

COMMONWEALTH OF VIRGINIA  
STATE CORPORATION COMMISSION

AT RICHMOND, DECEMBER 15, 2004

APPLICATION OF

GORDONSVILLE ENERGY, L.P.

CASE NO. PST-2002-00046

Application for review and  
correction of assessment of  
the value of property subject  
to local taxation-Tax Year 2002

OPINION OF THE COMMISSION

Before the State Corporation Commission ("Commission") is the application of  
Gordonsville Energy, L.P. ("Gordonsville Energy" or the "Company"), for review and correction  
of the tax year 2002 assessment of the value of its property subject to local taxation. On  
January 1, 2002, Gordonsville Energy was an electric supplier as defined in § 58.1-2600 of the  
Code of Virginia ("Code"). As required by § 58.1-2633 of the Code, the Commission assessed  
the value of the Company's generating equipment, vehicles, general plant equipment, and  
materials and supplies located in Louisa County at \$151.863 million for tax year 2002. (Ex. 10  
at 1.)<sup>1</sup> In this proceeding, Gordonsville Energy maintains that the fair market value of its  
generating equipment was \$56,414,000; the fair market value of other equipment was \$39,000;  
and the fair market value of real property, including land, was \$3,347,000, for a total of  
\$60,000,000 (Ex. 5 at 4 and Section 15-2.)

The Commission's assessment of value cannot be compared directly with Gordonsville  
Energy's proposed fair market value. As required by § 58.1-2604 A of the Code, we must apply

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<sup>1</sup> The Commission assessed value of \$147,663,860 by Assessment Order of September 3, 2002, In re The Assessment of Water, Heat, Light, and Power Corporations, Electric Suppliers, and the Gas and Pipeline Distribution Corporations for 2002. (Ex. 1, GELP 1.) By Supplemental Assessment Order of March 3, 2004, In re Gordonsville Energy, L.P., Matter No. PST-2004-0000 3217, we made an additional assessment for tax year 2002 of \$4,179,248. (Ex. 10, Attachment 13.) The assessments sum to \$151,863,164.

the ratios reported by the Department of Taxation in arriving at the assessed values reported to the localities. While the Commission's assessments for tax year 2002 reflect the reported ratio for Louisa County, 0.899 (Ex. 9 at 6 and Attachment 8), Gordonsville Energy's witness did not apply the ratio in arriving at fair market value. In addition, the Company's witness maintained that its real property, including leased land, had a fair market value of \$3,547,000. (Ex. 5 at 4 and Section 15-2.) The Commission interpreted § 58.1-2628 D of the Code in effect for tax year 2002 to exclude leased land from central assessment. (Ex. 9 at 2-3.) Although these valuations may not be directly compared, the magnitude is apparent. The issue before us is whether Gordonsville Energy has rebutted the presumption that our assessment of \$151.863 million is correct and established that the Commission's assessment should be reduced on the order of \$100 million.

#### *The Commission Proceeding*

On December 11, 2002, the Company filed pursuant to § 58.1-2670 of the Code its application for review and correction. On March 24, 2003, the Commission issued an Order for Notice and Hearing in which we found that Gordonsville Energy had made timely application. We docketed the matter; provided for notice to Louisa County; established dates for the filing of testimony and exhibits; and scheduled the matter for hearing. Neither Louisa County nor any interested person sought to participate in the proceeding. At Gordonsville Energy's request, the case was continued until Howard P. Anderson, Jr., the Commission's hearing examiner assigned to this proceeding, entered his Hearing Examiner's Ruling of July 15, 2003. The hearing examiner provided for the filing of testimony and exhibits by the Company and the Commission Staff and for a public hearing on March 16, 2004.

At the hearing, proof of the notice to the affected locality required by § 58.1-2671 of the Code was admitted as Exhibit 1. In support of its application, Gordonsville Energy offered the testimony and exhibits of Ian Cuthbertson, manager of the facility, and Michael J. Remsha, an appraisal expert. The Staff offered the testimony and exhibits of Robert S. Tucker, Director of the Commission's Public Service Taxation Division ("Division"). Gordonsville Energy offered rebuttal testimony from Mr. Remsha and from Maria Rigatti, its Executive Director and a member of the Company's management committee.

On June 11, 2004, Hearing Examiner Anderson filed redacted and confidential versions of his Report, the transcript of the hearing, and the exhibits admitted at the hearing. The hearing examiner found that Gordonsville Energy had not met its burden of proving that the tax year 2002 assessment of value was excessive, and he recommended that the application be denied. (Report of Howard P. Anderson, Jr., Hearing Examiner, of June 11, 2004 (Redacted) at 9.) In a response filed in redacted and confidential versions, the Company excepted to the findings and recommendations made by the hearing examiner. The Staff filed a brief response, which addressed a technical issue of statutory language.

By Final Order of September 10, 2004, the Commission denied the application. Upon review of the record, we determined, as did the hearing examiner, that Gordonsville Energy has not established that the assessments of value were erroneous. On September 30, 2004, the Company moved for reconsideration and suspension of the Commission's Final Order. By Order of October 1, 2004, we denied the motions.

#### *The Property at Issue*

As of January 1, 2002, Gordonsville Energy operated two combined-cycle units. Each unit included a combustion turbine, a heat recovery steam generator, and a steam turbine. In

addition to these principal components, the property included pollution control equipment, electric transformer and substation equipment, controls and instruments, and related equipment. The nominal design capacity of the facility was 240 megawatts per hour, and the turbines could operate on natural gas or fuel oil. The facility was located on leased land. (Ex. 5 at Sections 7-2 through 7-5.) As of January 1, 2001, Gordonsville Energy reported the total cost of the facility to be \$200,526,807.54. (Ex. 3, GELP-2.) The Commission used an original cost of \$200,249,491, as of January 1, 2002, in making its assessments. (Ex. 9, Attachment 8.) Gordonsville Energy witness Remsha testified that the reproduction cost new of the facility, as of January 1, 2002, was \$206,303,000. (Ex. 5 at Section 14-7.)

#### *Gordonsville Energy's Operations*

On January 1, 2002, Gordonsville Energy operated as a qualifying cogeneration facility under federal law. See Gordonsville Energy, L.P. - Unit I, 60 F.E.R.C. ¶ 62,137 (1992); Gordonsville Energy, L.P. - Unit II, 60 F.E.R.C. ¶ 62,136 (1992). The electricity produced at the facility was sold to Virginia Electric and Power Company (Dominion Virginia Power) pursuant to power purchase and operating agreements for Unit 1 (Ex. 7C) and Unit 2 (Ex. 8C). According to Company witness Remsha, the contracts required Dominion Virginia Power to pay in excess of January 2002 market prices for electricity generated at the facility. (Tr. at 42-43; Ex. 5 at Section 13-4.) The Company also was a party to an agreement that required it to provide steam to an adjacent wastewater treatment plant. (Ex. 5 at Sections 3-1, 13-6; Ex. 4 at A33.) The provision of steam was required by federal law for operation as a qualifying cogeneration facility. (Ex. 4 at A33; Tr. at 120, 121.)

The power purchase and operating agreements permitted Dominion Virginia Power to dispatch the facility as its system required. (Tr. at 27-28.) Dominion Virginia Power determined

when Gordonsville Energy would supply electricity and the amount that would be transmitted through the utility's system. A measure of the use of an electric generating plant is its capacity factor or the ratio of the amount of electricity generated during a time period to the electricity that could have been generated during the same time period if the facility operated at its design capacity. Gordonsville Energy's facility manager, Mr. Cuthbertson, recalled that the facility operated roughly 1,000 to 1,100 hours in 2001. (*Id.* at 28.) For the year 2001, the capacity factor was 7.86 percent. (Ex. 5 at Section 3-1.) According to the facility manager, between 1996 and January 2002, Gordonsville Energy had an annual capacity factor of approximately 10 percent. (Tr. at 33-34.)

The facility was capable of significantly greater utilization. (Tr. at 54; Ex. 5 at Section 10-3.) The greatest number of hours of operation and the highest capacity factor were achieved in the winter months. During some months, the facility has operated at a monthly capacity factor in excess of 30 percent. (Tr. at 29-30.) Mr. Cuthbertson explained that it was necessary to use fuel oil during the winter months because natural gas shipments were curtailed. (*Id.* at 30-31, 32-33.)

#### *The Evidence on the Value of the Facility*

##### *Gordonsville Energy's Position*

Gordonsville Energy's witness Remsha offered an opinion on the fair market value of the facility developed through application of an income valuation approach and a cost valuation approach. The witness considered but did not apply a sales approach because he concluded that there was insufficient information on sales of comparable facilities. (Ex. 5 at Sections 2-1, 12-1; Tr. at 133-34.) As a preliminary step in his analysis, Mr. Remsha concluded that, as of January 1, 2002, the facility operated as a peaking unit with a low level of utilization. (Tr. at

52-53.) The witness determined that the facility was not economically viable as two combined-cycle units operating with an annual capacity factor of approximately ten percent. The highest and best use of the facility would be as an intermediate facility, which operated with an annual capacity factor of 30 percent. (Ex. 4 at A34; Ex. 5 at Sections 10-2 to 10-4; Tr. at 51-52.)

Mr. Remsha used a discounted cash flow model in his income approach to develop an indicated value of the facility. He assumed that the plant would operate at an annual capacity factor of 30 percent and produce 630,720,000 kilowatt hours per year. (Ex. 4 at A34; Ex. 5 at Section 13-5.) Based on projected prices for electricity in the competitive, wholesale market for 2002-2013, revenues for each year were estimated. Expenses of producing the electricity, including estimates of the cost of natural gas, various operating expenses, depreciation, and capital costs were also estimated for each year. Using these estimates of revenues and expenses, an estimated net income was calculated for each year. A discount rate was applied to arrive at an indicator of value for the generating and other equipment of \$40,259,809, including land. (Ex. 4 at A34; Ex. 5 at Sections 13-5, 13-6, 13-17.)

In his application of the cost approach, Gordonsville Energy's witness first calculated the replacement cost new of \$206,303,000 for the facility in operation on January 1, 2002. (Ex. 5 at Sections 14-6 to 14-8.) Mr. Remsha contended that a prudent investor would substitute a simple-cycle gas-fired unit for the existing combined cycle units capable of operating on gas or fuel oil. (Ex. 4 at A33, A35; Ex. 5 at Section 14-9; Tr. at 53-55, 128-29.) The cost of such a substitute unit was determined to be \$108,273,000. Subtracting the cost of the substituted simple-cycle facility from the replacement cost new of the existing facility results in an adjustment of \$98,030,000 for excess capital cost or functional obsolescence. (Ex. 5 at Sections 14-9, 14-12; Tr. at 55.) Mr. Remsha also made an adjustment for excess operating costs related to the

functional obsolescence. (Ex. 5. at Sections 14-14, 14-17; Tr. at 54.) An adjustment for physical deterioration was also calculated and applied. (Ex. 5 at Sections 14-12 to 14-14.)

In summary, Gordonsville Energy witness Remsha first calculated a replacement cost new for the facility in operation on January 1, 2002, of \$206,303,000. He made a series of adjustments to arrive at a cost approach indicator of value of \$75,218,400 for the facility plus \$256,500 for the value of land for a total value of \$75,474,900. (*Id.* at Section 14-16.)

The final step in deriving fair market value was a correlation of the value indicated by the income approach, \$40,259,809 (including land) and the value indicated by the cost approach, \$75,474,900 (including land). (Tr. at 125-26, 129.) Mr. Remsha arrived at a fair market value of \$60,000,000, including the value of land. (Ex. 5 at Sections 15-1 to 15-2; Tr. at 126, 130-31.)

#### *The Commission Staff's Position*

Public Service Taxation Division Director Tucker reviewed the methodology used to develop the recommended assessments of value, which the Commission adopted by its Orders of September 3, 2002, and March 3, 2004.<sup>2</sup> Mr. Tucker explained that the same methodology was used for all electric suppliers, including Gordonsville Energy, and for all electric utilities. (Ex. 9 at 2, 3; Tr. at 106.) In preparing recommended assessments of value for the Company, the Division developed percent condition factors for generating station equipment; office furniture and equipment; tools, shop, and garage equipment; and automobiles and trucks reported by Gordonsville Energy. The percent condition factors were calculated using useful life tables of 25 years and 10 years. (Ex. 9 at 4, 5, and Attachments 2 and 4.) On cross-examination, Mr. Tucker explained that an assumed life of 25 years was reasonable and was probably conservative. He noted that Gordonsville Energy witness Remsha used a life of 35 years for

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<sup>2</sup> See Footnote 1, *supra*.

some generating equipment in his study. (Tr. at 90-91.) The appropriate percentages from the life tables were applied to the plant additions made each year to develop a percent condition factor for each class of property. (Ex. 9, Attachments 3, 5, 6, 7.). These percent condition factors and the Louisa County ratio reported by the Department of Taxation were applied to the original cost of the classes of plant and equipment reported by the Company. (Id. at 4, 6, and Attachment 8.)

### *The Subject Property Sale*

In addition to explaining the methodology used to develop the assessments of value, Mr. Tucker discussed the sale of the Gordonsville Energy facility in 2003. On August 8, 2003, Dominion Virginia Power applied for Commission approval of its purchase of Gordonsville Energy's generating facilities. (Ex. 9, Attachment 9 at 1; Ex. 11 at A13.) According to Dominion Virginia Power's application, its power purchase and operating agreements with Gordonsville Energy would be terminated upon the closing of the transaction, if approved. (Ex. 9, Attachment 9 at 1; Ex. 11 at A15.) Dominion Virginia Power would record the value of generating facilities, fuel, and materials at their fair market value. The excess of purchase price over the fair market value of generating facilities, fuel, and materials would be recorded in its Purchased Power Account. (Ex. 9, Attachment 9 at 2.) The publicly announced sales price was \$150.8 million. (Ex. 9, Attachment 10 at 13.) This price was adjusted for fuel reserves, spare parts, prorated expenses, interest, and fees, but the total of these adjustments was not significant. As discussed by the hearing examiner (Report of Howard P. Anderson, Jr., Hearing Examiner of June 11, 2004 (Redacted) at 7), Dominion Virginia Power retained an appraisal expert to offer an opinion on the fair market value of Gordonsville Energy's operating equipment, fixtures and buildings, fuel, and materials as a condition of the purchase agreement.

The Commission authorized the transaction by Final Order of October 31, 2003, in Virginia Electric & Power Co., Case No. PUE-2003-00395. The transaction closed on November 21, 2003. (Ex. 11 at A12.)

Mr. Tucker also reviewed the Commission's assessment of the value of Gordonsville Energy's property as of January 1, 2003, for tax year 2003. Because of changes in the statutes governing the assessing of electric suppliers' property, the Commission assessed for tax year 2003 land and improvements as well as generating and other equipment. The Commission's assessment for tax year 2003 totaled \$160,760,414. Subtracting from the total assessment the value of land and improvements assessed at \$6,949,700 results in assessed value for generating and other equipment and materials of \$153,810,714, as of January 1, 2003. (Ex. 9 at 8-9 and Attachment 12; Ex. 10 at 1-2.) As Mr. Tucker noted, the Commission's tax year 2002 assessment, \$151.863 million, and the 2003 assessment of generating and other equipment, \$153.81 million, were clearly in line with the sales price.

Gordonsville Energy witness Remsha did not consider the sales of any comparable property when he made his studies. He concluded that there was insufficient information on sales of similar facilities. (Ex. 5 at Sections 2-1, 8-1, 12-1; Tr. at 134.) According to this witness, the 2003 sale of the subject facility was not a factor affecting his determination of fair market value. (Ex. 12 at A6.) The Gordonsville Energy-Dominion Virginia Power transaction provided for the termination of the power purchase and operating agreements. (Ex. 7C; Ex. 8C.) According to Mr. Remsha, these contracts were separate intangible assets, which should not be included in his appraisal. (Ex. 12 at A7; Tr. at 42-44.) Gordonsville Energy contended that the 2003 transaction was a sale of tangible property (i.e., the generating facility) and intangible property (i.e., the power purchase and operating agreements). (Ex. 12 at A7.)

### *Discussion*

Our consideration of this application must be guided by the Constitution of Virginia and enabling statutes, which govern the Commission. The Constitution of Virginia mandates two principles of property taxation. As required by Va. Const. art. X, § 2, property must be assessed at its fair market value. Of equal significance is the requirement of Va. Const. art. X, § 1, which provides that all property taxes "shall be uniform upon the same class of subjects within the territorial limits of the authority levying the tax." In affirming a Commission tax decision, the Supreme Court has approved our uniformity in assessment as promoting equity in the burden of taxation. Southern Ry. v. Commonwealth, 211 Va. 210, 214 (1970).

Uniformity remains an essential element of our assessment of the value of the property of electric suppliers and electric utilities (the corporations providing heat, light, and power by means of electricity). The Commission first assessed the value of the property of electric suppliers, which include qualified cogeneration facilities like the Company and independent power producers, in tax year 2002. Previously, the value of the property of Gordonsville Energy and the other electric suppliers was assessed by the localities. In 2002 and subsequent years, the Commission employed the same methodologies for assessing the value of electric suppliers' property subject to local taxation that has been used in assessing the value of electric utilities' property. We understand that this uniformity in assessment methodology was intended by the General Assembly.

It is another axiom of Virginia tax law that property be assessed at its highest and best use, and the Court has applied this principal in reviewing appeals of Commission assessments of the value of tangible property. Norfolk & W. Ry. v. Commonwealth, 211 Va. 692, 699 (1971). That principal may be extended to the assessment of the value of Gordonsville Energy's property

in this case. The Company and the Staff agreed that the highest and best use of the property was as a power plant.

The original-cost-less-depreciation method was used to make the Commission's assessments of the value of Gordonsville Energy's generating equipment, other equipment, and materials. Staff witness Tucker explained how this method was applied, and he provided exhibits showing the calculations of the assessments, which the Commission adopted. (Ex. 9.) The Virginia Supreme Court has affirmed the use of this methodology for assessing the value of property other than real property. Norfolk & W., 211 Va. at 700-01.

As discussed, the Company's witness correlated the results of an income approach and a cost approach to arrive at a fair market value of the property. Virginia law recognizes both approaches for valuing personal property. 211 Va. at 697, 700-01. The Commission is not persuaded, however, that Gordonsville Energy properly applied these methodologies to arrive at the value of the generating equipment, other equipment, and materials.

In his application of the income approach, the Company's witness made assumptions about revenues and expenses that varied greatly from historical and reasonably foreseeable operations. Gordonsville Energy witness Remsha determined that value of the facility was maximized when the capacity factor was about 30 percent. (Ex. 5 at Sections 10-2 to 10-4.) At that annual capacity factor, the Company's plant would generate 630,720,000 kilowatt hours and operate for approximately 2,600 hours during the year. (Ex. 6 at Section 13-4; Tr. at 28, 66.)

While the facility in place might have been capable of such operation, historically, it had been used in another manner. Gordonsville Energy witness Rigatti testified that the facility was built to perform under the power purchase contracts with Dominion Virginia Power. (Tr. at 115.) As provided by the power purchase agreements, Dominion Virginia Power could

dispatch the unit at its discretion. (Id. at 27-28.) Historically, the facility operated at an annual capacity factor of 7.86 to 14.0 percent (Ex. 5 at Section 3-1), and the factor was typically less than ten percent (Id. at Section 10-2). The 2001 capacity factor was 7.86 percent. (Id. at Section 3-1.)

In his income approach to valuation, Gordonsville Energy's witness ignored the actual operating environment. He assumed that the facility could dispatch at will and ignored any operating constraints that Dominion Virginia Power might impose. (Tr. at 67-68.) Although the witness's study showed price variation from \$40 to \$250 per megawatt hour over the year (Id. at 51, 65-67), he assumed that Gordonsville Energy would sell electricity at the highest prices.

The Supreme Court's recent analysis of an income approach to valuation has arisen in challenges to the valuation of real estate, but some principals identified by the Court apply in this case. The assessor must consider both economic rent and contract rent. Tyson's Int'l Ltd. Partnership v. Board of Supervisors, 241 Va. 5, 11 (1991). In the circumstances of this case, an income approach must have a reasonable basis in actual operations. The assumption that the facility would choose to operate only when prices were high is inconsistent with its past and expected operation.

Gordonsville Energy also offered an indication of value based on cost. Like the application of the income approach, the Company's cost study includes assumptions that are contradicted by other portions of the record. Central to its application of the cost approach is the assumption that a simple cycle facility could be substituted for the existing combined cycle facility. (Ex. 4 at A33; Tr. at 54.) From this assumption followed a number of reductions to the replacement cost new of the existing facility, which resulted in the indicated value of \$75,218,400, exclusive of land. (Ex. 5 at Sections 14-6 to 14-18.)

As of January 1, 2002, Gordonsville Energy operated as a qualifying cogeneration facility, which must provide steam to a waste treatment facility. This obligation was imposed by federal law. Gordonsville Energy witness Rigatti testified that the facility might not meet its federal obligations as a qualified cogeneration facility if a simple cycle generation unit were used. (Tr. at 117.) Any valuation would have to take that obligation into account. The record does not support the assumption that a simple cycle unit could be substituted for the existing combined cycle units.

Further, Mr. Remsha never explained why the substitution principal applied to his application of the cost approach but did not apply to his application of the income approach. In his cost approach, Mr. Remsha advocated significant adjustments based on replacement of the combined cycle unit by a simple cycle unit. In his income approach, the witness assumed that the existing combined cycle unit operated at a higher capacity factor and during the most opportune hours. It appears that Gordonsville Energy's witness could have projected revenues and expenses based on the operation of a simple cycle facility to use in the cost approach. (Tr. at 54, 68, 71; Ex. 4 at A34.) He did not develop a cost approach indication of value using a simple cycle unit. If the existing combined cycle facility could yield higher revenues under more favorable operating conditions as shown in Mr. Remsha's income approach, then the adjustments of \$120 million to replacement cost new (Ex. 5 at Section 14-18) recommended in his cost approach appear excessive. Gordonsville Energy's witness appears to be selective in application of the substitution principal.

The record before us does not establish that the key aspect of the cost approach, substitution of the simple cycle unit for the existing combined cycle unit, was reasonable. Gordonsville Energy's own witness testified that operation of a simple cycle unit would make

compliance with a legal requirement difficult. Further, given the results of Mr. Remsha's income approach, the adjustments to reproduction cost new for obsolescence and excess capital cost appear excessive.

As the final step in arriving at fair market value, Gordonsville Energy's witness "correlated" the values indicated by his application of the income and cost methods. From the indicated values, \$40,259,809 using the income approach and \$75,474,900 using the cost approach, Mr. Remsha arrived at a fair market value of \$60,000,000, including the value of land. (Ex. 5 at Sections 15-1 to 15-2.) Through some unexplained computations, Mr. Remsha used the results of his income approach to revise downward the results of his cost approach. (Tr. at 125-26, 129, 131-33.) Nowhere in his direct testimony, cross-examination, or prepared exhibit does the witness satisfactorily explain how he reached the figure of \$60 million. There is no discussion on any weight assigned to the income or cost approach. On cross-examination, Mr. Remsha acknowledged that he assumed the fair market value was \$60 million and then derived the allocation in his Exhibit 5, Section 15-2 and Exhibit F. (Id. at 131.) Further, the witness would not adhere to the figure of \$60 million as the fair market value. In response to questioning, Mr. Remsha stated that the value could be \$58 million or \$62 million. (Id. at 132.)

The Commission recognizes that appraisal is not an exact science, and an element of judgment is involved. Southern Ry., 211 Va. at 215. However, the Commission must require some support and explanation for the exercise of judgment. If, as Gordonsville Energy contends, the Commission should find that \$60 million is the fair market value, it must provide some satisfactory basis for that figure.

As discussed previously, the Staff also presented testimony on the Commission's assessment of the value of Gordonsville Energy's property for tax year 2003 and the sales price

of the subject property in the same year. In Norfolk & Western, 211 Va. at 697-98, the Supreme Court recognized that the property assessed by the Commission rarely sold, so sales information was not usually available. The Commission should not, however, ignore sales. In cases involving the same assessment methodology used to value the Gordonsville Energy property, the Court found that the Commission was in error when it did not consider market data. Lake Monticello Serv. Co. v. Board of Supervisors, 233 Va. 111, 115 (1987); Lake Monticello Serv. Co. v. Board of Supervisors, 237 Va. 434, 438 (1989).

The sales price identified in the Dominion Virginia Power application of August 2003 was not available to the Commission when we made our assessment for tax year 2002. While the date of the assessments at issue is January 1, 2002, the record before the Commission shows that Gordonsville Energy operated in the same manner until the sale closed in November 2003. (Ex. 9, Attachment 10 at 2-3; Tr. at 23-24, 29, 30.) In the second Lake Monticello case, the Court found that the Commission's assessments of value were far above the fair market value. 237 Va. at 441. In contrast, the sales price of \$150.8 million, before adjustments, included in the Dominion Virginia Power application, was extremely close to the January 2002 \$151.8 million assessment of the Gordonsville Energy generating equipment, other equipment, and materials. In keeping with the Court's directions in the Lake Monticello cases, we should certainly consider the evidence of the sales price as we discharge the Commission's obligation to review our assessment upon application.

Gordonsville Energy offered testimony in support of its position that the 2003 sale was actually two related transactions and that the sales price must be allocated to each transaction. First, Dominion Virginia Power purchased the generating equipment and other equipment. Second, Dominion Virginia Power reached agreement with Gordonsville Energy to terminate the

power purchase and operating agreements, Exhibits 7C and 8C. (Ex. 11 at A13, A14.)

Consequently, Gordonsville Energy contended that there was a sale of tangible property, the generating facility, and the sale of intangible property, the power purchase and operating agreements. (Ex. 12 at A7.)

We are not persuaded that Gordonsville Energy properly characterized the transaction as having two components.<sup>3</sup> It was not conclusively established that the power purchase agreements should be viewed as separable from the facilities in place. The original developer secured the contracts through participation in Dominion Virginia Power's competitive solicitation for offers of power. (Ex. 9, Attachment 10 at 2.) Company witness Rigatti acknowledged that the facility was constructed to meet Dominion Virginia Power's conditions as specified in the power purchase and operating agreements. (Tr. at 115, 117.) She also noted that Gordonsville Energy had to satisfy the requirements for designation as a federal qualifying cogeneration facility in order to perform under the contracts. (Id. at 117.) Finally, the contracts served as the basis for financing the project. Gordonsville Energy witness Rigotti testified that negotiating an agreement for terminating the contracts and converting the facility to a merchant plant operating in the competitive market was not an attractive option for the members of the partnership. (Id. at 118.) In summary, there is evidence that Gordonsville Energy's facility was built to perform under the power purchase and operating agreements and that its value arose from its operation under the agreements.

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<sup>3</sup> There was some testimony on an appraisal of the generating facility made by a consultant to Dominion Virginia Power. As Examiner Anderson found, the study was not offered into evidence. (Report at 7.) Consequently, we cannot weigh the results of the appraisal obtained by Dominion Virginia Power as we consider the indications of value from Mr. Remsha's income approach, cost approach, and correlation of values and the methodology described by Staff witness Tucker.

As we noted at the commencement of this discussion on the weight accorded to the subject property sale in 2003, our assessment of value for tax year 2002 was not and could not be based on the transaction. Rather, we view the evidence on the sale as support for the 2002 assessment now under review. Even if we ignore the sale of the subject property, Gordonsville Energy has not established that the assessment is erroneous. As we discussed in detail, the application of the cost and income approaches to value are flawed.

The income approach is based on assumptions on the amount and timing of dispatch of electricity that have no basis in Gordonsville Energy's history. The Company would have the Commission assume that the facility would sell into the market at the most opportune time for the foreseeable future. Actual operating history shows that these assumptions are unsupportable and that actual income would certainly be lower. Lower income streams would almost certainly lead to a capitalized value of less than the \$40.3 million calculated by Company witness Remsha.

Likewise, the core of the cost approach is the assumption that a simple-cycle unit would replace the combined cycle unit in operation. One of its witnesses testified that Gordonsville Energy would have difficulty performing under the contract if a simple-cycle unit were in place. The Commission is required to assess the value of the property in use.

Finally, Gordonsville Energy's witness Remsha never satisfactorily explained how he used the indicated value using the income approach to adjust downward the indicated values using the cost approach. Ultimately, Gordonsville Energy simply expects the Commission to accept its expert's contention that the income approach value, \$40.3 million, and the cost approach value, \$75.47 million, correlate to \$60 million or \$58 million or \$62 million. (Tr. at 132.)

The Commission finds that Gordonsville Energy did not carry its burden of establishing error in the assessment and establishing that the fair market value of its facility, as of January 1, 2002, was \$60 million. Accordingly, the application must be denied.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to: John K. DeShong, Regional Vice President - Tax, and Lynn C. Norton, Tax Manager, Edison Mission Energy, 18101 Von Karman Avenue, Suite 1700, Irvine, California 92612-1046; Robert F. Riley, Esquire, Williams Mullen, 1666 K Street, N.W., Suite 1200, Washington, D.C. 20006; Robert E. Eicher, Esquire, Williams Mullen, P.O. Box 1320, Richmond, Virginia 23218-1320; and the Commission's Office of General Counsel and Division of Public Service Taxation.