

HOUSE BILL REPORT

ESHB 1589

As Amended by the Senate

Title: An act relating to supporting Washington's clean energy economy and transitioning to a clean, affordable, and reliable energy future.

Brief Description: Supporting Washington's clean energy economy and transitioning to a clean, affordable, and reliable energy future.

Sponsors: House Committee on Environment & Energy (originally sponsored by Representatives Doglio, Fitzgibbon, Berry, Alvarado, Bateman, Ramel, Peterson, Lekanoff, Hackney, Macri and Kloba).

Brief History:

Committee Activity:

Environment & Energy: 2/6/23, 2/13/23 [DPS].

Floor Activity:

Passed House: 3/6/23, 52-44.

Floor Activity:

Passed House: 1/22/24, 52-45.

Senate Amended.

Passed Senate: 3/1/24, 27-22.

Brief Summary of Engrossed Substitute Bill

- Prohibits any large gas company that serves more than 500,000 retail natural gas customers in Washington as of June 30, 2023, from providing natural gas service to any commercial or residential location that did not receive gas service or have filed applications for gas service as of June 30, 2023.
- Creates exemptions to the prohibition on the extension of natural gas service for certain types of facilities, including manufacturing, medical care, correctional, and military facilities.
- Requires the Utilities and Transportation Commission (UTC) to initiate a

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process by September 1, 2023, to consolidate utility planning requirements and to waive any UTC rules necessary to facilitate an integrated system plan.

- Requires a combination utility to file an integrated system plan by January 1, 2026, and every four years thereafter, that achieves certain specified objectives.
- Requires the UTC to establish by rule a cost-effectiveness test for certain emissions reduction measures taken by a combination utility.
- Requires the UTC to determine the appropriate, cost-effective cost recovery mechanisms for a combination utility to meet its integrated system plan.
- Requires the UTC to adopt specified depreciation schedules for any gas plant in service as part of any multiyear rate plan filed by a combination utility.
- Authorizes the UTC to approve a merger of the electric and gas rate bases of a combination utility if the UTC finds that the merger will result in a net benefit to the costumers of the combination utility.
- Establishes labor requirements for any project in a gas decarbonization plan or electrification plan with a cost of more than \$10 million.

HOUSE COMMITTEE ON ENVIRONMENT & ENERGY

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 9 members: Representatives Doglio, Chair; Mena, Vice Chair; Berry, Duerr, Fey, Lekanoff, Ramel, Slatter and Street.

Minority Report: Do not pass. Signed by 6 members: Representatives Dye, Ranking Minority Member; Ybarra, Assistant Ranking Minority Member; Abbarno, Barnard, Couture and Goehner.

Staff: Robert Hatfield (786-7117).

Background:

Utilities and Transportation Commission.

The Utilities and Transportation Commission (UTC) is a three-member commission with broad authority to regulate the rates, services, and practices of a variety of businesses in the state, including four natural gas companies. The UTC must ensure rates charged by these companies are fair, just, reasonable, and sufficient. In 2021 the Legislature directed every gas or electric utility filing a general rate case to include a proposal for a multiyear rate plan

beginning January 1, 2022.

Greenhouse Gas Emission Reduction Limits.

In 2020 the Legislature updated statewide greenhouse gas (GHG) emissions reduction limits to 45 percent below 1990 levels by 2030, 70 percent below 1990 levels by 2040, and 95 percent below 1990 levels, as well as net-zero emissions by 2050.

Clean Energy Transformation Act.

In 2019 the Legislature enacted the Clean Energy Transformation Act (CETA), which requires Washington's electric utilities to meet 100 percent of their retail electric load using non-emitting and renewable resources by January 1, 2045. Additionally, the CETA requires electric utilities to eliminate coal-fired resources from their allocation of electricity by December 31, 2025, and to make all retail sales of electricity GHG neutral by January 1, 2030.

Multiyear Rate Plan.

Every general rate case filing of a gas or electric utility before the UTC must include a proposal for a multiyear rate plan (MYRP). The UTC may by order after an adjudicative proceeding, approve, approve with conditions, or reject, an MYRP proposal made by a utility, an alternative proposal made by one or more parties, or any combination of these. The UTC's consideration of an MYRP proposal is subject to the same standards as other related filings, including that it be in the public interest and that the rates be fair, just, reasonable, and sufficient.

Summary of Engrossed Substitute Bill:

Prohibition on Gas Service Expansion.

A large gas company is prohibited from furnishing or supplying gas service, instrumentalities, and facilities to any commercial or residential location that did not receive gas service or file an application for gas service as of June 30, 2023. A large gas company is defined as a gas company that serves more than 500,000 retail natural gas customers in Washington on June 30, 2023.

The prohibition does not apply to facilities engaged in one or more manufacturing processes described by North American Industry Classification System codes beginning with 31, 32, or 33.

The prohibition does not apply to the following facilities until January 1, 2040:

- facilities with building occupancies classified as Institutional I-2 (medical care facilities) or I-3 (correctional facilities) pursuant to the International Building Code, that are required by federal or state regulation to have redundant emergency backup power generation systems; and
- facilities owned or operated by the United States Department of Defense that utilize reciprocating internal combustion engine generators that support energy resilience,

energy security, and energy efficiency initiatives.

Integrated System Plan.

By September 1, 2023, the Utilities and Transportation Commission (UTC) must initiate a process to consolidate utility planning requirements and to waive any UTC rules necessary to facilitate an integrated system plan. The UTC must issue a notice and request for comment and must hold a public comment hearing.

Subject to approval by the UTC, by January 1, 2026, and every four years thereafter, a combination utility must file an integrated system plan demonstrating how the combination utility plans to achieve certain objectives, including:

- achieve its legal obligations pursuant to the Climate Commitment Act, the Clean Energy Transformation Act, the Energy Independence Act, and existing pipeline safety and replacement plans, among other legal obligations;
- achieve gas utility and electric utility emissions reductions equal to their proportional share of statewide emissions reduction requirements; and
- maximize investments of revenues generated from consigning allowances pursuant to the Climate Commitment Act in programs that aid in the transition from the direct use of fossil fuels.

In addition to the above, an integrated system plan must satisfy a number of additional requirements, including, among others:

- include an emissions reduction target, and set forth specific actions that the combination utility will take to reduce greenhouse gas emissions to meet the emissions reduction target;
- present and evaluate a range of resource portfolios and proposed programs to advance clean energy and gas decarbonization measures;
- include programs targeted to low-income customers, vulnerable populations, and overburdened communities;
- prioritize investments in energy efficiency, demand response, and energy conservation measures;
- quantify projected cumulative greenhouse gas emissions reductions for each emissions reduction period resulting from each portfolio presented in the integrated system plan; and
- describe the effects of the specific actions and investments of each portfolio presented in the integrated system plan on the safety, reliability, and resilience of the combination utility's energy service.

The UTC must approve, reject, or approve with conditions the integrated system plan within 12 months of receiving the final plan. Once approved, a combination utility may include an integrated system plan in a proposal for a multiyear rate plan. In determining whether to approve the plan, the UTC must evaluate whether the plan is in the public interest according to a specified set of criteria, including whether the integrated system plan and the proposed actions in the plan are cost-effective and how the integrated system plan is likely to result in

a reasonable cost to customers.

The UTC must establish by rule a cost-effectiveness test for emissions reduction measures taken by combination utilities to comply with state clean energy and climate policies. The cost-effectiveness test must be used for the purpose of determining the cost-effectiveness of decarbonization measures taken by a combination utility. The UTC may approve, or amend and approve, an integrated system plan that exceeds the cost-effectiveness test only if it finds that the plan is in the public interest, costs to customers are reasonable, the plan includes mitigation of rate increases for low-income customers, and the benefits of the plan, including the costs of greenhouse gas emissions, exceed the costs.

The UTC must determine the appropriate, cost-effective cost recovery mechanisms for a combination utility to meet its integrated system plan including, among others:

- the majority of total capacity and energy necessary to meet the requirements of the Clean Energy Transformation Act to be supplied from resources owned and operated by the combination utility or an affiliate of the combination utility;
- a performance incentive mechanism;
- a return on generation assets and generation under contract based on the combination utility's authorized return on equity; and
- a return on power purchase agreements that is no less than the authorized cost of debt and no greater than the authorized rate of return of the combination company, multiplied by the operating expense incurred by the combination utility under the power purchase agreement.

Emissions Reduction Targets.

A combination utility must include the following in calculating its emissions baseline and projected cumulative emissions for an emissions reduction period:

- methane leaked from the transportation and delivery of gas from the gas distribution and service pipelines from the city gate to customer end use;
- greenhouse gas emissions resulting from the combustion of gas by customers not otherwise subject to federal greenhouse gas emissions reporting and excluding all transport customers; and
- emissions of methane resulting from leakage from delivery of gas to other gas companies.

In calculating an emissions reduction target, a combination utility must show its emissions baseline and projected cumulative greenhouse gas emissions for the applicable emissions reduction period separately and must show that the total emissions reductions are projected to make progress toward the achievement of the emissions reduction targets identified in the applicable integrated system plan. The final calculation must be presented on a carbon dioxide equivalent basis.

Depreciation Schedules and Single Energy Rate Base.

In any multiyear rate plan filed by a combination utility, the UTC must adopt depreciation

schedules for any gas plant in service. The incremental depreciation for each year of a multiyear rate plan is equal to 1 percent of the gas revenue requirement for the preceding year.

After the approval of an integrated system plan, the combination utility may propose a merger of the rate bases supporting gas and electric operations of the combination utility into a single energy rate base and the adoption of rates for electric and gas service that support the recovery of such a merged energy rate base. The UTC may approve the merger of electric and gas rate bases if the UTC finds that the proposal will result in a net benefit to customers of the combination utility.

For a combination utility that has merged gas and electricity rate bases, the combination utility must monetize benefits from any applicable federal and state tax incentives for the benefit of customers. These benefits must be separately accounted for and amortized on a schedule designed to mitigate the rate impacts to customers after the rate bases are combined. These credits may not be used for any other purpose.

Project Labor Agreements.

For any project in a gas decarbonization or electrification plan that is part of a competitive solicitation and that costs more than \$10 million, the combination utility must certify to the UTC that any work on the project will be constructed by contractors in a way that includes community workforce agreements or project labor agreements, the payment of area standard prevailing wages, and apprenticeship utilization requirements, provided the following apply:

- the combination utility and contractors have the absolute right to select any qualified and responsible bidder for the award of contracts on a specified project without referring to existing agreements, and a successful bidder is designated only when a bidder is willing, ready, and able to become a party to an agreement, signs a letter of assent, and complies with such an agreement; and
- it is a self-contained, stand-alone agreement, and the contractors are not obligated to sign any other local, area, or national agreement.

Electric Utilities.

Investor-owned and consumer-owned electric utilities are encouraged to:

- work with large gas companies providing gas service within their service areas to identify opportunities for electrification and the provision of energy peaking service by the large gas company;
- account for the costs of GHG emissions, set total energy savings and GHG emissions reduction goals, and develop and implement electrification programs in collaboration with large gas companies providing service; and
- include an electrification plan or transportation electrification program as part of a clean energy plan.

Definitions.

Several terms are defined including alternative energy resource, cost-effective, electrification, and emissions reduction period.

Title.

The act may be known as the Washington Decarbonization Act for Large Combination Utilities.

EFFECT OF SENATE AMENDMENT(S):

As compared to Engrossed Substitute House Bill 1589, the Senate amendment:

- removes the prohibition on the expansion of natural gas service to new commercial and residential locations by a large gas company;
- removes the modification to a large gas company's obligation to furnish natural gas service;
- amends the direction to the Utilities and Transportation Commission (UTC) to consolidate the planning requirements for a large combination utility in multiple ways, including:
 - by July 1, 2025, the UTC must complete a rule-making proceeding to implement consolidated planning requirements under multiple specified statutes for gas and electric service for large combination utilities;
 - by January 1, 2027, large combination utilities must file an integrated system plan demonstrating how the large combination utilities' plans are consistent with the requirements of the act and which achieve multiple other specified objectives, including that the utility achieve annual demand response and demand flexibility equal to or greater than 10 percent of winter and summer peak electric demand, and that the utility include a 10-year clean energy action plan for implementing the requirements of the Clean Energy Transformation Act at the lowest reasonable cost;
 - the UTC must establish by rule a cost test for emissions reduction measures achieved by large combination utilities to comply with state clean energy and climate policies; and
 - establishes criteria by which the UTC must approve, reject, or approve with conditions an integrated system plan;
- requires large combination utilities to work in good faith with specified energy stakeholders to develop market structures and mechanisms that require the sale of wholesale electricity from generating resources in a manner that allows the greenhouse gas attributes of those resources to be accounted for when they are sold into organized markets;
- authorizes the UTC to approve, reject, or approve with conditions an application for a certificate of necessity related to proposed investments in new or existing electrical generating capacity, or proposed power purchase agreements, that meet certain criteria;
- modifies the direction to the UTC to adopt an accelerated depreciation schedule for the gas plant of a large combined utility, to specify that the UTC must adopt a

depreciation schedule that depreciates all gas plants in service as of July 1, 2024, by a date no later than July 1, 2050;

- modifies the criteria by which the UTC may approve the merger of the electric and natural gas rate bases of a large combination utility, to include that the merger must include reasonable rate protections for low-income natural gas and electric customers;
- prohibits large combination utilities, beginning January 1, 2025, for residential customers and beginning January 1, 2031, for commercial and industrial customers, from offering any form of incentive or rebate to natural gas customers to purchase any natural gas appliance or equipment;
- requires, by November 1, 2025, a large combination utility to educate its ratepayers about the benefits of electrification and the availability of incentives to purchase energy efficient electric appliances;
- amends multiple statutes to conform with the direction to the UTC to complete a rule-making proceeding to implement consolidated planning requirements under multiple specified statutes for gas and electric service for large combination utilities;
- requires that the integrated system plan of a large combination utility, when the plan proposes electrification within an area in which a consumer-owned utility provides electrical service, to include a process for outreach by the large combination utility to each such consumer-owned electric utility in order for the consumer-owned electric utility to assess the sufficiency of the capacity of the electric distribution system to accommodate the projected additional electrical load; and
- makes changes to definitions.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect immediately.

Staff Summary of Public Testimony:

(In support) This bill represents a complementary policy to the Clean Energy Transformation Act and the Climate Commitment Act, both of which set aggressive decarbonization goals for gas and electric utilities. It will be a steep hill to climb to achieve those goals. This bill provides the right tools for Puget Sound Energy (PSE) to achieve those goals in the most cost effective way possible. The bill ensures PSE will have a balanced portfolio between purchased and owned resources. The bill would allow PSE to equitably distribute the benefits and burdens of electrification and decarbonization. It used to be that if the rates for everyone were the same, that was considered equitable, but some of those past assumptions are being reexamined and more equitable ways of approaching rates are being considered.

Climate change disproportionately affects low-income and BIPOC communities. The bill is an important step in reducing natural gas expansion. Natural gas in the residential sector is

currently responsible for almost half of Seattle's current carbon emissions. Electrification will cause a load increase, so it is important to work to prepare the electrical grid.

The bill prioritizes creation of family wage jobs through the use of project labor agreements and community workforce agreements.

It is important to transition to a clean energy economy, and businesses must be involved in that transition.

Buildings represent the fastest-growing sector of greenhouse gas emissions in Washington. The bill provides a pathway for the transition to clean energy. Recently adopted building codes require heat pumps. There is support for limiting the expansion of natural gas infrastructure. Converting from natural gas to electricity is a challenge. Some cities are promoting heat pump conversions in a number of ways, including through funding and streamlined permitting.

This bill is bold, complicated, and necessary. As natural gas sales decline, gas utilities will be unable to survive on their gas revenues. The bill provides a merger of the natural gas and electric rate bases. One policy question to address is whether the natural gas rate base should be shifted to other consumers of PSE, or whether the rate base should be shifted to the electric utilities that provide electricity to areas that get their natural gas, but not their electricity, from PSE.

The bill provides a pathway for incentivizing electric transmission and generation facilities. There is important labor and workforce language in the bill. The bill provides both certainty and opportunity.

(Opposed) There need to be some changes to make the bill workable. There are significant consumer protection concerns with the bill. There is no meaningful cost protection for customers related to the decarbonization and electrification plans. Nothing in the bill limits what PSE can spend on these plans, and cost control measures are very important to consumers. The requirement that PSE get 60 percent of its electricity from resources that PSE owns will increase costs to customers. Also, requiring a rate of return to PSE for its power purchase agreements is a windfall to PSE.

There is strong opposition for the anti-competitive provisions regarding electricity in the bill. There is intense interest in how to decarbonize the power structure. Carving out 60 percent of the clean energy market to be owned by one utility sacrifices the integrity of the whole sector in order to keep one utility whole. The bill gives PSE a profit center on each contract it enters into, with no benefit to customers. The bill undermines the premise of competition. Utilities received major advantages in the Inflation Reduction Act, including making it easier to monetize federal tax credits.

(Other) Natural gas is a fossil fuel, and decarbonizing a gas utility is a challenging

endeavor. There is much work to be done on the bill, and the devil is in the details. It is important that the bill allow the Utilities and Transportation Commission the authority to manage costs and ensure greenhouse gas reductions. If this bill is done right, it could provide a national model for transitioning utilities to electricity. Natural gas prices are one of the largest drivers of utility rates, and gas prices have been increasing significantly recently. It is important to understand the low-income provisions in the bill.

There need to be mandatory emissions reduction targets in the bill.

The bill should have language that calls for a reporting element with regard to labor usage.

Avista has a company goal of being carbon-neutral in natural gas by 2045. Full electrification for Avista would require doubling its current electrical consumption. Gas backup heat pumps are helpful. It is important to maintain the resilience and reliability of the electrical grid while advancing decarbonization goals in a cost sensitive way.

There is a recognition that there is a commitment to have the bill apply only to PSE, and no one else. The provisions in the bill do not work for a gas-only utility. There is a need to address how to handle rates in those areas where customers get their electricity from PSE but their gas from someone else. It is important to make sure the state does not create overburdened customers as a result of this bill.

It is important to ensure that labor standards and safety standards are met.

Hospitals are required to maintain redundant power services, so there needs to be a slight change in the wording of the bill. Hospitals have to have access to reliable power. As currently written, hospitals would not be able to access new gas connections. New hospitals, or current hospital in new locations, would need to have access to natural gas connections.

It is important to think through what it looks like to decarbonize the energy sector. There are both climate impacts and health impacts to burning natural gas inside the home. It is critical to begin planning now to make sure the transition to clean energy is affordable for all customers. The mechanisms in the bill are new, and it is important to continue to talk through their implementation.

There is support for the intent of the bill. One concern is that the bill provides certainty to the utility company, but there is a need to make changes to provide assurances to customers, including emissions reduction and cost control. The bill does not address protections for low-income customers, which is important to do.

The transition to clean energy needs to consider impacts on people, including people who manage the energy delivery system.

Persons Testifying: (In support) Representative Beth Doglio, prime sponsor; Mendy Droke, Seattle City Light; Sam Hem, Northwest Regional Council Sheet Metal, Air, Rail and Transportation Workers Local 66; Ken Johnson, Puget Sound Energy; Jim Lazar, Regulatory Assistance Project; Matthew Hepner, Certified Electrical Workers of Washington; Donny Donovan, International Association of Machinists and Aerospace Workers 751; and Jay Arnold, City of Kirkland.

(Opposed) Sommer Moser, Alliance of Western Energy Consumers; and Spencer Gray, Northwest and Intermountain Power Producers Coalition.

(Other) John Worthington; Anna Lising, Office of the Governor; Dave Danner, Utilities and Transportation Commission; Jennifer Ziegler, National Construction Alliance; Zosia Stanley, Washington State Hospital Association; Kurt Swanson, Washington State Association Plumbers and Pipefitters; Charlie Brown, Northwest Natural and Cascade Natural Gas; Christine Reid, International Brotherhood of Electrical Workers 77; Lauren McCloy, Northwest Energy Coalition; Kelly Hall, Climate Solutions; and John Rothlin, Avista.

Persons Signed In To Testify But Not Testifying: None.