

State Corporation Commission 2007 Fiscal Impact Statement

1. Bill Number SB1416

House of Origin ☒ Introduced ☐ Substitute ☐ Engrossed

Second House ☐ In Committee ☐ Substitute ☐ Enrolled

2. Patron Norment

3. Committee Commerce and Labor

4. Title Electric utilities.

5. Summary/Purpose: Electric utilities. Advances the scheduled expiration of the capped rate period from December 31, 2010, to December 31, 2008, and establishes a new methodology for determining electric rates for investor-owned electric utilities after the expiration or termination of capped rates. After the expiration or termination of capped rates, the State Corporation Commission (SCC) is required to conduct biennial reviews of the rates for generation, distribution and transmission services, on an unbundled basis, by each investor-owned incumbent electric utility. The reviews shall be conducted to determine, for a 12-month test period, whether the utility's earnings have produced a fair combined rate of return on the utility's common equity for its generation and distribution services. If a utility earned more than the fair combined return on both its generation and distribution services in the test period, earnings above such return will be shared between the company and customers as follows: (i) the first 100 basis points of earnings is retained by the company; (ii) one-half of any excess between 100 and 200 basis points above the fair combined return is to be credited to customers; (iii) two-thirds of any excess between 200 and 300 basis points above the fair combined return is to be credited back; (iv) three-fourths of any excess between 300 and 400 basis points above, is to be credited back; and (v) all earnings more than 400 basis points above the fair combined return is to be credited back to customers. If a utility earned more than 100 basis points above a fair combined rate of return on both its generation and distribution services, and total aggregate regulated rates of such utility were more than five percent, compounded annually, above the total aggregate regulated rates of such utility determined in the biennial review for the base period, the SCC may direct that the earnings for such test period that were more than 100 basis points above the fair combined rate of return be credited to customers' bills. A "fair rate of return" on common equity is 600 basis points above the latest available three month average bond yield of investment-grade bonds using Moody's Long Term Baa Utility Bonds; however, if the bond yield exceeds 12 percent, the SCC may adopt an alternative method that produces a figure not less than 12 percent (which when added to the 600 basis point bump is 18 percent). The Commission may increase or decrease the rate of return by up to 0.5 percentage points under a "Performance Incentive." 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 and recoverable under a rate adjustment clause. Utilities may also obtain, during or after the capped rate period, rate adjustment clauses, for various purposes, including demand-side management, conservation, renewable energy, energy efficiency and load management programs, which shall be approved if the costs or the need for the incentives are demonstrated with reasonable certainty. The provision

of the Virginia Electric Utility Restructuring Act that currently addresses the development of a coal-fueled generation facility in Southwest Virginia is amended to apply to other generation facilities, environmental projects, and major unit modifications of generation facilities and to provide that the utility has the right to recover the costs of the facility through its rates, including allowance for funds used during construction plus a fair rate of return, through a rate adjustment clause. During such a rate proceeding, the SCC may examine the prudence of any cost incurred except for those transmission-related and FERC-approved demand response programs declared to be reasonable and prudent. Costs that are recoverable through rate adjustment clauses will be considered on a stand-alone basis without regard to the other costs, revenues, investments or earnings, and the requests for their approval are to be decided within specified time limits. After the capped rate period ends, only customers whose annual demand exceeds five megawatts 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 generation plus various mark-ups including the fair rate of return discussed above. The measure also (i) authorizes any public utility to apply to the Commission to implement rate design changes which overall, and by customer class, are not designed to increase or decrease the aggregate regulated operating revenues of such utility; (ii) directs that the fuel factor allowing the recovery of costs of purchased fuel by an electric utility that divested its generation assets prior to January 1, 2002, shall increase its regulated electric revenue by an amount not more than 20 percent of such revenue during the previous calendar year, with a deferral of any costs excluded by this limitation until subsequent proceedings, with interest at a rate no less than the rate for refunds in rate cases; (iii) provides that in fuel factor proceedings, energy revenues associated with off-system sales of power are to be credited against fuel factor expenses in an amount equal to the total incremental fuel factor costs incurred in the production and delivery of such sales, with 50 percent of the total positive accumulated energy revenues received from off-system sales transactions, less the total incremental costs incurred in the production and delivery of such sales, being credited against fuel factor expenses and 50 percent of the energy margins being retained by the utility by excluding this margin from the new biennial reviews of electric utilities' rates; (iv) repeals the existing provision that allows the Commission to dispense with the fuel factor procedures for any electric utility if it finds that its fuel costs can be reasonably recovered through rates established through other provisions; and (v) requires electric utilities to file plans for how they will meet generation and transmission requirements to serve native load for the ensuing 10 years.

Provisions of the Restructuring Act that exempt the generation of electric energy from regulation, prohibit public service corporations from exercising the power of eminent domain to acquire property for generation facilities, authorize the Commission to take certain actions to expand transmission capacity, and authorize competition for metering and billing services are repealed.

6. Fiscal Impact Estimates are: Not available at this time. See Item # 8.

7. Budget amendment necessary: No.

8. Fiscal implications: The fiscal impact is not quantifiable at this time. The concentration of electric utility cases on a biennial basis may require additional staff or the use of consultants to complete required analyses in a limited time period. The legislation could potentially have a significant impact on the revenues received by electric utilities and the rates paid by electric consumers. These impacts are impossible to quantify.

9. Specific agency or political subdivisions affected: State Corporation Commission and its utility divisions and Office of General Counsel

10. Technical amendment necessary: None specifically noted; but see comments at # 11.

11. Other comments: This legislation is the subject of meetings by a number of stakeholders.

The following comments on the legislation have been submitted by the Division of Public Utility Accounting:

(1) Lines 90-92, the proposed language prohibits off-system sales losses from flowing through the fuel factor; however, such losses are not also prohibited from inclusion in the biennial review of base rates, possibly shifting 100% of any losses to customers while sharing net profits 50/50 between customers and the utility.

§ 56-585.1 A:

(2) Generally, this section provides for utilities to increase rates for a host of reasons via adjustment clauses on a stand alone, single issue, basis ignoring current earnings levels. Rates can only increase, regardless of earning levels. Revenue sharing of earnings above a legislated level is only done every other year.

(3) Lines 746-753 require biennial reviews of “rates, terms and conditions;” however, subdivision 2 of that section (lines 754-761) limits the biennial review to rates. It appears terms and conditions cannot be changed or analyzed during biennial reviews.

(4) Subdivision 4, line 782 requires the use of SEC financial statements in utility filings for biennial reviews. The use of FERC Form 1 annual report would be more appropriate because utility accounting systems are based on FERC’s uniform system of accounts.

(5) Subdivision 5 (lines 793-804) requires the Commission to find FERC approved transmission costs to be reasonable and prudent and to implement adjustment clauses for the recovery of such costs. Subdivision 6 (lines 805-810) provides that utilities may petition the Commission for an adjustment clause to recover, among other things, transmission environmental and reliability expenditures. This may result in a double-up of cost recovery first by mandating approval of FERC approved costs and then by providing for approval by the Commission for certain transmission costs.

(6) Subdivision 7 provides for the recovery of all major generation projects and specifically states the types of costs recoverable and requires that the Commission approve a rate adjustment clause to provide for such costs to be recovered on a timely and current basis. This seems to provide for recovery of plant construction costs during the construction period (2-5 years), rather than over the facilities useful life (30-40 years).

(7) Subdivision 9 (lines 864-867) uses the term “*rate year*” which is not defined and is unclear as it relates to a refund of prior year over earnings, not a rate change. Also, allocating refunds based on the last approved revenue allocation used to design rates is outdated for most electric utilities.

(8) Subdivision 10 provides that in a biennial review the Commission may order refunds of all distribution and generation earnings more than 100 basis points above the fair return if “the total aggregate regulated rates of such utility were more than five percent, compounded annually, above the total aggregate regulated rates of such utility....” The parameter is unclear.

(9) Subdivision 11 (lines 892-899) provides that the Commission is not precluded from reviewing the prudence of costs during proceedings conducted pursuant to this section (except FERC approved costs). This language seems to conflict with specific language in subdivisions requiring Commission approval of specific costs. Further, the time allowed for Commission investigation is insufficient to allow for prudence reviews.

Date: 01/25/07 / sdl/cw/to

cc: Secretary of Commerce and Trade