

**Commonwealth of Virginia**

**State Corporation Commission**

**Report to the Commission on Electric Utility Regulation  
of the Virginia General Assembly**

**and the Governor of the Commonwealth of Virginia**



**Status Report: Implementation of The Virginia  
Electric Utility Regulation Act**

**Pursuant to § 56-596 B of the Code of Virginia**

**September 1, 2008**



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## INTRODUCTION

In 2008, the General Assembly amended § 56-596 B of the Code of Virginia to require the Virginia State Corporation Commission (“SCC” or “Commission”) to provide annual reports to the Governor and the General Assembly on the status of the implementation of the Virginia Electric Utility Regulation Act (the “Regulation Act”), and to offer recommendations for any actions by the General Assembly or others.<sup>1</sup> This report is tendered by the Commission in compliance with § 56-596 B.

During the past year, the SCC continued the scheduled implementation of components of the Regulation Act as required by statute. The majority of this report will highlight these activities.

We also note that the SCC, both by itself and as a member of the Organization of PJM States, Inc. (“OPSI”), continued to participate in various proceedings before the Federal Energy Regulatory Commission (“FERC”) this past year. While Virginia’s return to regulated retail rates alters the impact of PJM Interconnection, LLC (“PJM”)<sup>2</sup> electricity market outcomes on Virginia’s homes and businesses, PJM markets and processes are still important to the Commonwealth’s energy future. Nearly all of Virginia’s electric utilities are members of PJM and participate in the power markets that PJM operates. For example, Virginia’s electric cooperatives and municipal utilities and their retail customers are directly affected by exposure to PJM’s wholesale market electricity prices. Additionally, the electric investor-owned utilities continue their participation in PJM markets, with Virginia Electric and Power Company d/b/a

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<sup>1</sup> The SCC is not making any legislative recommendations in this report.

<sup>2</sup> PJM Interconnection, LLC is a regional transmission organization in the mid-Atlantic area comprising all or part of 13 states: Delaware, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia, and the District of Columbia. PJM attempts to ensure the reliable operation of the electric power supply system, facilitate an effective wholesale electricity market, and manage a long-term regional electric transmission planning process to maintain grid reliability and relieve congestion. Additional information is available at: <http://www.pjm.com>.

Dominion Virginia Power (“Virginia Power” or “DVP”) purchasing a significant portion of its energy needs and with Allegheny Power (“AP”) purchasing all or nearly all of its energy needs from PJM administered wholesale markets.

Accordingly, this report addresses matters before the Commission, as well as relevant FERC proceedings.

## IMPLEMENTATION OF THE REGULATION ACT

### Consumer Education

Under Code of Virginia § 56-592, the SCC is directed to develop and implement an electric energy consumer education program to provide retail customers with information regarding energy conservation, energy efficiency, demand-side management, demand response, and renewable energy. In establishing a consumer education program, the SCC is to:

- Take into account the findings and recommendations of the subgroup on Information/Consumer Education that participated in the proceeding in Case No. PUE-2007-00049;<sup>3</sup>
- Regularly consult with representatives of consumer organizations, community-based groups, state agencies, utilities, and other interested parties throughout the program's implementation and operation;
- Provide periodic updates on the program to the General Assembly's Commission on Electric Utility Regulation.

With the advice and assistance of interested stakeholders, the SCC is developing a consumer education program designed to strengthen awareness of electricity efficiency and conservation in Virginia households, businesses and institutions, thereby promoting informed and confident energy decisions. As stated in the Governor's Virginia Energy Plan released in

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<sup>3</sup> The SCC was directed to establish a proceeding to: (i) determine whether the ten percent electric energy consumption reduction goal can be achieved cost-effectively through the operation of such programs, and if not, determine the appropriate goal for the year 2022 relative to base year of 2006, (ii) identify the mix of programs that should be implemented in the Commonwealth to achieve cost-effectively the defined electric energy consumption reduction goal by 2022, including but not limited to demand-side management, conservation, energy efficiency, load management, real-time pricing, and consumer education, (iii) develop a plan for the development and implementation of recommended programs, with incentives and alternative means of compliance to achieve such goals, (iv) determine the entity or entities that could most efficiently deploy and administer various elements of the plan, and (v) estimate the cost of attaining the energy consumption reduction goal. The SCC established Case No. PUE-2007-00049 to respond to these directives.

September 2007, an expanded consumer energy education program will help overcome barriers to implementing energy efficiency and conservation actions.

It is currently envisioned that this program will provide Virginians with relevant information on available conservation and efficiency alternatives including their relative costs, energy savings and ease of implementation. It is important that this information be provided in a manner that is clear and easy to understand. The SCC will utilize a mix of materials and media designed to impact consumers throughout Virginia. The selective use of print, broadcast and web-based advertising will increase overall awareness. Public relations and grassroots outreach efforts will educate, inform and connect directly with consumers at the local level. Market research will be used to gain an understanding of consumer attitudes, to measure campaign progress, and refine the communications programs as needed.

The preparation of a plan to define and implement the consumer education program is underway. In drafting the plan, the SCC is relying on the recommendations and campaign framework produced by the subgroup on Information/Consumer Education that participated in Case No. PUE-2007-00049. This diverse group of interested stakeholders has given valuable input in the preliminary stages. In addition, the subgroup will continue contributing by reviewing and commenting on the preliminary draft of the plan, will meet in the early fall of 2008 to finalize their recommendations, and will be invited to serve as an education advisory committee to the SCC during the implementation of the program.

The finished plan will be reported to the Commission on Electric Utility Regulation in late 2008. To support the SCC in the development and implementation of the program, the SCC anticipates that it will seek solicitations in early 2009 from firms capable of assisting with outreach, website development and advertising. The energy efficiency and conservation program will be operational in the summer of 2009.

## **Rules Governing Retail Access**

The Rules Governing Retail Access to Competitive Energy Services (“Retail Access Rules”)<sup>4</sup> adopted by Commission Order in Case No. PUE-2001-00013,<sup>5</sup> currently consist of 12 sections in Chapter 312 (20 VAC 5-312-10 *et seq.*) of Title 20 of the Virginia Administrative Code and pertain to various relationships among the local distribution companies, competitive service providers and retail customers.

In light of the Regulation Act, the Commission Staff (“Staff”) proposed revisions to the Retail Access Rules to reflect the new requirements. The Commission initiated Case PUE-2008-00061 on July 29, 2008 and seeks comments to the Staff’s proposal by September 22, 2008. The Commission notes that under the Regulation Act, mass market retail competition is scheduled to end on December 31, 2008, while retail choice remains for large commercial and industrial customers and for certain aggregated load beyond 2008. Since January 1, 2003, six competitive service providers (“CSP”) and five aggregators have registered with DVP to provide service within its Virginia territory. Only one CSP, Pepco Energy Services (“PES”), currently provides any service in DVP’s territory. PES serves 1,211 residential customers and 18 commercial customers with higher-priced “green” power as of August 1, 2008. To date, no CSP has registered with AP or Appalachian Power Company (“APCo”) or any electric cooperative to provide service within their respective Virginia service territories.

The Commission remains responsible under §§ 56-587 and 56-588 of the Code of Virginia for licensing suppliers and aggregators interested in participating in the retail access

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<sup>4</sup> The rules were to be developed for both a competitive electricity market and a competitive natural gas market. Our focus in this report is the electricity market.

<sup>5</sup> The Rules Governing Retail Access to Competitive Energy Services are available on the Commission’s website at: <http://www.scc.virginia.gov/eaf/csp.aspx>.

programs in Virginia. The Staff established a streamlined mechanism for processing license applications<sup>6</sup> and an internal deadline of 45 days from the receipt of a complete application to the issuance of a license.<sup>7</sup> Thus far, that deadline has been met for nearly all of the CSP applications. Currently, 28 electric and natural gas CSPs and aggregators renewed their licenses with the Commission in 2008 to participate in retail access and one new natural gas CSP applicant was granted a license on July 23, 2008. A current list of licensed suppliers can be found at <http://www.scc.virginia.gov/power/compsup.aspx>.

### **Renewable Tariff**

One component of the Regulation Act redefines the eligibility of customers to choose an electricity CSP. After the termination of capped rates on December 31, 2008, large non-residential customers with at least 5 MW of load will continue to have the ability to choose competitive electricity supply. Smaller non-residential customers may petition the Commission for permission to aggregate such load to meet the 5 MW threshold to maintain the ability to choose a CSP.

Residential customers will retain the ability to choose only a CSP offering supply from a 100% renewable resource, provided that the local distribution company does not offer a Commission approved tariff for electricity supplied 100% from renewable energy pursuant to § 56-577 A 5 of the Regulation Act.

Two investor-owned utilities have submitted applications to the Commission for approval of a tariff to provide renewable energy options. Virginia Power submitted its initial application on May 29, 2008, and a supplemental application on June 11, 2008, for approval of

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<sup>6</sup> Guidelines to become licensed as a competitive service provider or aggregator are available on the SCC's website at: <http://www.scc.virginia.gov/eaf/csp.aspx>.

<sup>7</sup> Section 56-235.8 F 1 of the Code of Virginia established a 45-day deadline for natural gas CSPs and the Staff has used this deadline internally for all CSP applications.

its Rider G Renewable Energy Program. The Commission issued an Order for Notice and Comment on July 8, 2008, in Case No. PUE-2008-00044, seeking comments and company responses by October 14, 2008. As noted previously, some customers in northern Virginia currently taking electricity supply from PES will be directly affected by the outcome of this application.

APCo submitted its application on July 1, 2008, for approval of its Renewable Power Rider. The Commission issued an Order for Notice and Comment on July 23, 2008, in Case No. PUE-2008-00057, seeking comments and company responses by October 31, 2008.

### **Distributed Generation**

Distributed generation involves moving the generation of electricity away from large central units to smaller units located closer to the point of consumption. In accordance with Code of Virginia § 56-578, the Commission instructed its Staff to work with interested parties to develop proposed interconnection standards for distributed generation. Section 56-578 specifies that the interconnection standards “shall not be inconsistent with nationally recognized standards acceptable to the Commission.”

The Commission issued an Order Establishing Proceeding, in Case No. PUE-2008-00004, to consider interconnection standards for distributed generation for the Commonwealth in accordance with Code of Virginia § 56-578 C. The Staff developed proposed rules to meet the statutory requirements that were attached to the Order, and interested persons have been given an opportunity to comment thereon. This case is currently pending before the Commission, and a final order will be issued before the end of the year.

### **Net Metering**

Amendments to § 56-594 of the Code of Virginia: (1) increase the allowable total aggregate generation capacity of net metering customers in each utility's Virginia service territory from 0.1% to 1.0% of the utility's adjusted Virginia peak-load forecast in the previous year; and (2) require each utility, upon written request of a net metering customer, to enter into a contract to purchase the generation that exceeds the customer's own usage for the 12-month net metering period at a rate approved by the Commission, unless the parties agree to a higher rate.

Accordingly, the Commission established Case No. PUE-2008-00008 to amend the Regulations Governing Net Energy Metering, 20 VAC 5-315-10 *et seq.*, previously adopted by the Commission in Case No. PUE-2006-00073, to reflect the statutory changes. The Staff prepared proposed rules that were attached to the Order, and interested persons were given an opportunity to comment thereon. Comments regarding the Staff's proposal were received in late June. The Commission issued its Order Adopting Final Regulations on August 7, 2008.

### **Generation and Transmission Additions**

Since 1998, 12 generating plants have been built and placed into commercial operation within the Commonwealth, adding 4,450 megawatts ("MW") to existing generation facilities physically located in Virginia.<sup>8</sup> Certificates to construct six additional facilities were granted by this Commission with capacities totaling 3,865 MW. Four of these projects did not develop and their certificates expired. The remaining two did not develop, but the proposed construction sites were purchased by Virginia Power. Three other certificate applications have been granted

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<sup>8</sup> These new plants are comprised of four Dominion generating stations (aggregating to 1,800 MW), two ODEC facilities (aggregating to 940 MW), and six independent power plants (aggregating to 1,710 MW).

by the Commission. The respective projects, including a 39 MW wind turbine facility, a 150 MW combustion turbine extension, and a 585 MW circulating fluidized bed coal facility, are in various stages of development. Currently, one project for a natural gas-fired combined cycle facility in Buckingham County is pending before the Commission, Case No. PUE-2008-00014. The table at the end of this section provides further detail regarding such applications.

Virginia utilities continue to expand their transmission facilities. Five short transmission lines that were granted approval by the Commission are now under construction. Eight additional certificate applications are pending before the Commission.<sup>9</sup>

As a result of PJM's Regional Transmission Expansion Planning process focusing on 2011 needs, PJM has approved two proposed 500 kV or above bulk transmission projects as the best solutions for addressing regional transmission reliability concerns (including Northern Virginia) by improving west-to-east power flows. These include a 500kV transmission line project from 502 Junction in Pennsylvania to Mt. Storm, West Virginia, proposed to be built by an affiliate of Allegheny Power known as "TrAILCo"<sup>10</sup> that connects a joint TrAILCo/DVP 100-mile 500 kV transmission line from Mt. Storm to Loudoun County in Virginia. These two lines in combination are referred to as the TrAILCo project. Pursuant to a FERC order that is subject to further litigation, the cost of these lines will be allocated in proportionate share to all loads in PJM including those in Virginia.

The Commission's Hearing Examiner issued his report to the Commission on July 29, 2008 in Case Nos. PUE-2007-00031 and PUE-2007-00033, recommending approval of the TrAILCo transmission line. His recommendation is conditioned upon the regulatory approval

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<sup>9</sup> The list of such projects appears on the summary table following this section. Additionally, several new natural gas pipelines were approved by FERC and are either in service or nearing completion.

<sup>10</sup> Or, the Trans-Allegheny Interstate Line Company.

in West Virginia<sup>11</sup> and Pennsylvania.<sup>12</sup> PJM has also approved two DVP proposed projects, a 56-mile 500 kV Carson to Suffolk line and a 26-mile 230 kV Suffolk to Thrasher line to address reliability concerns in Eastern Virginia. These proposals are pending before the Commission, and final orders thereon will be issued before the end of the year.

American Electric Power (“AEP”) and Allegheny Power recently proposed a new 765 kV-500 kV transmission line stretching from West Virginia to Maryland, referred to as the Potomac-Appalachian Transmission Highline (“PATH”). AEP states that the proposed line is designed to relieve transmission congestion and enhance west-to-east power flows and reliability. The utilities intend to submit applications to the respective state commissions during December, 2008. A portion of the 500 kV PATH line may pass through Loudoun County and a portion of the 765 kV PATH line may pass through Frederick County. If so, SCC approval will be required.

DVP is studying the possible construction of up to two more nuclear generating units at its North Anna Power Station. In 2003, DVP filed an application with the Nuclear Regulatory Commission (“NRC”) for an early site permit, which was approved in November, 2007. Shortly thereafter, Dominion submitted an application to the NRC for a combined operating license at North Anna.

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<sup>11</sup> The Public Service Commission of West Virginia on August 1, 2008, approved Allegheny Power’s plans to build the portion of the TrAILCo project traversing across northern West Virginia.

<sup>12</sup> On August 21, 2008, Administrative Law Judges recommended the Pennsylvania Public Utility Commission not authorize the construction of the TrAILCo project through Pennsylvania.

**Summary of Construction Activity in Virginia**  
**As of August 1, 2008**

<i>Company/Facility</i>	<i>Size</i>	<i>Location</i>	<i>Docket</i>	<i>Fuel</i>	<i>C.O.D.*</i>	<i>Hearing</i>	<i>Order</i>
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**New power plants in operation**

Commonwealth Chesapeake	300 MW	Accomack County	PUE960224	3-OilCT	sum 01	1/23/97	8/5/98
Dominion Virginia Power	600 MW	Fauquier County Remington	PUE980462	4-GasCT	sum 00	1/05/99	5/14/99
Wolf Hills Energy, LLC	250 MW	Washington County Bristol	PUE990785	5-GasCT	sum 01	4/27/00	5/2/00
Dominion Virginia Power	360 MW	Caroline County Ladysmith	PUE000009	2-GasCT	sum 01	5/23/00	10/10/00
Doswell Limited Partnership	171 MW	Hanover County Doswell	PUE000092	1-GasCT	sum 01	6/13/00	6/15/00
Allegheny Energy Supply	88 MW	Buchanan County	PUE010657	2-C/GCT	Jun 02	none	6/25/02
Dominion Virginia Power-Possum	540 MW	Prince William County PP	PUE000343	convert/GasCC	May 03	1/16/01	3/12/01
Louisa Generation, LLC (ODEC)	472 MW	Louisa County BoswillTavr	PUE010303	5-Gas CT	Jun 03	11/14/01	7/17/02
Tenaska Virginia Partners I, LP	885 MW	Fluvanna County	PUE010039	Gas CC	May 04	3/13/02	4/19/02
INGENCO Wholesale Power, LLC	16 MW	Chesterfield County	PUE-2003-00538	48-LFGas	Jun 04	none	4/12/04
Marsh Run Generation, LLC (ODEC)	468 MW	Fauquier County	PUE020003	3-GasCT	Sep 04	5/21/02	11/6/02
Dominion Virginia Power	300 MW	Caroline County	PUE-2007-00032	2-dualCT	Jun 08	none	8/24/07

**4,450 MW**

**Power plants granted SCC certificates**

Highland New Wind Development	39 MW	Highland County	PUE-2005-00101	19-wind	fall 07	7/17/07	SCC app 12/20/07
Dominion Virginia Power	150 MW	Caroline County	PUE-2007-00032	1-dualCT	sum 09	none	SCC app 3/19/08
Dominion Virginia Power	585 MW	Wise County	PUE-2007-00066	CFBCoal	sum12	1/8/08	SCC app 3/31/08

**774 MW**

**New power plants that have applied for an SCC certificate**

Appalachian Power Company-Financing	(629 MW)	Mason County, WV	PUE-2007-00068	IGCC	sum12	2/12/08	SCC deny 4/14/08
Tenaska Virginia Partners II, LP (8/15/01) extended 1/8/07, site sold to DVP – see	(900 MW)	Buckingham County	PUE010429	Gas CC	n/a	5/28/02	SCC app 1/9/03, renewal
Dominion Virginia Power	580 MW	Buckingham County	PUE-2008-00014	Gas CC	sum10	9/30/08	pending
CPV Warren, LLC (3/07 renewal) sold to DVP 3/4/08, not yet filed	(520 MW)	Warren County	PUE-2007-00018	2-GasCC	spr 05	7/24/02	SCC renew 6/20/07 site

**580 MW**

\*Commercial Operation Date

<b><u>Company/Facility</u></b>	<b><u>Size</u></b>	<b><u>Location</u></b>	<b><u>Docket</u></b>	<b><u>C.O.D.</u></b>	<b><u>Order</u></b>
<b><u>Transmission lines</u></b>					
DVP Brambleton-Greenway	230kV – 8 mi	Loudoun	PUE-2002-00702	12/08	10/8/04 approved, under construction
DVP Pleasant View-Hamilton	230kV- 16 mi	Loudoun	PUE-2005-00018	6/10	2/18/08 & 5/28/08 approved, under construction
DVP Bristers-Gainesville	230kV – 16 mi	Fauquier & Prince William	PUE-2006-00048	5/09	11/13/06 approved, under construction
DVP Garrisonville	230kV - 5mi	Stafford	PUE-2006-00091	6/09	4/8/08 approved, under construction
DVP Carson-Suffolk-Thrasher	500/230kV-82 mi	Dinwiddie-Suffolk	PUE-2007-00020	6/11	pending
DVP Meadowbrook-Loudoun	500kV	Northern Virginia	PUE-2007-00031	6/11	pending
DVP Clinch River-VA City	138kV – 9 mi	Wise & Russell	PUE-2007-00111	11/10	7/9/08 approved, under construction
DVP Ladysmith	230kV - 5mi	Caroline	PUE-2008-00002	5/10	pending
DVP Beaumeade-NIVO	230kV – 1 mi	Loudoun	PUE-2008-00063	4/10	pending
APCo Lake Forest	138kV – 3 mi	Botetourt	PUE-2007-00113	6/09	pending
APCo Duty	138kV – 2mi	Buchanan	PUE-2008-00006	12/08	pending
APCo Sunscape	138kV – 3mi	Roanoke City	PUE-2008-00053	6/10	pending
TrailCo Mt Storm-Meadowbrook	500kV	Frederick, Warren	PUE-2007-00033	6/11	pending
<b><u>Natural gas pipelines</u></b>					
DVP	20” – 14 mi	Prince William County	PUE000741	2003	SCC app 11/5/01, in-service 7/03
Duke Energy Patriot Extension	24”-95 mi	Wythe to Rockingham Cty	FERC	2004	FERC app 11/20/02, in service 2/04
Dominion Transmission Greenbrier	30”-279 mi	Charleston to Rockingham	FERC	2007	FERC app 4/9/03, cancelled 1/07
Saltville Gas Storage Co., LLC	24”-7 mi	Saltville / Chilhowie	PUE010585	2003	SCC approved 1/22/03, in-service 8/03
Cove Point East Pipeline capacity expansion	87 mi	Maryland to Loudoun	FERC	fall 2008	FERC approved
Cove Point LNG terminal capacity expansion	9.6BCF storage	Cove Point, Maryland	FERC	fall 2008	FERC approved
<b><u>Regional Transmission Organization membership</u></b>					
AP (PJM West)	PUE-2000-00736	Order of 10/8/04 approving transfer of operation of transmission facilities to PJM West, implemented 3/1/02.			
AEP (PJM West)	PUE-2000-00550	Order of 8/30/04 approving transfer of operation of transmission facilities to PJM West, implemented 10/1/04.			
DVP (PJM South)	PUE-2000-00551	Order of 11/10/04 approving transfer of operation of transmission facilities to PJM, implemented 5/1/05.			

### **Certificate of Public Convenience and Necessity Requirements**

On July 25, 2008, the Commission initiated a rulemaking proceeding, Case No. PUE-2008-00066, prompted by recent statutory changes to § 56-580 D of the Code of Virginia pertaining to the Commission's approval and certification of any electric generation facility proposed by such utilities for construction and operation in the Commonwealth. The Commission's Order seeks comments from interested persons by September 26, 2008, to the Staff's proposed amendments to the Commission's Generation Rules reflecting: (i) the newly-reestablished "need" showings required of Virginia's regulated electric utilities; (ii) the policy objectives established by Virginia's newly enacted integrated resource planning ("IRP") statutes; and (iii) expedited review of proposed electric generation facilities of 5 MW or less in capacity.

### **Integrated Resource Planning Requirements**

Chapter 476 (Senate Bill 311) of the 2008 Acts of Assembly established a mandatory IRP requirement for Virginia's jurisdictional electric utilities.<sup>13</sup> As established by this legislation, IRPs provide forecasts of electric utilities' expected load obligations (projected over a 15 year period), and the utilities' plans to meet these load obligations over that period through supply side and demand-side resources. According to Code of Virginia § 56-597, the IRPs are intended to "promote reasonable prices, reliable service, energy independence and environmental responsibility." The Staff is developing a proposal for the information requirements to be included with the IRP filings Virginia's electric utilities are to make by September 1, 2009, and to be updated biennially thereafter. The Commission expects to initiate a rulemaking proceeding regarding the Staff's proposal later this fall.

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<sup>13</sup> Senate Bill 311 added a new Chapter 24 (§ 56-597 *et seq.*) in Title 56 of the Code of Virginia.

## **Renewable Portfolio Standards**

As evidenced by the Governor's Virginia Energy Plan and actions by the General Assembly to afford, among other things, incentives for regulated electric utilities to implement or increase the sale of electricity from renewable sources through development of a program emphasizing a renewable energy portfolio standard ("RPS"), the Commonwealth's interest in developing alternative energy sources continues to grow. On December 3, 2007, the Commission established a proceeding, Case No. PUE-2007-00107, pursuant to the General Assembly's enactment of § 56-585.2 G of the Code of Virginia directing the Commission to "promulgate such rules and regulations as may be necessary to implement the provisions of this section including a requirement that participants verify whether the RPS goals are met in accordance with this section." Upon consideration of the evidence and comments submitted in this case, the Commission found that its existing rules are adequate to implement the provisions of § 56-585.2 G of the Code of Virginia.

APCo filed with the Commission an application seeking approval to participate in a voluntary RPS program, pursuant to § 56-585.2 B of the Code of Virginia. In its application, APCo stated that to further the General Assembly's goal of increasing the amount of renewable energy used within the Commonwealth, § 56-585.2 was enacted to allow electric utilities to participate in an RPS program with voluntary RPS Goals that commence in 2010 and reach certain target levels by 2021. The Commission established a proceeding to consider the application and received comments thereon from interested persons and Staff (Case No. PUE-2008-00003). On August 11, 2008, the Commission issued a Final Order approving the application. The Final Order, among other things, found APCo had demonstrated that it has a reasonable expectation of achieving 12% of its base year electricity sales from renewable energy sources during calendar year 2022.

## **Conservation, Energy Efficiency and Demand Response**

Chapter 933 of the 2007 Acts of Assembly includes as the Third Enactment clause, among other provisions, as follows:

That it is in the public interest, and is consistent with the energy policy goals in § 67-102 of the Code of Virginia, to promote cost-effective conservation of energy through fair and effective demand side management, conservation, energy efficiency, and load management programs, including consumer education. These programs may include activities by electric utilities, public or private organizations, or both electric utilities and public or private organizations. The Commonwealth shall have a stated goal of reducing the consumption of electric energy by retail customers through the implementation of such programs by the year 2022 by an amount equal to ten percent of the amount of electric energy consumed by retail customers in 2006.

The Commission established a proceeding on June 8, 2007, Case No. PUE-2007-00049, to: (i) determine whether the 10% electric energy consumption reduction goal can be achieved cost-effectively through the operation of such programs, and if not, determine the appropriate goal for the year 2022 relative to base year of 2006, (ii) identify the mix of programs that should be implemented in the Commonwealth to achieve the defined electric energy consumption reduction goal cost-effectively by 2022, including but not limited to demand-side management, conservation, energy efficiency, load management, real-time pricing, and consumer education, (iii) develop a plan for the development and implementation of recommended programs, with incentives and alternative means of compliance to achieve such goals, (iv) determine the entity or entities that could most efficiently deploy and administer various elements of the plan, and (v) estimate the cost of attaining the energy consumption reduction goal. On December 14, 2007, the Commission provided a report, (Senate Document No. 17, 2007) to the Governor and the General Assembly to satisfy these directives. The report noted, among other things, that the electric energy consumption reduction goal is achievable.

On January 17, 2008, the Commission issued an Order approving nine pilot projects ("Pilots") proposed by DVP.<sup>14</sup> The Commission found that DVP's nine new Pilots, in addition to the extension of DVP's compact fluorescent bulb ("CFL") bulb program, are necessary in order to acquire information which is or may be in furtherance of the public interest, specifically how the Commonwealth's goal of reducing energy demand by 10% by 2022 may be reached. The Commission further found that the public interest is served by approving the application without hearing so that implementation of the Pilots and collection of the data for 2008 will not be delayed.

In addition, the Commission stated that DVP should be prepared quickly to expand any elements of these Pilots that prove to be cost effective, noting that Virginia Power must follow up its Pilots with aggressive action to expand use of energy efficiency, conservation, and demand management programs as called for in the Virginia Energy Plan.

DVP implemented all of the Pilots and filed its first quarterly report on July 1, 2008 regarding the status of the programs. On August 15, 2008, DVP supplemented its report stating that all of the programs were fully subscribed or near full subscription. DVP has informally kept the Staff apprised of its progress, and DVP will submit its next formal report around October 1, 2008.<sup>15</sup>

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<sup>14</sup> The Pilots include five conservation and energy efficiency Pilots: (i) Standard Residential In-Home Energy Audits ("Residential Audit"), (ii) ENERGY STAR® Qualified Homes Energy Audits ("Energy Star"), (iii) Energy Efficiency Welcome Kits ("Welcome Kit"), (iv) PowerCost Monitor pilot ("PCM"), and (v) Small Commercial On-Site Energy Audits ("Commercial Audit"); and four demand response/load management Pilots: (i) Direct Load Control — Outdoor Air-Conditioning Control Device ("DLC"), (ii) Programmable Thermostats — Indoor Air-Conditioning Control Device ("PT"), (iii) Programmable Thermostats with Advanced Metering Infrastructure ("AMI") and Critical Peak Pricing ("CPP") (collectively "AMI/ CPP"), and (iv) Distributed Generation/Load Curtailment Pilot ("DG/LC"). Seven of the Pilots are proposed to run through December 2008. The Programmable Thermostats with AMI and CPP Pilot would run through May 2009, and the Distributed Generation/Load Curtailment Pilots are proposed to run through December 31, 2014.

<sup>15</sup> According to its press release on June 19, 2008, DVP unveiled an energy conservation plan aimed at cutting emissions, reducing energy usage and saving customers millions of dollars over the next 15 years. The key component to DVP's plan is the replacement of existing electric meters with new "smart meters" to enable new technologies to provide new possibilities for energy conservation. The utility hopes to implement the plan next year following an expected and detailed application with the Commission seeking approval of such programs.

## **Additional Regulatory Proceedings**

### **Appalachian Power**

#### *General Rate Case*

APCo has filed two general rate cases during the capped rate period. Most recently, on May 30, 2008, APCo filed an application<sup>16</sup> for a general rate increase pursuant to Chapter 10 of Title 56 and § 56-582 of the Code of Virginia, and the Commission's Rate Case Rules. APCo requests an increase in its annual base revenues of \$207.9 million, or 23.9%, based on a return on common equity of 11.75%. In its Order of Notice and Hearing and Suspending Rates, issued June 6, 2008, the Commission, among other things, suspended the proposed rates through October 27, 2008, and set the matter for public hearing on October 29, 2008. If APCo implements its rates prior to a final decision in this case, such rates will be interim, and subject to refund with interest.<sup>17</sup>

#### *Adjustments to Capped Rates for Environmental and Reliability ("E&R") Costs*

On July 16, 2007, APCo filed its application<sup>18</sup> to revise the E&R Factor established in Case No. PUE-2005-00056, effective December 1, 2007. This new E&R Factor was designed to recover \$59.5 million of incremental E&R costs incurred during the period October 2005 to September 2006. The matter was the subject of a hearing on November 5, 2007. On December 13, 2007, the Commission issued its Final Order in this proceeding, authorizing an E&R Factor designed to collect \$48.9 million over a one-year period effective January 1, 2008. This E&R Factor is to cease for service rendered after December 31, 2008.

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<sup>16</sup> Case No. PUE-2008-00046, *Application of Appalachian Power Company, For an increase in electric rates.*

<sup>17</sup> Under § 56-238 of the Code of Virginia the Commission can only suspend rates for 150 days. After that time a utility may implement its requested rate increase. If the Commission later approves a lower amount, the utility must refund any amounts overcollected with interest.

<sup>18</sup> Case No. PUE-2007-00069, *Application of Appalachian Power Company, For adjustment to capped electric rates pursuant to § 56-582 B (vi) of the Code of Virginia.*

On May 30, 2008, APCo filed its most recent application<sup>19</sup> to adjust capped rates pursuant to § 56-582 B (vi) of the Code of Virginia to revise its surcharge for the recovery of its E&R costs. In its current application, APCo requests that its E&R Factor be revised effective January 1, 2009 to recover approximately \$66.5 million of E&R costs incurred during the period October 2006 to December 2007. The proposed E&R Factor would be effective for one year, through December 31, 2009. The Commission issued its Order of Notice and Hearing on June 6, 2008 that, among other things, suspended implementation of the E&R Factor pending further order of the Commission, and set the matter for hearing on September 17, 2008.

*Rate adjustment factor to recover generation facility costs*

On July 16, 2007, APCo filed an application<sup>20</sup> pursuant to § 56-585.1 A 6 of the Code of Virginia, to recover financing costs associated with an Integrated Gasification Combined Cycle (“IGCC”) power plant proposed to be built in West Virginia. Based on the Regulation Act, APCo requested that the Commission: (1) approve its proposed rate adjustment clause, including an enhanced rate of return on common equity capital for a “clean-coal powered” facility, to be effective January 1, 2009, (2) find that construction of the proposed IGCC facility is reasonable and prudent, and (3) grant APCo other relief as necessary. The proposed rate adjustment clause was designed to recover the carrying costs on construction expenditures made from July 1, 2007 through December 2009. APCo proposed to track actual costs and recoveries and true-up any differences in subsequent years. The application projected the revenue requirement to be recovered during 2009 to be \$45.4 million, based on a return on equity of 14.0%. On August 9, 2007, the Commission issued an Order for Notice and Hearing

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<sup>19</sup> Case No. PUE-2008-00045, *Application of Appalachian Power Company, For adjustment to capped electric rates pursuant to § 56-582 B (vi) of the Code of Virginia.*

<sup>20</sup> Case No. PUE-2007-00068, *Application of Appalachian Power Company, For a rate adjustment clause pursuant to § 56-585.1 A 6 of the Code of Virginia.*

which, among other things, established a procedural schedule and set the case for hearing on February 12, 2008.

The Commission issued its Final Order in this proceeding on April 14, 2008, denying APCo's requests, finding that the IGCC facility was not reasonable or prudent based on the record before the Commission. On April 29, 2008 APCo filed a Petition for Reconsideration and/or Rehearing, which the Commission denied by Order dated May 29, 2008.<sup>21</sup>

#### *Fuel case*

On July 16, 2007, APCo filed an application<sup>22</sup> pursuant to § 56-249.6 of the Code of Virginia, to, among other things: (1) decrease its fuel factor from 2.030 cents/kWh to 1.614 cents/kWh effective September 1, 2007, and (2) concurrently terminate the Off-System Sales ("OSS") Margin Rider established in Case No. PUE-2006-00065. The net effect of these proposed changes would result in an annual increase in revenues of approximately \$33.4 million. On August 20, 2007, the Commission issued an order that, among other things, established a procedural schedule for the case, scheduled an evidentiary hearing for November 8, 2007, allowed APCo's proposed fuel factor to go in effect on an interim basis subject to refund on September 1, 2007, and terminated the OSS Margin Rider on an interim basis for bills effective September 1, 2007. The Commission issued its Order Establishing Fuel Factor<sup>23</sup> on February 1, 2008, which decreased APCo's fuel factor to 1.418 cents/kWh effective February 4, 2008, and made permanent the termination of the OSS Margin Rider. This order increased APCo's annual operating revenues by approximately \$4.0 million.

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<sup>21</sup> APCo also filed on May 13, 2008, a Notice of Appeal to the Supreme Court of Virginia of the Commission April 14, 2008 Final Order; however, such Appeal was subsequently withdrawn on June 26, 2008.

<sup>22</sup> Case No. PUE-2007-00067, *Application of Appalachian Power Company, To revise its fuel factor pursuant to § 56-249.6 of the Code of Virginia*.

<sup>23</sup> On February 29, 2008, Old Dominion Committee for Fair Utility Rates filed a Notice of Appeal to the Supreme of Virginia. Such Appeal was subsequently withdrawn on May 15, 2008.

On July 18, 2008, APCo filed its most recent application<sup>24</sup> pursuant to § 56-249.6 of the Code of Virginia to increase its fuel factor from 1.418 cents/kWh to 2.255 cents/kWh effective September 1, 2008. The proposal would increase revenues approximately \$132.5 million on an annual basis, or 15%. The typical bill of a residential customer using 1000 kWh per month would increase approximately 11.7%. The Commission issued an Order Establishing 2008-2009 Fuel Factor Proceeding on July 21, 2008, which, among other things, established a procedural schedule including an evidentiary hearing on September 23, 2008, and allowed an interim Factor of 2.255 cents/kWh to take effect on September 1, 2008.

### **Dominion Virginia Power**

#### *Rate adjustment factor to recover generation facility costs*

On July 13, 2007, Virginia Power filed an application<sup>25</sup> for approval, certification, and a rate adjustment clause under §§ 56-585.1, 56-580 D, and 56-46.1 of the Code of Virginia with regard to a carbon capture compatible, clean-coal powered electric generation facility it proposed to construct in Wise County, Virginia. Based on the Regulation Act, DVP requested that the Commission: (1) grant a certificate and approval to construct and operate a coal plant, (2) establish a general rate of return on equity of 11.75% and authorize an additional 200 basis points of return above 11.75%, (3) find that the competitive bidding rules do not apply, or alternatively, grant exemptions for certain portions of such rules, (4) approve a proposed rate rider to be effective January 1, 2009, and (5) provide other relief as necessary. The proposed rate rider was designed to recover the carrying costs on construction expenditures made from inception of the project through December 2009. Virginia Power proposed to track actual costs

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<sup>24</sup> Case No. PUE-2008-00067, *Application of Appalachian Power Company, To revise its fuel factor pursuant to § 56-249.6 of the Code of Virginia.*

<sup>25</sup> Case No. PUE-2007-00066, *Application of Virginia Electric and Power Company, For a certificate of public convenience and necessity to construct and operate an electric generation facility in Wise County, Virginia, and for approval of a rate adjustment clause under §§ 56-585.1, 56-580 D, and 56-46.1 of the Code of Virginia.*

and revenue recoveries and true-up any differences in subsequent years. DVP's projected revenue requirement for calendar year 2009 is \$83.3 million, resulting in an average monthly increase of \$1.53 to a residential customer with usage of 1000 kWh. On August 9, 2007, the Commission issued its Order for Notice and Hearing which, among other things, established a procedural schedule and set the case for hearing on January 8, 2008.

On March 31, 2008, the Commission issued a Final Order that: (1) granted Virginia Power a certificate of public convenience and necessity to construct and operate the generation facility in Wise County, Virginia; (2) established a general rate of return on equity of 10.0% and, as subsequently proposed in a stipulation by Virginia Power and several parties in the case, authorized an additional 100 basis points of return above 10.0% for this coal facility; (3) granted a limited exception to the bidding rules; and (4) approved a rate rider to be effective January 1, 2009, subject to true-ups beginning in 2010. On April 18, 2008, the Southern Environment Law Center, filed on behalf of itself, Appalachian Voices, Chesapeake Climate Action Network, Sierra Club, and Southern Appalachian Mountain Stewards, a Notice of Appeal of the Commission's March 31, 2008 Final Order to the Supreme Court of Virginia.

#### *Fuel case*

On May 6, 2008, DVP filed an application<sup>26</sup> to increase its fuel factor from 2.232 cents/kWh to 4.245 cents/kWh effective July 1, 2008. The proposed increase included recovery of \$231 million of the projected \$697 million June 30, 2008 deferred fuel balance. The \$231 million represented the amount to be recovered by increasing the total June 30, 2008 rates of the residential class by 4%. Virginia Power concurrently filed a Proposed Rule that would (1) defer recovery of the \$231 million prior period costs for one year and (2) provide for

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<sup>26</sup> Case No. PUE-2008-00039, *Application of Virginia Electric and Power Company, To revise its fuel factor pursuant to Code of Virginia § 56-249.6.*

recovery of the entire June 30, 2008 deferred balance over three years beginning July 1, 2009. The net effect of the above proposals was a fuel factor of 3.893 cents/kWh.

On May 9, 2008, the Commission issued its Order Establishing 2008-2009 Fuel Factor Proceeding that, among other things, established a procedural schedule, required public notice, set the case for hearing, and permitted the filing of legal memoranda addressing the legal permissibility of the Proposed Rule. A hearing was held on June 24, 2008, at which several case participants presented a proposed Stipulation and Recommendation for Commission consideration. The stipulation provided for recovery of \$231 million of the June 30, 2008 deferred fuel balance, and further provided for the deferral of \$231 million of the projected current fuel costs without carrying costs, resulting in a fuel factor of 3.893 cents/kWh. If the Stipulation was accepted, Virginia Power requested that it be permitted to withdraw its Proposed Rule.

On June 27, 2008, the Commission issued its Order Establishing Fuel Factor which, among other things, approved a fuel factor of 3.893 cents/kWh, and approved the Proposed Stipulation and Recommendation.

#### *Bidding Program*

On August 8, 2008, Virginia Power submitted an application to abandon its established bidding program pursuant to 20 VAC 5-301-10 *et seq.* in addition to revise its cogeneration tariff pursuant to PURPA Section 210. The application is pending before the Commission.

## **Delmarva Power**

### *Transfer of Service Territory and Facilities to A&N Electric Cooperative*

On July 2, 2007, Delmarva and A&N Electric Cooperative filed a joint application<sup>27</sup> and a joint petition<sup>28</sup> for, among other things, approval of Delmarva's sale of its Virginia service territory and facilities to A&N Electric Cooperative. In a related matter, A&N Electric Cooperative filed an application<sup>29</sup> on July 13, 2007, for approval of special rate schedules to be applicable to A&N's new customers in the former Delmarva Virginia service territory. The Commission issued its Order for Notice and Comment in these matters on July 18, 2007, setting a procedural schedule.<sup>30</sup>

On October 19, 2007, the Commission entered its Order Granting Approval, wherein, among other things, it approved the joint applications and joint petitions, allowed the sale of Delmarva's Virginia service territory and facilities to A&N Electric Cooperative and Old Dominion Electric Cooperative, approved a special rate for A&N Electric Cooperative, and required that on or before January 1, 2012, A&N Electric Cooperative file a base rate case with a cost-of-service study encompassing the post-acquisition service area footprint to establish cost-based rates for the combined system.

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<sup>27</sup> Case No. PUE-2007-00061, *Joint Application of A&N Electric Cooperative and Delmarva Power and Light Company, For approval of certificates of convenience and necessity.*

<sup>28</sup> Case No. PUE-2007-00060, *Joint Petition of A&N Electric Cooperative and Delmarva Power and Light Company, For approval of purchase and sale of service territory and facilities.*

<sup>29</sup> Case No. PUE-2007-00065, *Application of A&N Electric Cooperative, For approval of special rates pursuant to § 56-235.2 of the Code of Virginia.*

<sup>30</sup> Also concurrently considered by the Commission were Case No. PUE-2007-00062, *Joint Petition of Old Dominion Electric Cooperative and Delmarva Power and Light Company, For approval of purchase and sale of transmission facilities* and Case No. PUE-2007-00063, *Joint Application of Old Dominion Electric Cooperative and Delmarva Power and Light Company, For approval of certificates of convenience and necessity.*

## **Allegheny Power**

### *Fuel cases*

On April 12, 2007, Allegheny Power filed an application<sup>31</sup> with the Commission to implement a levelized fuel factor to recover its purchased power expenses incurred between July 1, 2007 and June 30, 2008. The projected factor, for full recovery of projected purchased power costs, would have increased its capped generation rate of 3.456 cents/kWh to 6.123 cents/kWh. Due to the substantial increase, Allegheny Power proposed a three year phase-in of the rate increase. On June 28, 2007, the Commission entered an order denying AP's application and its May 10, 2007 Motion to Establish Interim Rates.

Allegheny Power appealed the Commission's decision to the Supreme Court of Virginia. On April 11, 2008, the Supreme Court issued its order affirming the Commission's denial of Allegheny Power's requested rate increase.

On September 11, 2007, Allegheny Power filed an application<sup>32</sup> to increase rates to recover a portion of the projected purchased power costs, to take effect in October 2007 and requested that any over- or under-recovery of actual purchased power costs be subject to true-up during its next fuel and purchased power proceeding. Allegheny Power also requested that the Commission authorize interim rates effective October 16, 2007 to recover an increase of \$44.9 million in annual revenues. On October 10, 2007, the Commission issued its Order of Notice and Hearing that, among other things, established a procedural schedule and denied Allegheny Power's request for interim rates.

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<sup>31</sup> Case No. PUE-2007-00026, *Application of Potomac Edison Company d/b/a Allegheny Power, for an increase in electric rates pursuant to Code of Virginia §§ 56-249.6 and 56-582.*

<sup>32</sup> Case No. PUE-2007-00085, *Application of Potomac Edison Company d/b/a Allegheny Power, for an increase in electric rates pursuant to Code of Virginia §§ 56-249.6 and 56-582.*

On December 20, 2007, the Commission issued its Final Order authorizing a levelized purchased power factor of .306 cents/kWh. This rate increases Allegheny Power's annual revenues by approximately \$9.5 million. The Commission further ordered that Allegheny Power track the over- or under-recovery of such approved purchased power costs and file, on or before July 1, 2008, an application requesting rate treatment of (1) such over- or under-recovery and (2) projected purchased power costs for the twelve months beginning July 1, 2008. On January 16, 2008, Allegheny Power filed its Notice of Appeal to the Supreme Court of Virginia of the Commission's December 20, 2007 Final Order. The appeal is pending.

On April 30, 2008, Allegheny Power filed an application<sup>33</sup> with the Commission to implement a levelized purchased power factor to recover its purchased power expenses incurred between July 1, 2008 and June 30, 2009, along with proposed alternative methods to calculate such a factor. On May 8, 2008 the Commission issued its Order for Notice and Hearing that, among other things, established a procedural schedule including an evidentiary hearing, allowed an interim factor of 2.351 cents/kWh to take effect July 1, 2008, asked for legal memoranda addressing AP's claim of financial distress as well as other legal issues raised by Allegheny Power, and scheduled oral argument on such legal issues.

On July 18, 2008, the Commission issued an Order finding that, as a matter of law, the applicability of the Memorandum of Understanding's ratemaking provisions, used to determine the cost of power recoverable by Allegheny Power, would cease on December 31, 2008. The Order set forth a number of questions and assertions to be considered by the Commission in deciding this case. On August 15, 2008, the Office of the Attorney General filed a Notice of Appeal of this Commission Order with the Supreme Court of Virginia.

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<sup>33</sup> Case No. PUE-2008-00033, *Application of Potomac Edison Company d/b/a Allegheny Power, for an increase in electric rates pursuant to Code of Virginia §§ 56-249.6 and 56-582, and, alternatively, request to Modify Memorandum of Understanding and Order in Case No. PUE-2000-00280.*

## **Rate Case Rules**

On January 29, 2008, the Commission initiated a proceeding to revise its current Rules Governing Utility Rate Increase Applications and Annual Informational Filings, 20 VAC 5-200-30. The Commission established this proceeding primarily to accommodate statutory changes creating a new mechanism for regulating electric utilities, which includes a mandated rate case in 2009 as well as subsequent biennial reviews of rates. The Commission's January 29, 2008 Order included Proposed Rules<sup>34</sup> drafted by the Staff, and permitted interested parties to comment on the Proposed Rules and request Oral Argument. The Staff has met with each utility that filed comments as well as the Office of the Attorney General and submitted a report with revised Proposed Rules. Interested parties may file replies to the Staff report and an oral argument will be held on September 16, 2008.

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<sup>34</sup> A new Chapter 201 in Title 20 of the Virginia Administrative Code, consisting of sections 20 VAC 5-201-10 through 20VAC5-201-80.

## **RTE PARTICIPATION**

Section 56-579 G of the Code of Virginia requires the Commission to report annually “its assessment of the practices and policies of the RTE.”<sup>35</sup> APCo, Allegheny Power, and DVP, as well as ODEC, are currently participating in PJM, a RTE.<sup>36</sup> This report will discuss recent developments in RTE participation and the impacts of RTE operations on the energy market.

As a result of requirements set forth in Code of Virginia § 56-579 A, Virginia’s largest electric utilities have now been integrated into PJM for at least three years. Consequently, the Commission Staff continues to gather and review data to facilitate a better understanding of the implications of PJM membership on the utilities and to assess the effectiveness of the electric utility industry in the Commonwealth. This task remains extremely difficult given the sheer volume of PJM’s operating rules and the complexities associated with the transmission grid. Although § 56-579 draws the Commission’s attention to policies and tasks made by and for Virginia and resulting PJM market outcomes, Virginia utilities will continue to participate in PJM markets and processes in substantial ways. For example, Virginia’s electric cooperatives and municipal utilities and their retail customers still face significant exposure to PJM wholesale market electricity prices. Also, Virginia Power currently purchases a significant portion of its energy needs from PJM-administered wholesale markets. In addition, Virginia’s utilities participate in PJM demand response programs and are impacted by PJM’s proposed construction of major bulk transmission lines. Thus, PJM matters to Virginia.

Prices associated with PJM’s energy markets are based on a system of locational

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<sup>35</sup> “RTE” is an acronym for the term “regional transmission entity.”

<sup>36</sup> PJM accepted control of Allegheny’s transmission facilities on April 1, 2002, AEP’s on October 1, 2004, and Virginia Power’s on May 1, 2005.

marginal prices (“LMP”), where the price for a given time increment is based on the offer to sell electricity submitted by the last, or highest-priced, unit needed to operate during that time period, as selected through a competitive auction. All units selected during this time interval receive the same payment based on the last selected bid, i.e. the “market clearing” price. Virginia’s electricity consumers are impacted to the extent that their utilities purchase electricity from the PJM market. For a more detailed description of LMP and its effects on Virginia, see Appendix A.

## **SIGNIFICANT RTE-RELATED DOCKETS AT FERC**

The Regulation Act directs the Commission to participate “to the fullest extent permitted” in RTE-related dockets at the FERC (§ 56-579 C of the Code of Virginia). Section 56-579 G also directs the Commission to provide an annual report to the CEUR concerning the Commission’s assessment of the RTE’s practices and policies and a description of the Commission’s actions regarding requests for transfer of ownership or control of transmission facilities to an RTE and the economic effects of such proposed transfers.

### **PJM’s Reliability Pricing Model**

On August 31, 2005, PJM filed under sections 205 and 206 of the Federal Power Act (“FPA”) a proposal for a reliability pricing model (“RPM”) to replace its then current capacity obligation rules. The RPM is a proposal to fundamentally change the manner and dollar amounts that generating units are paid for making generating capacity available to participate in the PJM markets. PJM’s RPM proposal attempts to address a key concern that competitive markets will not ensure adequate development of new generating capacity at reasonable cost to consumers. Accordingly, the goal of RPM is to incent the right amount of supply-side and demand-side infrastructure to ensure grid reliability and a target reserve margin. The proposed RPM is, in large part, an administrative mechanism that will set generator payments at the intersection of an auction-based supply curve and an administratively determined demand curve. The annual auctions would solicit capacity offers for one year to four years into the future. The intersection of those points will yield an administratively determined level of capacity necessary to provide adequate reliability. This process is done separately for different sub-regions within PJM to take into account regional deliverability issues. The proposal also includes a reliability backstop feature that has PJM enter into long-term contracts for capacity if

the capacity auction fails to produce a sufficient level of capacity necessary to meet PJM reliability requirements.

FERC established the matter as Docket Nos. EL05-148 and ER05-1410. On April 20, 2006, FERC issued an “initial” order in this matter that found PJM’s existing capacity construct was unjust and unreasonable. No evidentiary hearing had been conducted.

In comments filed in these dockets, the Commission stated that, like FERC, it is “well aware that there must be an adequate supply of generation for the near- and long-term future.” The Commission expressed concern with PJM’s proposed RPM since, to that date, there had been no showing that PJM’s proposed capacity market redesign will, or can, provide additional generation at just and reasonable rates. The Commission advised FERC that the RPM, as proposed, would increase the cost of generation to customers today and that proponents of the RPM have not established that customers will receive more than an empty promise for their increased payments.

The Commission’s position is that PJM has not established that a capacity construct based on the proposed RPM will result in just and reasonable rates nor has PJM demonstrated that its proposal will resolve resource adequacy problems. In addition, the Commission’s position is that PJM has not established that the proposed RPM will move its market closer towards transparency and competitiveness and that, in fact, the RPM may make these goals more elusive. The Commission closed its June 1, 2006 comments by re-stating its position that FERC should reject PJM’s RPM filing.

By order of December 22, 2006, FERC accepted a contested settlement agreement in these dockets subject to certain modifications. The Commission did not join this settlement. PJM thereafter conducted four transitional auctions under the procedures approved by FERC. On May 30, 2008, a number of interested parties, including the Maryland Public Service

Commission, the Delaware Public Service Commission, the Pennsylvania Public Utility Commission and the New Jersey Board of Public Utilities, filed a complaint at FERC, alleging that "PJM's Reliability Pricing Model ('RPM'), as implemented through the "transitional" Base Residual Auctions, has produced unjust and unreasonable capacity prices." The Commission subsequently intervened in support of the complaint, reiterating its earlier statements to FERC that PJM had never, and still has not, demonstrated that the RPM construct would result in just and reasonable rates.

### **Issues Related to PJM's Market Monitoring Function**

The SCC and its Staff have long been concerned with market monitoring issues at PJM. OPSI has shared these concerns as well. Last year's report to the CEUR detailed an ongoing dispute between PJM and its Market Monitoring Unit ("MMU") that culminated in OPSI filing a complaint regarding actions by PJM that impair the independence and effectiveness of its MMU and that constitute violations of the PJM Market Monitoring Plan contained in Attachment M to PJM's Open Access Transmission Tariff, as well as FERC's Orders and the Federal Power Act. PJM subsequently filed a contested unilateral Offer of Settlement, purporting to resolve outstanding issues in these two consolidated complaints regarding PJM's ongoing pattern of interfering with the independence and judgment of its internal MMU. OPSI opposed the proposed settlement. FERC issued an order finding that PJM had not violated its tariff in dealing with the putatively independent market monitor, but finding that the structure may have become unjust and unreasonable. FERC therefore required the parties to attempt to settle the dispute and create a new structure for market monitoring.

Under the supervision of John Moot, former General Counsel of FERC, and other members of FERC staff, OPSI,<sup>37</sup> PJM, the PJM Market Monitor and other interested parties

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<sup>37</sup> Whose President was, at that time, SCC Commissioner Mark C. Christie.

met numerous times to negotiate a compromise. On December 19, 2007, virtually all of the parties participating in the negotiations, including OPSI and the Commission acting in its individual capacity, filed a Settlement Agreement with FERC. Under the Settlement, the PJM MMU was moved to an external unit, led initially by the existing internal PJM Market Monitor. The Settlement Agreement also put in place a number of safeguards insisted upon by OPSI, including access to data relied upon by the Market Monitor in issuing reports and drawing conclusions, the ability of state regulators to request additional analyses from the Market Monitor, and creation of a committee to ensure continuing oversight of the MMU by state regulators. FERC approved the Settlement Agreement on March 21, 2008, and the external MMU is formally set to begin operating independently on August 1, 2008.

#### **FERC NOPR on Wholesale Competition in Regions with Organized Markets**

FERC held two technical conferences in 2007 to address issues related to wholesale competition in regions with functioning RTEs. As a result of these technical conferences, FERC issued an Advanced Notice of Proposed Rulemaking on June 22, 2007 and a Notice of Proposed Rulemaking (“NOPR”) on February 22, 2008, proposing substantive changes to the rules governing RTEs and their markets in four areas: demand response, long-term contracting, market monitoring, and RTE/ISO<sup>38</sup> responsiveness.

OPSI submitted comments in response to the NOPR on May 9, 2008. In general, OPSI supported FERC's initiatives regarding demand response and long-term contracting, but expressed some reservations as to proposals that could diminish the access achieved in the PJM MMU settlement. For example, OPSI opposed FERC's proposal to have state commissions petition FERC on a case-by-case basis for access to information from an RTE, and recommended that any rules reflect the data availability practices established in the Settlement.

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<sup>38</sup> “ISO” is an acronym for the term “independent system operator”.

In addition, while OPSI supported efforts to increase the responsiveness of RTE boards and upper management to stakeholders and market participants, OPSI opposed proposals for hybrid RTE/ISO boards that include stakeholders as RTE/ISO board members because "[s]takeholders such as generation and transmission owners already have substantial clout and voting rights within many of the various committees that develop RT[E]/ISO policies. Board membership would only strengthen stakeholder clout at a crucial stage in the process without providing for effective counterweights."

## **CLOSING**

As described in this report, the Commission continues to implement the various components of the Virginia Electric Utility Regulation Act. As stated previously, the SCC does not tender any legislative recommendations at this time but stands ready to provide additional information or assistance if requested.

**APPENDIX A**

**DESCRIPTION OF**

**LOCATIONAL MARGINAL PRICING**

## **DESCRIPTION OF LOCATIONAL MARGINAL PRICING**

Since the various components of the transmission system have differing levels of capacity, PJM has to control flows across its system so that no single transmission element becomes overloaded. PJM controls transmission flows by dispatching generating units based both on the bids of the units and physical conditions. The results of this dispatch are the basis for LMPs throughout the PJM region. LMPs within PJM are typically not uniform for each time interval since the PJM grid cannot always reliably accommodate a free flow of power throughout the entire PJM footprint.

During these constrained periods, market clearing prices begin to separate throughout PJM to reflect the accessibility of load to generation or conversely of generation to load. In effect, the LMP system recognizes that PJM's electricity market segments into smaller markets as the ability of the transmission grid to reliably accommodate economic transfers of power decreases. Unfortunately, transmission flows are a function of an ever-changing set of conditions that include but are not limited to generating unit availability and output, transmission configuration, and load levels. As such, the size of a particular electrical market is never static.

Generally, electrical markets separate and become smaller as the electrical system becomes more constrained. As markets grow smaller they become less competitive since the available universe of buyers and sellers shrink. During unconstrained periods there are many buyers and sellers. At the other extreme, when the system is very constrained, a relevant electrical market may consist of a single buyer or seller. In other words, the competitive playing field is often not level or balanced. The field typically becomes less balanced as the transmission system becomes more constrained. As such, the degree of

separation in LMPs throughout PJM can provide insights with regard to the competitiveness of the electrical system for a given area.

While the degree of LMP price separation within PJM can provide insights as to the competitiveness of the segmented electrical markets, factors other than transmission constraints can contribute to the degree of price separation and the degree of price separation is not an absolute indicator of competitiveness. The greatest difference in price between regions may not correspond with the time when the system is the most constrained due to other factors that may impact LMPs. For example, LMP price differences may be greater when the spread between fuel prices, i.e. between coal and gas prices, is higher even if dispatch and transmission flows are identical.

LMP prices can also be used as indicators of what competitive prices would be in the absence of regulation or price caps. The LMP market is in effect a spot market where the spot price of electricity is clearly defined. Once again, however, LMP prices should not be viewed as an absolute indicator of the market price of electricity. Competitive prices may also be derived through bilateral contracts or auctions. While not absolute, LMP is a reasonable indicator of potential market prices since they may also form the basis for longer-term pricing arrangements. Such arrangements will likely reflect expectations of LMPs over the terms of those arrangements as well as the risk premiums or discounts that may be required as a result of risk aversion.

Given the insights that can be obtained from LMPs, the Staff has collected LMP information and analyzed that information in a number of ways. The following table presents the load-weighted monthly average day-ahead LMPs for the Virginia zones of AEP, AP, DVP, and the entire PJM footprint for the 12 months ending June, 30, 2008.

The load weighted LMP price is a better indicator of market prices in that the actual costs incurred to serve load will vary with the respective load and price for the varying time intervals. LMPs paid by loads vary hourly.

**Average Monthly Load Weighted LMP**

	<i>AEP</i>	<i>AP</i>	<i>DVP</i>	<i>PJM</i>
	/MWh	/MWh	/MWh	/MWh
<b>Jul</b>	\$ 45.46	\$ 58.21	\$ 72.41	\$ <b>59.27</b>
<b>Aug</b>	\$ 62.22	\$ 69.75	\$ 85.50	\$ <b>72.82</b>
<b>Sep</b>	\$ 42.00	\$ 52.09	\$ 63.72	\$ <b>52.06</b>
<b>Oct</b>	\$ 51.70	\$ 59.28	\$ 69.65	\$ <b>60.42</b>
<b>Nov</b>	\$ 49.43	\$ 53.83	\$ 71.94	\$ <b>58.96</b>
<b>Dec</b>	\$ 47.21	\$ 58.49	\$ 68.82	\$ <b>60.22</b>
<b>Jan</b>	\$ 53.59	\$ 69.35	\$ 82.50	\$ <b>68.68</b>
<b>Feb</b>	\$ 57.01	\$ 71.63	\$ 74.61	\$ <b>67.73</b>
<b>Mar</b>	\$ 59.78	\$ 68.63	\$ 70.80	\$ <b>69.26</b>
<b>Apr</b>	\$ 60.14	\$ 71.96	\$ 77.23	\$ <b>71.87</b>
<b>May</b>	\$ 47.76	\$ 58.77	\$ 72.68	\$ <b>62.88</b>
<b>Jun</b>	\$ 75.80	\$ 187.25	\$ 126.67	\$ <b>102.76</b>
<b>12 Months</b>	\$ <b>54.46</b>	\$ <b>73.25</b>	\$ <b>78.44</b>	\$ <b>67.49</b>

The Staff has also examined differences in hourly LMP prices for the Virginia Zones and PJM in an attempt to gain insights as to the degree of market segmentation impacting operation in the Commonwealth. During periods of congestion, prices will be higher or lower in the various zones depending on each zone's access to specific generating units. If a given zone has less access to low cost generation as a result of transmission congestion it will experience higher LMPs. Conversely, zones that have

lower cost generation that would otherwise be dispatched in the absence of transmission congestion would see lower LMPs when the system is congested. For example, the average hourly LMP for the AEP zone exceeded the PJM-wide average LMP during only 33 hours and was below the PJM-wide average LMP during 8,751 hours during the twelve months ending June, 2008. On the other hand, LMPs in the Dominion zone were lower during only 987 hours and higher than the PJM-wide average LMP during 7,797 hours for this same period. This indicates that the AEP zone generally has access to lower cost generation while the Dominion zone has far less access to cheaper generation.