State Corporation Commission
2007 Fiscal Impact Statement

1. Bill Number HB3068

House of Origin ☐ Introduced ☐ Substitute ☐ Engrossed

Second House ☐ In Committee ☐ Substitute ☒ Enrolled

2. Patron Hogan

3. Committee Passed Both Houses

4. Title Virginia Electric Utility Restructuring Act.

5. Summary/Purpose: Virginia Electric Utility Restructuring Act.
Relaxes the requirements on adjustments allowed to be made in rate requests before the State Corporation Commission (SCC) for all utilities. Provision prohibiting speculative adjustments is stricken. Provides the SCC authority to approve a performance-based rate-making methodology for electric utilities; current statute applies only to gas utilities. The fuel increase for Dominion for July 1, 2007 is limited to an increase of 4% over total rates at that time. Fuel costs over that amount, if any, are to be deferred without interest for future recovery as follows: in calendar year 2008, that portion recoverable by increasing the 1/1/08 total residential rate by 4%; in calendar year 2009, that portion recoverable by increasing the 1/1/09 total residential rate by 4%; and, in 2010 any remaining deferred balance shall be recovered. Subsequent fuel increases, beginning in 2008, are allowed to become effective each July 1st at the full projected annual amount. Margins from off-system sales are to be credited 75% to the fuel factor and the remaining 25% shall not be considered in biennial reviews. After notice and hearing the SCC may reduce the 75% credited to customers, thereby increasing the portion of off-system sales margin retained by the Company, via the fuel factor if it finds such action is in the public interest. Repeals the SCC's authority to consider a utility's overall cost of service when reviewing the need for an increase in its fuel adjustment clause. Instead costs that are recoverable through the fuel rate adjustment clause will be considered on a stand-alone basis without regard to the other costs, revenues, investments or earnings.

After the capped rate period ends, only (i) customers whose annual demand exceeds five megawatts but did not exceed 1% of the customer's incumbent electric utility's peak load during the most recent calendar year unless such customer had noncoincident peak demand in excess of 90 megawatts in 2006 or any year thereafter, and (ii) two or more nonresidential retail customers that petition the SCC and receive authority to aggregate their demands to meet the above limitation, will be permitted to purchase electricity from a competing provider of generation services. The ability of large customers to purchase electric power from a licensed competitive supplier is subject to the condition that they cannot thereafter purchase electricity from their incumbent utility without giving five years' notice, unless it demonstrates that the supplier failed to perform and that such customer is unable to obtain service from an alternative supplier. If a customer receives an exemption from the five-year minimum stay requirement, the cost of its power during the exemption period will be the market-based costs of the utility generation plus various mark-ups including the fair rate of return defined by § 56-585.1, discussed below.

The SCC's authority to take certain actions to expand transmission capacity is repealed. The bill removes the prohibition against the filing for eminent domain for construction or

enlargement of generation facilities. It specifically provides that an electric utility may offer metering options. Adds a requirement that the SCC find that any facility constructed and operated by a utility whose rates are regulated pursuant to § 56-585.1 of the Code of Virginia, are required by the public convenience and necessity. The expiration of capped rates is moved up from December 31, 2010 to December 31, 2008.

Requires that the SCC initiate general rate cases for each investor-owned electric utility in the first six months of 2009 pursuant to Chapter 10 (§ 56-232 et seq.) except that return on equity must be set within the range described in § 56-585.1 A subdivision 2. If combined rates of return are 50 basis points below the determined combined rate of return then rates will be increased to provide for earnings not less than the combined rate of return; if rates are 50 basis points above the determined combined rate of return the SCC shall either (i) order rate reductions to provide for earnings at the determined rate of return for generation and distribution, or (ii) require that 2008 earnings greater than 50 basis points above the combined fair rate of return be credited back to customers over a 24-month period.

The bill requires the SCC to conduct biennial reviews beginning in 2011 (however, the SCC may defer Dominion's first biennial review to 2012), subject to notice and opportunity for hearing, of the rates terms and conditions of investor-owned electric utilities. Fair rates of return on equity for each distribution, generation, and combined shall be determined during biennial reviews based on any method the SCC finds to be in the public interest provided such return on common equity falls within the following specific parameters: (i) no less than the average returns on equity reported to the Securities and Exchange Commission of a peer group of companies (the specific companies may be chosen by the SCC based on guidelines provided in the statute) for the previous three years; and (ii) no higher than such peer group average returns plus 300 basis points. The return calculated according such parameters may be increased or decreased based on the operating performance of the utility, as compared to national standards, by 50 basis points. If a combined fair return on equity calculated in a biennial review increases by a percentage greater than the percent increase in the CPI-U over the Initial Return set by the SCC after July 1, 2009, (over a like time period) the SCC may conduct an additional analysis to determine whether such combined fair return on equity is in the public interest. In this instance the SCC may set the combined fair return on equity as the Initial Return increased by at least the percent increase in the CPI-U since the Initial Return was set. If a utility's earnings are within 50 basis points of such return, it shall be considered neither excessive nor insufficient.

Costs for transmission services provided by PJM Interconnection and approved by the Federal Energy Regulatory Commission (FERC) and costs of FERC-approved demand response programs administered by PJM, are deemed reasonable and prudent. After the expiration of capped rates, but not more than once in any 12-month period, the SCC shall approve recovery of the following costs, without limitation, through a rate adjustment clause in the retail rate schedules: costs for transmission service, charges for new and existing transmission facilities, administration charges and ancillary service charges. Such rate approval will be made on a stand-alone basis, without consideration of the overall earnings of the electric utility. The SCC must issue its final order within three months of an application.

Electric utilities may at any time after the capped rate period and not more than once in any 12-month period, petition the SCC for approval of rate adjustment clauses that: (i) incremental costs described in clause (vi) of subsection B of § 56-582 if such utility is deferring such costs at July 1, 2007 pursuant to a SCC order; (ii) provide incentives for the utility to design and operate various programs including, demand-side management, conservation, energy efficiency and load management programs, which shall be approved if the program is in the public interest and the cost of providing the incentives is demonstrated with reasonable certainty;

(iii) provide for projected and actual costs of participation in a renewable energy portfolio standard program; the SCC shall approve petitions allowing for recovery of costs of programs approved pursuant to § 56-582.2; (iv) provide for projected and actual costs of projects necessary to comply with environmental laws and regulations, including an enhanced return in some instances. The SCC must issue its final order within eight months of an application and has the authority to determine the duration of adjustment clauses allowed pursuant to this section.

To ensure a reliable and adequate supply of generation to meet a utility's native load obligations, a utility may petition the SCC at any time after the termination of capped rates (and for specific projects prior to the termination of capped rates) for cost recovery, via a rate adjustment clause, of a coal-fueled generation facility in Southwest Virginia, other generation facilities, and major unit modifications of generation facilities. The legislation provides that the utility that constructs such generation facilities has the right to recover all costs of the facility through its rates, including allowance for funds used during construction plus a fair rate of return. Further, as an incentive to undertake such generation projects, all projects, except simple-cycle combustion turbines, shall include the cost of an enhanced rate of return on the utility's investment for the construction period and a period after commercial operation as determined by the SCC within a range specified in the legislation. The enhanced rate of return will be 200 basis points for coal and nuclear projects and 100 basis points for combined-cycle combustion turbine projects. If a utility applies to construct a generation facility that utilizes integrated gasification combined cycle technology, the SCC must issue an order, after a hearing, stating the portion of the service life that the enhanced return will be in effect. Subsequent to such order the utility shall have the option of withdrawing the application. The SCC must issue its final order within nine months of an application. The adjustment clause shall be considered on a stand alone basis, without regard to a utility's overall earnings. All costs incurred relative to a specific adjustment clause are to be deferred for future recovery until the latter of an SCC order or the implementation of such a factor. New adjustment clause factors must be effective within 60 days of a final order of the SCC. If the SCC finds during its biennial review that includes the year 2018, that Dominion has not filed all necessary federal and state applications for approval to construct one or more nuclear or coal-fired generation facilities to add total capacity of at least 1500 megawatts, or if such approvals have been granted and Dominion has not made reasonable and good faith efforts to construct such facilities, then the SCC may reduce on a prospective basis any enhanced rate of return on common equity previously granted for such facilities.

Based on the results of the SCC's biennial reviews: (i) if earnings are more than 50 basis points below the combined fair rate of return, without regard to the enhanced return or other matters in regard to generation projects, rates shall be increased to provide earnings of the fair rate of return; (ii) if earnings are more than 50 basis points above the fair combined rate of return, without regard to the enhanced return or other matters in regard to generation projects, 60% of such excess shall be returned to ratepayers over a 24-month period; however, if the SCC finds that rates during the review period increased more than the CPI-U, then, if in the public interest, the SCC can require that all earnings more than 50 basis points above the fair rate of return be refunded back to customers (this higher refund is in lieu of the 60% earnings refund and rate reductions discussed next); (iii) if earnings are more than 50 basis points above the fair combined rate of return for two consecutive biennial review periods considered as a whole, without regard to the enhanced return or other matters in regard to generation projects, the SCC shall order rate reductions in addition to refunds provided such reductions will continue to allow the utility to earn a fair combined rate of return. The SCC's final order in biennial proceedings must be issued within 9 months of the end of the test period, or six months after the review is filed with the SCC.

The SCC shall regulate a utility on a stand-alone basis utilizing the actual end of test period capital structure and cost of capital of such utility, unless the SCC finds that the debt to equity ratio in such capital structure is unreasonable, without regard any entity to which it may be affiliated, specifically when considering federal and state income tax costs. Utilities may file for rate increases pursuant to § 56-245 or the SCC rate case rules, except the rate of return shall be determined per § 56-585.1. Investor-owned electric utilities may apply to the SCC to participate in a renewable energy portfolio standard (RPS) program and the SCC shall approve such application if the utility shows it will likely achieve 12% of base year electric energy sales by 2022. The legislation provides for an increase in the fair rate of return as an incentive whenever the utility meets an RPS goal. The specific RPS goals are defined by the legislation. The legislation states that it is in the public interest for utilities to achieve RPS goals.

The SCC shall not require any cooperative to reflect changes in wholesale power costs which occurred during the capped rate period, other than during a general rate proceeding. Cooperatives may by vote of its Board of Directors, without SCC review and approval, (i) change its base rates provided any cumulative increase or decrease, excluding fuel provisions, does not exceed five percent over a three year period, (ii) amend terms and conditions that do not result in revenue changes, and (iii) make adjustments to any pass through of third-party service charges and fees, and to any fees, charges and deposits set out in Schedule F of such cooperative's terms and conditions at January 1, 2007. Revised tariffs, terms and conditions are to be filed promptly with the SCC.

Sections 56-581.1 and 56-583 of the Code of Virginia are repealed. It is in the public interest and consistent with the energy policy goals of § 67-102 of the Code to promote cost-effective conservation of energy through fair and effective demand side management, conservation, energy efficiency, and load management programs. The Commonwealth shall have a stated goal of reducing the consumption of electric energy by retail customers by the year 2022 by an amount equal to 5% of the amount of electric energy consumed by retail customers in 2006. The SCC shall establish a proceeding to determine various specifics relating to whether and how such a plan can work and provide costs estimates of attaining the established goals. The SCC is to report to the Governor and the Commission on Electric Utility Restructuring (CEUR). The Department of Taxation shall conduct an analysis of the potential implications of changes to the system of taxation resulting from this law and report its findings to the CEUR November 1, 2007. This legislation does not modify or impair the terms of any SCC orders approving the divestiture of generation assets. The Office of Attorney General (OAG), in consultation with the SCC, shall submit annual reports to the CEUR on or before November 1, 2007 and 2008 in which it identifies and recommends appropriate corrective legislation to address issues that may impede the implementation of the provisions of this act. The SCC in consultation with the OAG shall submit a report to the Governor and the General Assembly by November 1, 2012 and every 5 years thereafter, assessing the rates and terms and conditions of incumbent electric utilities. The Department of Mines, Minerals and Energy shall, in conjunction with the Secretary of Agriculture and Forestry, representatives of the agriculture and silviculture industry, the Forest Council of Virginia and representatives of utilities conduct an assessment of the provisions of Virginia's renewable portfolio standards program and the availability of biomass resources in the Commonwealth. A report is to be submitted with findings and recommendations to the Governor and the CEUR.

6. Fiscal impact estimates are: Not available and cannot be determined at this time. See Item # 8.

7. **Budget amendment necessary:** Possibly. The Department of Forestry can provide an estimate of live biomass from Virginia's forest lands using Forest Inventory Analysis ongoing data collection and analysis. However, the Department of Forestry does not currently study the residual biomass left on tracts of land following harvesting. The Department believes that no reliable estimates of residual logging wood biomass can be determined without a statistically sound study. The Department of Forestry will require $ 85,000 to complete a logging residual wood study to determine the amount of residual biomass following a timber harvest. The Department of Forestry would hire part time personnel or contract the field data collection to measure the amount and type of residual biomass remaining on tracts following timber harvests. The results of the study would include a reliable estimate of the amount and types of residual biomass available regionally and statewide.

8. **Fiscal implications:** There will likely be a fiscal impact on the State Corporation Commission because electric reviews will be limited to a short time period each year. This concentrated work load may result in the need for hiring consultants to assist staff during the limited review period, particularly during 2009 when all investor-owned electric utilities will be subject to general rate cases. The legislation will have implications on revenues collected by electric utilities and the bills paid by electric consumers. Such impacts cannot be quantified; however, most major cost increases incurred by electric utilities will be recovered via adjustment clauses without regard to the overall earnings position of the company with little limitation on the number or frequency of such increases.

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   The Department of Taxation would have no administrative costs associated with conducting the study required by enactment clause 4. The study will be conducted with existing resources.

   The following entities may also incur expense in performing duties required by the legislation: Office of Attorney General and the Department of Mines, Minerals and Energy.

9. **Specific agency or political subdivisions affected:** State Corporation Commission; Virginia Department of Taxation; Office of Attorney General; Department of Mines, Minerals and Energy; Department of Forestry and Secretary of Agriculture and Forestry

10. **Technical amendment necessary:** None noted.

11. Other comments: Senate Bill 1416 is similar to this bill.

Date: 03/12/07 / sdl
cc: Secretary of Commerce and Trade
Secretary of Agriculture and Forestry