
Technology & Economic Development Committee

HB 2002

Brief Description: Concerning regulatory and financial mechanisms and means to promote the retirement of coal-fired electric generation facilities.

Sponsors: Representatives Morris, Magendanz and Fitzgibbon.

Brief Summary of Bill

- Creates the Washington State Coal Generation Retirement Program, including certain cost-recovery, regulatory, accounting, and financing provisions related to the early retirement of coal-fired electric generation facilities (coal plants).
- Authorizes an electrical company or its financing subsidiary to issue bonds for costs related to the retirement of a coal plant, secured by a charge, to be paid by all customers within the electrical company's service area.
- Authorizes an electrical company to create financing subsidiaries to accomplish the acquisition or retirement of one or more coal plants, and exempts such subsidiaries from regulation by the Utilities and Transportation Commission (Commission).
- Requires the Commission to deem certain investments to be prudently incurred and consequently recoverable by a utility through its rates, including investments related to acquisition or retirement of an eligible coal plant and mitigation payments made to another state.
- Requires the Commission to designate service area boundaries at the request of a public utility.
- Exempts long-term financial commitments to incur eligible coal plant acquisition costs from Greenhouse Gas Emissions Performance Standards.
- Makes an electric utility that acquires service territory or customers from another utility that serves more than 25,000 retail customers in Washington subject to the conservation and renewable resource acquisition requirements of the Energy Independence Act.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Hearing Date: 2/12/15

Staff: Jasmine Vasavada (786-7301).

Background:

Washington Utilities and Transportation Commission.

The Washington Utilities and Transportation Commission (Commission) is a three member commission that has broad authority to regulate the rates, services, and practices of investor-owned utilities (IOUs) in the state of Washington, including electrical companies. As part of the ratemaking process, the Commission considers whether, and to what extent, an electrical company should recover the cost of a resource acquisition or the cost of an investment in a new generating facility. The decision is made on a case-by-case basis, taking into consideration whether the resource has been identified as a least-cost resource in the IOU's Integrated Resource Plan (IRP).

Integrated Resource Planning.

Investor-owned and consumer-owned electric utilities in the state with more than 25,000 customers must develop an IRP. An IRP must describe the mix of generating resources and conservation and efficiency resources that will meet current and projected needs at the lowest reasonable cost to the utility and its ratepayers. When determining the lowest reasonable cost for resources identified in its IRP, a utility must consider, among other factors, state and federal policies regarding resource preference and the cost of risks associated with environmental effects including emissions of carbon dioxide. According to IRPs filed in 2013, the three electrical companies serving customers in the state currently own or partially own 12 coal-fired generation facilities throughout several western states.

Traditional Rate Base, Rate-of-Return Regulation.

An electrical company has an obligation to serve all customers by making investments enabling it to provide electrical power. In return, the electrical company is assured an opportunity to earn a rate of return on those investments "prudently incurred". The value of property on which an electrical company is permitted to earn a specified rate of return is called the "rate base". The allowed rate of return varies, depending on the relative risk of the company. Utility regulators, including the Commission, uniformly apply the prudent investment rule, established by courts interpreting federal constitutional law. To receive its allowed rate of return and recover the costs of an investment, a utility must demonstrate that the course of action leading to the utility incurring the expense or making the investment was prudent, reasonable, and necessary. Applying this rule, the Commission may require an evaluation of the economics of continued operation of the facility, in light of information reasonably available at the time of the decision.

Traditional rate base, rate-of-return utility regulation divides the initial shareholder investment (original cost of an asset) between net book value (NBV) and accumulated depreciation. The NBV is the value of an asset as recorded in the accounts of its owner. It is equal to the original cost of the asset minus accumulated depreciation and amortization. The NBV represents the investment made by shareholders that has not already been recovered in rates. Accumulated depreciation equals the sum of all prior years' depreciation expense already recovered through rates. Rate base, rate-of-return regulation does not guarantee future income on assets that are no longer used to provide service.

Affiliated Interests.

In a rate case or other proceeding, the Commission may disallow all or part of the compensation or other payments made by an electrical company to an affiliated interest, under a contract or arrangement, unless the electrical company establishes the reasonableness of the payments. The Commission may investigate and disapprove a contract or arrangement with an affiliated interest, if the electrical company fails to prove the contract is in the public interest. The Commission may require satisfactory proof of the cost to the affiliated interest in performing its obligations under the contract or arrangement.

Greenhouse Gas Emissions Performance Standard for Electric Generation Plants.

Electric utilities are prohibited by state law from entering into a long-term financial commitment with a baseload generating facility, such as a coal-fired power plant, if the generating facility's carbon dioxide emissions exceed the state Greenhouse Gas Emissions Performance Standard.

"Long-term financial commitment" means:

- either a new ownership interest in baseload electric generation or an upgrade to a baseload electric generation facility; or
- a new or renewed contract for baseload electric generation with a term of five or more years for the provision of retail power or wholesale power to end-use customers in this state.

Utility Service Territories.

Most electric providers may serve any customer in the state, regardless of their historic service territory. Providers are allowed by state law to enter into voluntary contractual service territories and obligations. Approval by the Commission is required for participation in such agreement by an investor-owned utility.

Condemnation Authority.

Various political subdivisions and private corporations in the state have been delegated the power of eminent domain, including municipalities, public utility districts, and electric power companies.

Energy Independence Act "Qualifying Utilities."

Certain "qualifying utilities" must comply with conservation and renewable resource acquisition requirements of the Energy Independence Act. "Qualifying utility" means an electric utility that serves more than 25,000 customers in Washington.

Summary of Bill:

Washington State Coal Generation Retirement Program.

The Washington State Coal Generation Program (Program) is created, with the intent of giving investor-owned utilities (IOUs) secure and predictable regulatory and financial mechanisms that encourage early retirement of certain coal-fired electric generation facilities and a secure and predictable customer base to support the costs of such retirement. The Program is expressly intended to preempt any inconsistent regulation or order issued by any political subdivision of the state. The Program provides a number of regulatory and financial mechanisms that an electrical company may utilize in connection with a coal-fired electric generating facility, including:

- recovery of eligible coal plant acquisition costs in rates;
- recovery of mitigation payments made to another state in rates;
- the use of financing mechanisms, such as bonds, upon the filing of a binding notice; and
- the creation of financing subsidiaries.

In addition, the Program provides for the establishment and enforcement of utility service area boundaries.

The Utilities and Transportation Commission (Commission) shall, upon petition of an electrical company, issue such orders as may be necessary to implement the regulatory and financial mechanisms authorized, and shall not take any action to directly or indirectly diminish the value of any of the mechanisms.

Recovery of Eligible Coal Plant Acquisition Costs and Mitigation Costs.

An IOU that provides retail electric service (electrical company) may include in its rate base all eligible coal plant acquisition costs. An "eligible coal plant" is a coal-fired electric generating facility that provides a portion of its load to retail customers in the state and is owned, in whole or in part, by an electrical company providing service in Washington. "Eligible coal plant acquisition costs" means all costs and expenses incurred in connection with the acquisition of an additional or increased interest in any one or more eligible coal plants, which, as of the effective date of the act, provide electricity to retail electric customers in Washington. Such costs may include but are not limited to:

- any and all rights and obligations related to the ownership, operation, and control of an interest in an eligible coal plant; and
- any and all transaction costs, including legal fees, incurred by an electrical company in connection with such acquisition.

An electrical company required to pay another state for measures that mitigate the retirement of an eligible coal plant is also entitled to recover those costs from its ratepayers. Mitigation costs may include such things as financial assistance to affected communities, financial assistance to retrain displaced workers, and any new tax or fee imposed upon the electrical company. The electrical company is entitled to petition the Commission to recover in rates any transmission costs associated with the retirement of an eligible coal plant.

The Commission must deem eligible coal plant acquisition costs and mitigation costs to be reasonably and prudently incurred. The Commission must allow a rate of return on eligible coal plant acquisition costs that is no less than the rate of return authorized by the Commission in the electrical company's most recent rate proceeding.

Binding Notice.

If an electrical company files a binding notice (Notice), it may opt to recover eligible coal plant acquisition costs as:

- carbon reduction costs, through a carbon reduction charge assessed through ratepayers. To choose this option, the costs must be included in a Financing Order and must be removed from the rate base; or
- accelerated depreciation and amortization, recovered through rates.

The Notice sets forth the financial and regulatory mechanisms the utility requires to "irrevocably" commit to the retirement of one or more eligible coal plants. These may include:

- creation of a regulatory asset account;
- the right to accelerated depreciation and amortization; and
- the use of financing mechanisms, such as bonds.

The Notice must include a number of specified criteria, including a description of the eligible coal plant, a preliminary retirement plan, and whether carbon reduction bonds will be issued to finance the retirement. The Commission must accept the Notice, unless it determines, based on clear and convincing evidence, that the Notice does not comply with one of the identified criteria.

An electrical company is relieved of its obligation to retire an eligible coal plant if: (1) after a Notice has been accepted, the utility must install new or additional emission control measures as required by state or federal law; and (2) the cost of the measures exceed 10 percent of the net book value of the plant. "Net book value" for this purpose is determined as of the date of the Notice. In addition, a plant retirement may be deferred for purposes of reliability, if approved by the Commission.

Creation of a Regulatory Asset Account.

An electrical company has the right to place all or a portion of its net plant investment into a regulatory asset account. The net plant investment shall include:

- the net book value (NBV) of the retired eligible coal plant as of the date of retirement;
- any and all transmission or other costs related to the eligible coal plant and traditionally included in an electrical company's rate base; and
- any carbon reduction costs associated with the eligible coal plant that are not otherwise recovered by a carbon reduction charge.

The amount recoverable in the regulatory asset account may be amortized and recovered in rates over a period not to exceed 20 years. The rate of return must be no less than the rate of return authorized by the Commission in the electrical company's most recent rate proceeding.

The Right to Accelerated Depreciation and Amortization.

An electrical company shall have the right to accelerated depreciation and amortization of all or a portion of the company's net plant investment in an eligible coal plant that has been designated in a Notice. The net plant investment shall be:

- the NBV of the plant, as of the date of the Notice;
- all subsequent capital investments required to keep such plant in service prior to retirement;
- all transmission or other costs traditionally included in the electrical company's rate base; and
- any carbon reduction costs that are not otherwise recovered by a carbon reduction charge.

Carbon Reduction Costs.

An electrical company or its successors may recover carbon reduction costs from customers through a carbon reduction charge. "Carbon reduction costs" are defined broadly to include any cost or expense incurred, or to be incurred, by an electrical company in connection with the retirement of an eligible coal plant. These include, for example, costs and expenses related to:

- permanent decommissioning, stranding, or closure of the plant;
- remediation of environmental and human health threats; and
- any damages and expenses incurred in a legal proceeding arising "in connection with any such matters".

In addition, these include:

- financing costs; and
- the unrecovered value of property that is retired, including any demolition or similar cost that exceeds the salvage value of the property.

Securitized Bond.

An electrical company or its financing subsidiary may issue a bond or bonds to recover carbon reduction costs, secured by the "carbon reduction charge" paid by customers of an electrical company or its successors. The issuance requires approval by the Commission of a financing order. An application for a financing order must meet specified criteria, including a description of the retirement plan and associated costs, and a methodology for allocating carbon reduction charges among customer classes. The Commission must approve the bond application within 120 days of its receipt, unless it finds, based on clear and convincing evidence, that:

- the retirement plan is inconsistent with applicable law;
- the estimated carbon reduction costs are not supported by substantial evidence; or
- the financed carbon reduction costs will lead to exceeding the program limit.

The Commission may not alter the terms and conditions of an application. The Commission will periodically adjust the carbon reduction charges to provide for timely payment of scheduled principal of and interest and the payment and recovery of other financing costs. While the state or its subdivisions may invest in bonds, the state is not liable on bonds, and bonds are not a debt of the state.

Creation of Financing Subsidiaries.

An electrical company may create or acquire one or more financing subsidiaries, and laws providing for Commission regulation of an electrical company's contracts with an affiliated interest do not apply to financing subsidiaries created for one of the following purposes:

- issuing, facilitating, or administering carbon reduction bonds;
- facilitating or administering carbon reduction property;
- entering into contractual obligations secured by carbon reduction property for the purpose of financing carbon reduction costs; or
- any other incidental purpose, including the ownership and use of carbon reduction property.

"Carbon reduction property" means the right to collect carbon reduction charges and all revenues and proceeds arising from such rights. The state pledges it will not take or permit any action that impairs the value of carbon reduction property. The electrical company's right to the property accrues at the moment that it is designated in the financing order. Additional provisions regulate the sale, transfer, priority, conveyance, assignment, and perfection of security interests in carbon reduction property.

Program Limit.

For any electrical company that retires any one or more eligible coal plants under the Program, the amount of the electrical company's program investment may equal, but unless approved by the Commission, shall not exceed, 9.8 percent of its rate base as of the effective date of the Program, as adjusted for inflation. The Commission may at any time increase, but may not decrease, the program limit if it determines such increase is in the public interest. The "Program limit" is the total allowable "program investment", which is the sum of :

- the amount of the net plant investment in a "regulatory asset account";
- the amount of the net plant investment allowed as accelerated depreciation and amortization; and
- the amount of the carbon reduction costs to be incurred and paid from proceeds of carbon reduction bonds authorized by a financing order.

Exemption from Greenhouse Gas Emissions Performance Standard.

An electrical company may enter into a long-term financial commitment to supply baseload electric generation without complying with the Greenhouse Gas Emissions Performance Standard, if the following conditions are met:

- the financial commitment is one pursuant to which an electrical company incurs eligible coal plant acquisition costs; and
- the company, within 10 years of the act's effective date, files a binding notice to retire one or more eligible plants.

Utility Service Territories.

A public utility or cooperative has the right, to the exclusion of other public utilities or cooperatives, to provide retail electric service within its designated service area. No public utility or cooperative may extend service into an adjoining service area served by any other public utility or cooperative. If a public utility or cooperative that has been unable to reach an agreement designating a service area boundary petitions the Commission, the Commission shall issue an order determining service area boundaries within 180 days, and shall prepare a map.

Any electric utility that acquires territory or customers from a Qualifying Utility, in violation of a designated service area, is defined as a Qualifying Utility under the Energy Independence Act (Act), and is subject to the Act's conservation and renewable resource acquisition targets.

Condemnation.

If an IOU is damaged or impaired by any threatened or actual condemnation by the state or any of its political subdivisions, the IOU is entitled to recover full compensation for any severance damages.

Appropriation: None.

Fiscal Note: Requested.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.