule 4, this contract for service shall at all times be subject to changes or modifications by the Commission as said Commission may from time to time direct in the exercise of its jurisdiction.

Service Contract, Paragraph 14, at 9.

<sup>22</sup>C&C Resorts, through the supporting affidavit of its Executive Vice President, expresses its preference to work with MECO on the proposed CHP project for the Four Seasons Resort Lanai at Manele Bay. Affidavit of Timothy Hill. The commission notes that the Manele Bay Hotel referenced in Docket No. 03-0261 and the Four Seasons Lanai at Manele Bay referenced herein is the same hotel.

The commission recognizes that the distributed generation project being considered on Lanai has not yet been proposed to, and approved by, the commission. Accordingly, this would not be a case of retroactive application of Decision and Order No. 22248.

It would be premature to determine that Decision and Order No. 22248 does not apply to the distributed generation projects being considered, but not yet approved, on Lanai. This issue has not been adequately briefed by the parties involved. Any such determination should be based on the specific facts supporting the proposed project, with the burden on the utility to justify its request.

c.

Showing of Competitive Process

The HECO Utilities, in addition to their discussions on the possible non-applicability of requirement (c) in certain instances, suggest a process that may satisfy requirement (c) when it does apply:

. . . . First, the Commission could facilitate the customer's consideration of non-utility DG services by actively compiling and maintaining a database of DG providers. The database of non-utility DG providers would be non-exclusionary and readily accessible to the public such as via the Internet, and the DG providers themselves should be responsible for the accuracy of any information in the database. A customer pursuing a DG project with the regulated utility would then be required to file a declaration with the Commission that attests that (1) it is aware of the availability of non-utility DG services, (2) the customer has solicited proposals and given due consideration to the non-utility DG alternatives, and (3) the customer desires the utility DG offering, because

the customer has determined that it provides the greatest value to the customer considering price, quality, reliability, or other criteria important to the customer.

HECO Utilities' Memorandum, at 10.

The Consumer Advocate states that if the HECO Utilities are merely seeking guidance on a possible process, as opposed to the adoption of a process, the Consumer Advocate does not oppose the HECO Utilities' request for guidance. However, if the HECO Utilities seek the commission's approval of their suggested process, the Consumer Advocate does not support the granting of such approval at this time.

HREA states, without explanation, that the HECO Utilities' suggestion that the commission develop and maintain a list of distributed generation providers may not be practical. Rather, HREA states that the commission could "declare that HECO cannot offer, as an inducement to the customer to choose the utility for CHP, a discount in the customer's electric rates and/or exemption from standby-charges."<sup>23</sup>

The process proposed by the HECO Utilities to give a fair opportunity to non-regulated utilities to offer distributed generation services as contemplated in Decision and Order No. 22248 appears to be a reasonable method of implementing the commission's requirements. The process appears to be a practical approach that considers the reality that customers are not regulated entities, and that it may not be appropriate for the commission to too closely oversee the competitive procurement

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<sup>23</sup>HREA's Response, at 5.

process to be conducted by utility customers. On the other hand, the commission may require more than an unsupported assertion that the customer has solicited proposals and given them due consideration. At a minimum, the utility would be well advised to require the customer to include in its declaration a list of the companies that were solicited by the customer and a list of companies that submitted proposals that were considered by the customer. In addition, it would be prudent for the utility to require the customer to include in its declaration to the commission the details of the terms of the utility's offer to the customer, so that the commission may determine whether the utility is attempting to utilize an unfair advantage as a regulated utility, which is the concern expressed by HREA.

The foregoing guidance, however, should not be construed as a pre-approval of the proposed process that is binding on the commission, as the commission will make such a determination when a utility files an application containing the details of a specific project with the commission. Moreover, the commission agrees with HREA's concern that the utility should not be able to offer a discount from regulated rates as an inducement to the customer to choose the utility's distributed generation.<sup>24</sup> The commission is committed to encouraging a competitive market for distributed generation services. If a utility engages in behavior inconsistent with that goal, the commission will entertain recommendations for restricting utility opportunities in distributed generation.

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<sup>24</sup>HREA's other concern regarding standby charges will be addressed in the utilities' standby tariffs.

B.

Renewable Forms of Distributed Generation

The HECO Utilities request clarification on the applicability of Decision and Order No. 22248 to renewable forms of distributed generation. In brief, they explain:

. . . because the utility has installed, and may seek to install or purchase, [photovoltaic] systems at customer sites in the interests of promoting the technology, stimulating the market, and complying with state [RPS] requirements. In addition, the Companies have not applied standby rates to customer-owned renewable DG systems in the past. The Companies intend to continue to treat renewable DG systems differently in their standby rate tariffs, unless otherwise directed by the Commission, in order to strike a balance between encouraging renewable energy and mitigating the negative effects of losing fixed cost recovery from non-utility DG.

HECO Utilities' Memorandum, at 11.

1.

Utility Ownership of Photovoltaic ("PV")  
Distributed Generation Systems on Customer Sites

Decision and Order No. 22248, Section II(D), provides in part:

Forms of Distributed Generation  
That are Feasible and Viable in Hawaii

. . . .

Since not all benefits and costs identified with distributed generation exist for each distributed generation project, the commission will not require all projects to satisfy all possible criteria to be considered distributed generation for purposes of the rights and

obligations established by this Decision and Order.

Decision and Order No. 22248, Section II(D), at 26 - 27 (footnote and text therein omitted).

The HECO Utilities note that increasing the amount of cost-effective renewable energy on the electric system is clearly a "legitimate system need" under requirement (a) and the RPS mandate.<sup>25</sup> In general, the HECO Utilities explain that the initial development and ownership of PV systems is not cost-effective for the utility, since regulated electric utilities are not eligible for federal renewable energy investment credits. However, once the non-regulated owner of a PV system makes full use of the federal and state energy tax incentives within the first five (5) years of installation, the PV owner may see value in selling the PV system in order to recoup the owner's initial capital investment, and the regulated utility may be in the best position to purchase the already installed PV system.

Under this scenario, the "[u]tility buy-out of existing PV systems could facilitate a larger overall PV market[.]"<sup>26</sup> Also, the utility's purchase and acquisition of any PV system "would be subject to Commission approval, and would depend on a showing that such acquisition is cost-effective, consistent with

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<sup>25</sup>See HRS chapter 269, part V, Renewable Portfolio Standards.

<sup>26</sup>HECO Utilities' Memorandum, at 12.

utility system needs and plans, and is beneficial to the utility's ratepayers."<sup>27</sup>

The HECO Utilities are also evaluating "a possible utility lease first-purchase later option approach to assist in the initial development of PV systems in partnership with host facility owners and third-party PV system owners."<sup>28</sup> "To the extent that the utility participates in developing or procuring PV systems, the [HECO Utilities] recognize that these activities would need to be done in an open and competitive manner."<sup>29</sup>

That said, the HECO Utilities seek confirmation of their understanding that:

D&O 22248 should at [a] minimum allow room for the Companies to pursue such [PV] efforts in collaboration with the PV industry and PV customers. The D&O criteria governing regulated utility ownership of customer-sited DG could support a utility PV DG model, provided that (1) addition of renewable energy is considered a legitimate system need, (2) a lowest reasonable cost standard and [renewable energy] portfolio approach can be applied, and (3) special consideration is given to the fact that, under such a business model, the utility would be providing inherent value to PV DG developers and market players rather than competing with them to offer DG services.

HECO Utilities' Memorandum, at 13 - 14 (emphasis added).

The Consumer Advocate states that the HECO Utilities' request for confirmation, in concept, appears reasonable. That said, the Consumer Advocate essentially reiterates that any commission decision as to whether a utility's purchase of a

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<sup>27</sup>HECO Utilities' Memorandum, at 13.

<sup>28</sup>HECO Utilities' Memorandum, at 13.

<sup>29</sup>HECO Utilities' Memorandum, at 13.

specific renewable distributed generation system is reasonable should be made only following the review of the application seeking the commission's approval to acquire such a system, based on the specific facts supporting the utility-owned customer-sited distributed generation project, with the burden on the utility to justify the reasonableness of the acquisition.

HREA contends that, in lieu of the HECO Utilities' purchasing of existing PV systems following the expiration of the five (5)-year period, it makes more sense for them to offer demand-side management rebates now. "These rebates, in turn, would leverage a greater amount of PV."<sup>30</sup> HREA also cautions the commission on the "potentially serious side-effects or unintended consequences of utility-owned PV on customer sites."<sup>31</sup>

The commission agrees with the Consumer Advocate that, although the concept described appears to be reasonable on its face, any commission decision as to whether a utility's purchase of a specific renewable distributed generation system is reasonable should be made only following the review of the application seeking the commission's approval to acquire such a system, based on the specific facts supporting the utility-owned customer-sited distributed generation project, with the burden on the utility to justify the reasonableness of the acquisition. Accordingly, the commission declines to provide the HECO Utilities with the requested confirmation at this time.

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<sup>30</sup>HECO Utilities' Memorandum, at 6.

<sup>31</sup>HECO Utilities' Memorandum, at 6.

2.

Applicability of Standby Rates  
to Renewable Distributed Generation

Decision and Order No. 22248 requires each electric utility to establish by tariff standby rates based on unbundled costs associated with providing generation, distribution, transmission, and ancillary services.<sup>32</sup> As instructed by the commission in Ordering Paragraphs 6 and 9:

6. To ensure that only economic distributed generation projects are developed, and that there is no cost shifting from the customer-generator to other customers or to utility shareholders, utility-incurred costs shall be allocated properly so that those costs that benefit the distributed generation project are borne by the project. This principle is applied to interconnection costs, standby and backup service costs, and unrecovered utility costs, as described above.

.....

9. HELCO and KIUC shall be allowed to continue utilizing their respective standby rates until new standby rates are approved by the commission.

Decision and Order No. 22248, Ordering Paragraphs No. 6 and No. 9, at 47 (emphasis added).

The HECO Utilities, in establishing new standby rates required by Decision and Order No. 22248, intend to develop special standby rate provisions for renewable forms of distributed generation in order to balance the objectives of encouraging the development of renewable energy systems consistent with the RPS mandate, while protecting ratepayers against the loss of fixed costs recovery due to non-utility owned

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<sup>32</sup>See Decision and Order No. 22248, Section II(H)(2), Standby and Backup Service Costs, at 41 - 42.

distributed generation systems.<sup>33</sup> "Options that will be considered include providing standby rate exemptions to renewable systems below a certain size or systems that provide less than a certain amount of a customer's total energy."<sup>34</sup>

The HECO Utilities seek the commission's confirmation that their approach of developing special standby rate provisions for renewable forms of distributed generation is acceptable in concept. They reason that such an approach appears consistent with the commission's stated intent to "consider whether there is a benefit to deferring the assignment of any unrecovered costs until a certain percentage of load has been lost to distributed generation applications."<sup>35</sup>

To the extent that the HECO Utilities' intentions are directed to net metering installations that by statute are not subject to standby charges, the Consumer Advocate agrees with the HECO Utilities' request for clarification. Nonetheless, the Consumer Advocate notes that:

. . . . it is premature to determine what should or should not be subject to the standby tariff without reviewing the proposals to be set forth before the Commission. Thus, the Consumer Advocate recommends that any determination as to what should or should not be subject to the standby tariffs should only be made after the tariffs are filed and the parties are able to review the specifics of such tariff. The Commission should not approve the [HECO

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<sup>33</sup>HELCO notes that its existing standby service tariff, Rider A, does not apply to a customer whose non-utility power is produced from a non-fossil energy source.

<sup>34</sup>HECO Utilities' Memorandum, at 15.

<sup>35</sup>HECO Utilities' Memorandum, at 15 (quoting Decision and Order No. 22248, at 43).

Utilities'] request in the context of [Docket No. 03-0371].

Consumer Advocate's Response, at 7 (emphasis added).

HREA expresses concern with the HECO Utilities' proposal to develop standby rate exemptions for smaller renewable systems or those that provide less than a certain amount of a customer's total energy load:

1. The HECO Utilities' proposal makes no distinction between standby costs and stranded costs, which should be separately calculated.

2. If the goal is to encourage the installation of renewable systems, "the standby charge should be waived for all renewable systems, and in particular for those which provide a greater portion of the customer's needs, not a smaller one."<sup>36</sup>

3. If the HECO Utilities intend to impose standby charges solely on fossil fuel-fired distributed generation, they should design the standby charge so that only the costs attributable to that type of distributed generation are included in the standby charge.

The commission appreciates the HECO Utilities' efforts to give renewable energy powered distributed generation projects favorable consideration. The commission, however, agrees with the Consumer Advocate that any determination as to what should or should not be subject to the standby tariffs should only be made after the tariffs are filed and the parties are able to review the specifics of such tariffs. Accordingly, the commission

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<sup>36</sup>HREA's Memorandum, at 7.

declines to provide the HECO Utilities with their requested confirmation at this time.

C.

Additional Points Concerning  
Decision and Order No. 22248

In Section III of their Motion for Clarification, the HECO Utilities: (1) appear to set forth certain points as further argument in the development of distributed generation policies; and (2) may reiterate these arguments as such issues arise in applying for the commission's approval of specific distributed generation projects.

Once again, the commission agrees with the Consumer Advocate that "[a]ny determination on each of the matters cannot be done without knowing the specific facts under which the proposals will be made[,]" with the utility having the burden of justifying the reasonableness of a proposed utility-owned customer-sited distributed generation system in the application seeking the commission's approval of such a project.<sup>37</sup>

D.

Comments on Policies of  
Distributed Generation and Competition

The HECO Utilities also offer certain comments concerning distributed generation and competitive policies in Section IV of their Motion for Clarification as further argument

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<sup>37</sup>Consumer Advocate's Response, at 8. See also id. at 8 - 10 (Section II(B)(3)(a), (b), and (c)).

in the development of distributed generation policies. The HECO Utilities may reiterate these arguments as such issues arise in applying for the commission's approval of specific distributed generation projects.

III.

Orders

THE COMMISSION ORDERS:

1. The HECO Utilities' Motion for Clarification of Decision and Order No. 22248 is granted in part and denied in part, consistent with the terms of this Order.

2. The HECO Utilities' Motion for Partial Reconsideration of Decision and Order No. 22248 is denied.

DONE at Honolulu, Hawaii APR - 6 2006.

PUBLIC UTILITIES COMMISSION  
OF THE STATE OF HAWAII

By Carlito P. Caliboso  
Carlito P. Caliboso, Chairman

By (EXCUSED)  
Wayne H. Kimura, Commissioner

APPROVED AS TO FORM:

Michael Azama  
Michael Azama  
Commission Counsel

By Janet E. Kawelo  
Janet E. Kawelo, Commissioner

03-0371.cs

CERTIFICATE OF SERVICE

I hereby certify that I have this date served a copy of the foregoing Order No. 22375 upon the following parties, by causing a copy hereof to be mailed, postage prepaid, and properly addressed to each such party.

JOHN E. COLE  
EXECUTIVE DIRECTOR  
DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS  
DIVISION OF CONSUMER ADVOCACY  
P. O. Box 541  
Honolulu, HI 96809

WILLIAM A. BONNET  
VICE PRESIDENT  
HAWAIIAN ELECTRIC COMPANY, INC.  
HAWAII ELECTRIC LIGHT COMPANY, INC.  
MAUI ELECTRIC COMPANY, LTD.  
P. O. Box 2750  
Honolulu, HI 96840-0001

DEAN MATSUURA  
DIRECTOR, REGULATORY AFFAIRS  
HAWAIIAN ELECTRIC COMPANY, INC.  
P. O. Box 2750  
Honolulu, HI 96840-0001

KENT D. MORIHARA, ESQ.  
MORIHARA LAU & FONG LLP  
841 Bishop Street, Suite 400  
Honolulu, HI 96813

Counsel for KIUC

H.A. DUTCH ACHENBACH, PRESIDENT & CEO  
JOSEPH McCAWLEY, MANAGER, REGULATORY AFFAIRS  
MICHAEL YAMANE, VICE PRESIDENT, STRATEGIC PLANNING  
KAUAI ISLAND UTILITY COOPERATIVE  
4463 Pahe'e Street, Suite 1  
Lihue, HI 96766

Certificate of Service  
Page 2

BRIAN T. MOTO, ESQ.  
CORPORATION COUNSEL  
CINDY Y. YOUNG, ESQ.  
DEPUTY CORPORATION COUNSEL  
COUNTY OF MAUI  
200 S. High Street  
Wailuku, HI 96793

Counsel for the COUNTY OF MAUI

KALVIN K. KOBAYASHI  
ENERGY COORDINATOR  
COUNTY OF MAUI  
DEPARTMENT OF MANAGEMENT  
200 S. High Street  
Wailuku, HI 96793

WARREN S. BOLLMEIER II  
PRESIDENT  
HAWAII RENEWABLE ENERGY ALLIANCE  
46-040 Konane Place, #3816  
Kaneohe, HI 96744

JOHN CROUCH  
Box 38-4276  
Waikoloa, HI 96738

RICK REED  
INTER ISLAND SOLAR SUPPLY  
761 Ahua Street  
Honolulu, HI 96819

HENRY Q CURTIS  
VICE PRESIDENT FOR CONSUMER ISSUES  
LIFE OF THE LAND  
76 North King Street, Suite 203  
Honolulu, HI 96817

SANDRA-ANN Y.H. WONG, ESQ.  
1050 Bishop Street, #514  
Honolulu, HI 96813

Counsel for HESS MICROGEN, LLC

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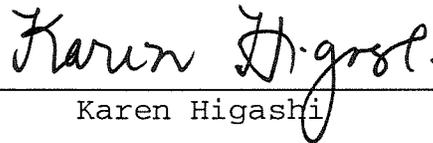
CHRISTOPHER S. COLEMAN, ESQ.  
DEPUTY GENERAL COUNSEL  
AMERANDA HESS CORPORATION  
One Hess Plaza  
Woodbridge, NJ 07095

Counsel for HESS MICROGEN, LLC

LANI D.H. NAKAZAWA, ESQ.  
OFFICE OF THE COUNTY ATTORNEY  
COUNTY OF KAUAI  
4444 Rice Street, Suite 220  
Lihue, HI 96766

Counsel for the COUNTY OF KAUAI

GLENN SATO, ENERGY COORDINATOR  
c/o OFFICE OF THE COUNTY ATTORNEY  
4444 Rice Street, Suite 220  
Lihue, HI 96766

  
\_\_\_\_\_  
Karen Higashi

DATED: APR - 6 2006