August 2020

# REWARD WITHOUT RISK:

*A Look at Imbalances in Virginia's Unique Regulatory Construct*

Prepared by E9 Insight on behalf of
Virginia Poverty Law Center

# EXECUTIVE SUMMARY

This report summarizes the findings of an examination by E9 Insight into specific aspects of the earnings framework for regulated utilities in Virginia. Specifically, the study focuses on two specific components – an expanded range of authorized returns and the further ability of utilities to retain earnings outside of this expanded range – established by the Virginia General Assembly in recent years.

The examination reviewed the earnings framework in 12 neighboring and comparable states, focusing on two key questions:

1. Is there an established earnings band?
2. Are there mechanisms in place for utility retention of over earnings?

In addition to these core questions, the review sought to identify other notable features of the regulatory structure that could support an informed review of Virginia's ratemaking framework and the impact of the legislatively prescribed features of utility regulation in the state.

Our major finding is that Virginia stands apart from other states, not because these components exist or that they are excessively generous, but because the legislature has prescribed them in isolation from the context of the rest of the ratemaking process, rendering them untethered from customary performance metrics and regulatory context.

Specific findings include:

1. No other state has an earnings band determined by the legislature. While not standard ratemaking, where these bands exist, they are typically the result of a commission proceeding or negotiated settlement agreement.
2. Where shared earnings mechanisms do exist, they are tied to specific performance metrics or comprehensive formula ratemaking frameworks. It should be noted that Virginia is anomalous in that the utilities keep 30% above the earnings band without any performance metrics.

In addition to these provisions, Virginia utilities enjoy protection from under-earnings through a legislatively prescribed directive to increase rates in the case of utility under-earnings. Additional research suggests that the COVID-19 pandemic has motivated many regulators to expedite customer refunds in cases of over-earning or over-collection by utilities.

The prescriptive nature of the two specific aspects examined in the investigation – the earnings band and over-earnings retention mechanism – set Virginia apart from the comparable states included in this review and suggest that lawmakers in the state may want to consider whether they are comfortable prescribing these specific outcomes.

# INTRODUCTION

This report summarizes the findings of an examination by E9 Insight into specific aspects of the earnings framework[1] for regulated utilities in Virginia. Throughout the United States, the "traditional" ratemaking process for utilities is complicated, multifaceted and layered with historical decisions that, in many cases, establish path dependencies or remain unquestioned. Given these complexities, this examination does not attempt to analyze all aspects of the earnings framework established in Virginia, but rather focuses on specific components – an expanded range of authorized returns and the further ability of utilities to retain earnings outside of this expanded range – established by the Virginia General Assembly in recent years. Information gathered from legislation, regulatory filings and interviews with commissioners, staff and industry stakeholders was used to assess what aspects of Virginia's ratemaking framework were consistent with or anomalous from states with comparable geographies, demographics and regulatory legacies.

Our major finding is that Virginia stands apart from other states. This is not because these components exist or that they are excessively generous, upon which we offer no opinion. These components are anomalous because the legislature has prescribed them in isolation from the rest of the ratemaking process, rendering them untethered from customary performance metrics and regulatory context.

# RESEARCH FOCUS

Utility regulation and ratemaking are complicated and ongoing endeavors. This report is not a comprehensive evaluation of the entire ratemaking structure established for regulated utilities in Virginia, which is a patchwork of authorized revenues collected from customers (consistent with traditional rate-of-return regulation), rate adjustment clauses and directives established by the legislature and commission decisions. The legislature has articulated, and the State Corporation Commission (SCC) governs, a process for determining the appropriate return-on-equity (ROE)[2] for regulated utilities in the state. Although some have asserted that the companies in Virginia enjoy comparatively generous authorized ROE, this examination does not purport to address those financial and economic questions.

Rather, this report focused on two aspects – both established by the Virginia General Assembly – that address the treatment of earnings *above* the authorized ROE ("excess returns" or "over-earnings"). Legislation in Virginia allows the two dominant regulated utilities – Dominion and Appalachian Power – to keep and not return to customers these "over-earnings" in two ways:

1) First, the companies are allowed to retain 100% of earnings up to 70 basis points (0.7%) over the authorized ROE; (In other words, if the authorized profit margin is 10%, the utilities keep everything up to 10.7%);

[1] The term "earnings framework" is used to refer collectively to the guiding principles, statues and policies that determine how earnings are authorized for regulated utility companies.

[2] The terms return-on-equity, ROE and authorized return are used interchangeably throughout this report in reference to the general principle of an authorized return for capital invested by the regulated utility.

2) Second, the companies are allowed to extract at their discretion 30% of earnings above the 70-basis point band.[3] In addition, this mechanism for retaining earnings allows the companies to withhold from customers if they choose not make certain specified investments in wind, solar and grid modernization technologies.

In addition to these provisions, Virginia utilities enjoy protection from under-earnings through a legislatively prescribed directive that, "the Commission shall order increases to the utility's rates necessary to provide the opportunity to fully recover the costs of providing the utility's services and to earn not less than such fair combined rate of return."[4] This provision establishes a notable asymmetry: while the companies are fully protected from the downside risk of underearnings, consumers are only partially protected from excessive utility earnings.

Through interviews and direct examination of regulatory filings and statutes, these earnings retention mechanisms were compared with similar provisions (if they existed) in 12 neighboring and relevant states. In addition, the research identified notable provisions from several other states that are highlighted for further reference.

## FINDINGS

The distinguishing characteristic of Virginia's ratemaking framework is the single-issue intervention by the legislature into a process that would customarily be deliberative, interactive and comprehensive in order to consider the interplay of various components and their implications for financial risk and reward. Accordingly, several of the key findings are from this analysis are:

1) *No other legislature has established an earnings band in isolation:* While the establishment of an earnings band surrounding the authorized ROE is not consistent with traditional ratemaking, it is also not entirely uncommon, especially in the states surveyed in the southeastern United States. However, it is anomalous for the earnings band to be prescribed in legislation and in isolation. In all other cases, the earnings band is established as the result of a commission proceeding, negotiated settlement or some other deliberative process.

2) *No other state legislature establishes an isolated mechanism to retain over-earnings:* Similarly, this review found no other mechanisms for utilities to retain over-earnings that were prescribed in isolation by legislation. While there are some situations in which earnings sharing mechanisms are established, in those instances they are provisions of more comprehensive formula ratemaking frameworks, where the actions of both regulators and utilities are constrained. Where shared earnings mechanisms do exist, they are typically tied to specific performance metrics or comprehensive formula ratemaking frameworks.

3) *Few state legislatures constrain rate adjustments by the regulatory commission:* The current ratemaking framework in Virginia restricts the regulatory commission's to adjust rates downward except under very specific conditions. In situations where such restrictions exist in other states, they are typically associated with multi-year rate plans, formula rates or some other more comprehensive ratemaking framework.

[3] In 2018, for instance, according to Dominion's own earnings reports filed with the Virginia State Corporation Commission, the combination of the 70 basis point earnings band plus 30% of everything above it caused Dominion Energy to achieve a functional rate of return equal to 13.47%, even though its authorized rate of return is only 9.2%.

[4] Virginia Code § 56-585.1(A)(8)(a). Generation, distribution, and transmission rates after capped rates terminate or expire. https://e9radar.link/189b5

4) *The COVID-19 pandemic has motivated regulators to expedite customer refunds:* Several states are taking specific actions to shield customers from the economic impacts of the COVID-19 pandemic and to return funds held by utilities that have been over-collected.

In general, the prescriptive nature of the two aspects of earnings examined in the research – the earnings band and the retained over-earnings – highlight how the role of the legislature in Virginia is not consistent with best regulatory practices found in other states.

Historically, state legislatures have delegated significant regulatory authority to public utility commissions in the area of ratemaking. Legislatures have done this for two main reasons. First, legislatures have recognized that utility regulation is one of the more complex and technical areas of practice. Ratemaking requires attention to the specific facts of each utility and consideration of how different provisions reduce or increase financial risk for utility companies. Second, legislators have recognized that the timescale of infrastructure investment demands a more consistent regulatory framework than the political process provides. This is one reason why most state legislatures confirm fixed-term commissioners to wield regulatory authority.

## TRADITIONAL RATEMAKING & THE VIRGINIA CONTEXT

One of the features of electricity industry regulation is that each state is unique with a regulatory history and tradition that, in most cases, dates back 100 years to the early 20th century. This history means that the specific elements of each state's regulatory structure will have slight variations that can make direct comparisons challenging. Yet while there is diversity and nuance, it's also true that there are common guiding principles and economic concepts that provide a common foundation. Together, these comprise "traditional ratemaking". In order to understand and contextualize the findings of this analysis, it is helpful to briefly review some principles that underlie the traditional ratemaking process and some of the specific components of the regulatory framework in Virginia.

### *Traditional Ratemaking*

The regulatory landscape across the United States, and in any specific state, has such variety and complexities that there is likely no situation that conforms to the implications of the term "traditional ratemaking". That said, the concepts and practices embedded in the traditional ratemaking model remain the foundation of the regulatory process from which policymakers, regulators and utilities have built upon. Typically, this process involves two steps. First, the utility would propose, and regulators would confirm, a required revenue that amounts to the total costs for operating the electricity system along with an appropriate rate of return to attract private capital. Second, regulators would define the rates, terms and conditions of service that will apply to each class of similarly situated customers. Those rates are designed so that the utility can achieve its required revenue, assuming proper management.

The rate structure thus defined, the utility substantially bears the risk that sales will be lower or costs are higher than anticipated (under-earning). Similarly, added benefits will accrue to the utility, should sales be higher or expenses lower than anticipated (over-earning). Under this traditional model, an authorized rate of return is established in the general rate case and any earnings in excess of that are kept by the utility and under-earnings are absorbed by the utility. As a result, this traditional

ratemaking model creates natural incentives for the utility to increase earnings by either reducing expenses or increasing sales between rates reviews.

Since at least the 1970's, this traditional model has been subject to a variety of regulatory tools that are intended to create specific incentives for utilities or provide true-up mechanisms for specific utility expenses, with the intention of reducing utility risk. For example, perhaps the most common adjustment mechanisms include separate true-up mechanisms for fuel costs that remove those costs from the general rate case process and pass them (and their associated financial risk) directly to consumers. Similarly, many jurisdictions have implemented a variety of revenue decoupling provisions, mostly associated with energy efficiency programs, that are intended to address the utilities' natural incentive to increase sales.

Today, "traditional" ratemaking is more a theoretical concept than a practical reality. In practice, the ratemaking process is very specific and highly complex. Provisions can vary by type of utility service (electric, gas, water, etc.) and often from company to company within a given states. Finally, the various flavors of ratemaking are often geared to the broader regulatory environment of a state, particularly the regulated industry structure, for example whether the utility owns generation and transmission assets or whether it acts as only as a distribution utility.

In this context, a core function of the regulator's job is to appropriately balance risk and reward. By establishing an authorized rate of return, regulators consider the risk of a utility's general business. This standard has been affirmed in court precedent and generally requires that regulators compare a utility's business with other, similar businesses that face similar risks.[5] Some risks result from the size or type of regulated utility. A utility with more ratepayers generally has a lower risk than one with fewer ratepayers. The regulatory environment can itself remove or add significant risks that should affect the authorized rate of return. For example, if one utility has a separate cost recovery tracking mechanism for pension plans while another does not, the difference might disqualify a comparison of authorized rates of return. Authorized returns compensate for risk and are therefore based on a comprehensive assessment of the regulatory and business environment of a utility, especially the presence or absence of other regulatory mechanisms, such as a capital tracker, a pension tracker, revenue decoupling, or fuel expense tracker.

### *Formula Rates, Multiyear Rate Plans and Performance-Based Rates*

There is a spectrum of alternatives to the traditional ratemaking process that are intended to incentivize favorable actions by the utility or reward specific outcomes. In addition to cost adjustment mechanisms, formula rates and multiyear rate plans provide utilities with certainty in recovering costs. Under a formula rate plan, typically enacted through legislation, rates are adjusted periodically to align actual earnings with authorized earnings based on specific factors. Under a multiyear rate plan, a utility agrees not to seek rate adjustments except within the parameters of the rate plan. Under a performance-based rate structure, utilities are able to achieve increased earnings or specific performance incentive incentives based on achieving specific outcomes and performance metrics.

[5] This general standard derives from Bluefield Waterworks Improvement Company v. Public Service Commission of West Virginia 262 US 679 (1923) in which the U.S. Supreme Court established that, "a public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties."

The earnings band is often a feature of these alternative frameworks or modifications to traditional ratemaking. The earnings band establishes a range surrounding the authorized rate of return in which there will be no adjustments to rates. That is, within this band, the utility shareholders bear the risk that their earnings may fall below the authorized ROE and, simultaneously, they will enjoy the benefits of any overearnings. Many states in the region have implemented similar mechanisms and have, through long-standing customary practice, incorporated earnings bands into their overall regulatory frameworks.

In theory, an earnings band accomplishes two major goals. First, it provides an incentive for utilities to reduce expenses (and therefore increase earnings) in between rate cases. Second, it allows for administrative flexibility and helps address the inherent volatility of underlying earnings drivers and the inability to make perfect predictions.

At the same time, earnings bands have notable downsides including: (1) they do not provide any incentive that prioritizes "good" from "bad" expense reductions (and, in fact, may encourage creative accounting strategies that do not reduce the total expense burden borne by customers); (2) in states without revenue decoupling, they exacerbate incentives to increase sales; and (3) they can effectively award higher earnings without an explicit justification or acknowledgement. Similar to the earnings band, an earnings sharing mechanism provides an allocation of excess earnings above the authorized rate of return between shareholders and consumers.

In practice, earnings bands and earnings sharing mechanisms are typically associated with comprehensive multi-year or formula rate plans, where there is a more comprehensive, negotiated framework that includes assurances for both utility and customer interests and where the earnings band provides some certainty protecting longer term ratemaking frameworks.

***Regulated Earnings in Virginia***

The most significant recent legislation in Virginia is the Grid Transformation and Security Act (GTSA), enacted in 2018. Among other elements, the GTSA lifted a rate freeze that had been previously established in 2015 prior to the anticipated implementation of the Clean Power Plan (developed by the Environmental Protection Agency under the Obama Administration). While the GTSA nominally allowed the SCC to conduct a rate case, it also provided that certain overearnings could be invested in grid hardening, solar energy and wind energy before being returned to ratepayers. The GTSA also established that a rate case review would be initiated before the SCC in 2020 for Appalachian Power and in 2021 for Dominion Energy.

Current Virginia law requires that the authorized ROE be established through a process before the SCC. (Currently, Dominion's authorized ROE is 9.2%.) While the statute does not establish the ROE itself, it does prescribe a 70-basis point "earnings band" (or "collar") around the authorized rate established by the SCC. Any earnings within that band are retained by the utility. If earnings fall below the 70 basis point band, the utility is entitled to recover those under earnings through a rate case before the SCC. If earnings are above the 70 basis point band, the utility shareholders retain 30% of those incremental earnings and 70% are refunded to ratepayers.

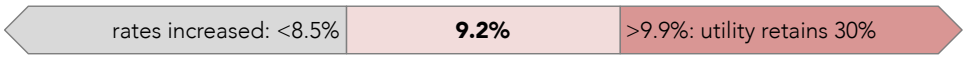
However, according to provisions established by the GTSA, the amount of potential customer refunds will be reduced by the total amount of certain authorized investments in grid hardening, solar energy and wind energy (known as "Customer Credit Refund Offset Mechanisms"). As a result, there is no guarantee that customers will receive these over earnings at all. In addition, a variety of rate adjustments are reconciled on an annual basis. Under the current rules, the SCC conducts a triennial

review of rates, but the GTSA further restrains the SCC from reducing rates except in the extraordinary case that two consecutive rate reviews determine that the utility has generated excess revenue (i.e., over-earning).

Many stakeholders have concerns that, in particular, Dominion has been in a persistent state of over-earning for some years. Dominion's base rates (which are supposed to enable it to recover its costs of service plus a fair profit) have not been set based on Dominion's actual cost of service since 1992, although the treatment of many costs has changed, in large part because of rate adjustment clauses. For example, many costs, such as environmental compliance investments, have been moved out of base rates and recovered through rate adjustment clauses and other single-issue ratemaking mechanisms. Likewise, rates are still based in part on long-term power purchase contracts that expired years ago.

Many stakeholders have raised concerns that the patchwork of cost recovery mechanisms may be distorting the earnings picture for utilities in Virginia and preventing the SCC from exercising its authority to review and adjust rates.

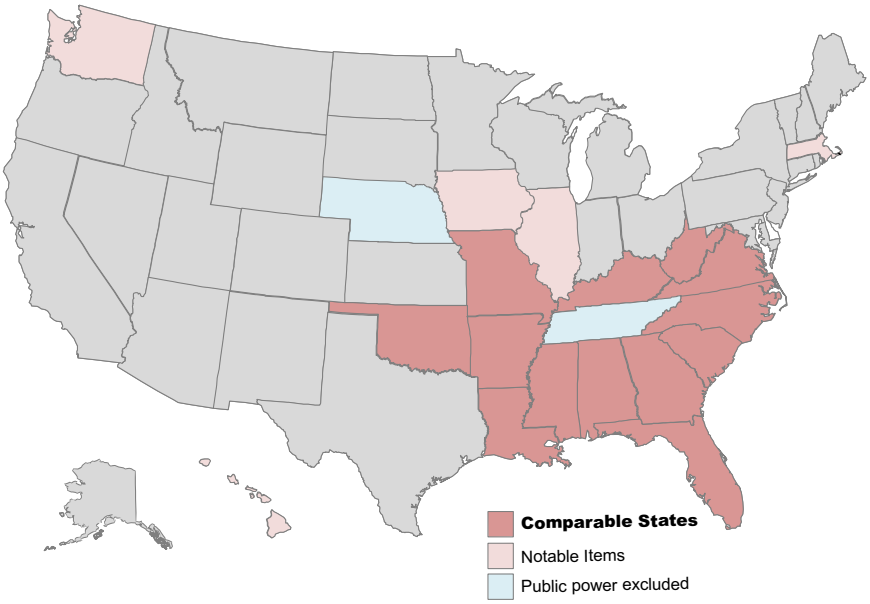
**Authorized ROE Earnings Band**
(with additional earnings retention mechanism)




Virginia legislation establishes a 70-basis point (0.7%) earnings band that surrounds the authorized ROE of 9.2%. If the utility earnings fall below 8.5%, the commission is compelled to raise rates to cover 100% of utility under-earnings. If the utility collects more than 9.9%, only part of the over-earnings are returned to customers (and only after certain qualified investments in grid hardening and clean energy projects have been considered).

## STATE REVIEW METHODOLOGY & FINDINGS

In order to examine two specific aspects of Virginia's ratemaking framework, a cohort of 12 states was reviewed based on the geographic proximity, regulatory structure and size of regulated utilities in the state. These states include the peer utilities defined by Virginia statute.[6] Analysis was based on (1) discussions with commissioners, commission staff and industry experts and (2) direct examination of regulatory filings, legislation and policy directives.




The review focused on two key questions:

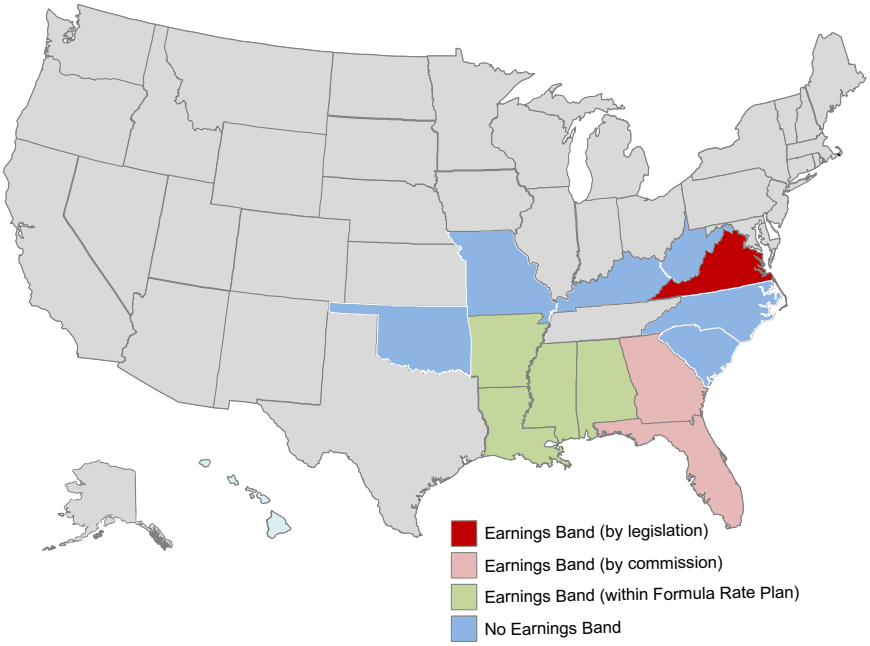
3. Is there an established earnings band?
4. Are there mechanisms in place for utility retention of over earnings?

In addition to these core questions, the review sought to identify other notable features of the regulatory structure that could support an informed review of Virginia's ratemaking framework and the impact of the legislatively prescribed features of utility regulation in the state.

[6] Virginia Code § 56-585.1(A)(2)(a-b)

### *Summary of State Findings*

The following table summarizes the findings and specifies how the specific earnings band or earnings retention mechanism are established.




| State | Established by: | Earnings Band | Excess Earnings Retention Mechanism |
|---|---|---|---|
| AL | Formula Rate Plan | 23 basis point earnings band on Weighted Common Equity Return (unique formula), plus a performance-based adder of 7 basis points | Utility earns 75% of earnings 0-50 points above collar; 60% for 50-100 points above; 25% for 100-150 points above; 0% above 150 points |
| AR | Formula Rate Plan | 50 basis points incorporated into FRP | FRP adjusts rates; no sharing |
| FL | Commission | 100 basis points | None; option to launch investigation |
| GA | Commission | 100 basis points, increasing to 125bp after 2020. | 2018-2019, 50/50 customer refund and asset payments; 2020 onward, 20% to utility, 40% to customers, 40% to assets |
| KY | Commission | None | None (optional ESM was terminated) |
| LA | Formula Rate Plan | Established in each utility's FRP - Entergy has 60 basis points, Cleco has 90, SWEPCO has 50 | Differs by utility - Entergy has no sharing mechanism; Cleco refunds retains 40% within 85 points above collar, 0% for >85 points above; SWEPCO refunds 100% to customer |
| MO | Commission | None | None |
| MS | Formula Rate Plan | Earnings band varies by utility in FRP. Entergy 50bp. | FRP adjusts rates; shared savings mechanism determined by performance-rate formula |
| NC | Commission | None | Earnings kept by utility |
| OK | Commission | None | None |
| SC | Commission | None | Refunds prescribed by legislative statute |
| WV | Commission | None | Earnings kept by utility |

# STATE SUMMARY INFORMATION

The following provides summaries of the findings for the states reviewed. For each state, these summaries include:

- Details of established earnings band and earnings sharing mechanisms
- Overview of ratemaking process and authorized returns
- Other notable and relevant details

## ALABAMA

| | |
|---|---|
| *Earnings Band:* | 23 basis points earnings band established by commission investigation. 7 basis points performance-based adder available |
| *Shared Earnings:* | Utility earns 75% of earnings 0-50 points above the collar; 60% for 50-100 points above; 25% for 100-150 points above; 0% above 150 points |

The Alabama PSC established a Rate Stabilization and Equalization (RSE) framework in November 1982[7] as a mechanism to adjust utility rates. In February 2013, the PSC held public hearings and opened an investigation in to examine consistent over-earnings by Alabama Power Company (APC). The concluding order in August 2013[8] created a new PSC staff review process and modified its RSE to reflect a formula rate plan structure. Annual rate increases were capped at 5%, and the PSC replaced the existing ROE range with a Weighted Common Equity Return (WCER) range, set at 5.75-6.21% with a target of 5.98%. The adjustment was designed to recognize the capital structure of Alabama Power and the relationship between equity ratio and ROE. APC was also permitted to receive a performance-based adder of 7 basis points (0.07%) to the adjusting point if they possess an "A" credit rating OR if the company is in the top third of the customer value benchmark survey conducted by the PSC.[9]

ALABAMA POWER. APC modifies its Rate RSE through a consolidated, ongoing docket originally opened in 2005.[10]. In April 2018,[11] APC submitted a petition to modify the overearnings division in order to maintain good credit quality. In May 2018, the commission approved the modifications,[12] including a provision for Alabama Power to retain a portion of the revenue that causes the WCER to exceed the allowed range. These modifications allowed Alabama Power to adjust its earnings to better fit inside of the approved range. Additionally, the WCER range was reduced from 6.21% to 6.15%, and a moratorium on rate increases was implemented for 2019-2020.

According to the 2018 modifications, if Alabama Power's actual WCER is between 6.15% and 7.65%, the utility receives 75% of the amount between 6.15% and 6.65%; 60% of the amount between 6.65% and 7.15%; and 25% of the amount between 7.15% and 7.65%. Customers receive all earnings in excess of an earned WCER of 7.65%. These dividends depend on whether there was a rate increase.[13]

[7] 2001. Alabama Public Service Commission 2001 Annual Report. https://e9radar.link/9daf7
[8] August 2013. Alabama Public Service Commission's Order on Rate RSE. Docket nos. 18117 and 18416. https://e9radar.link/713f6
[9] Alabama Public Service Commision. 2019 Annual Report. https://e9radar.link/ztjt
[10] Docket nos. 18117 and 18416. Rate RSE and CNP for Alabama Power Company. https://e9radar.link/d2d59
[11] April 2018. Alabama Power Co. Revisions to Rate RSE. Docket nos. 18117 and 18416. https://e9radar.link/582f
[12] May 2018. Alabama Public Service Commission Order for Revisions to Rate RSE and Refund Mechanism. https://e9radar.link/jeue
[13] February 2020. Southern Company Annual Report, p. II-65. https://e9radar.link/ccd74

Alabama's unique WCER formula has attracted scrutiny from advocates; according to an analysis of APC's equivalent ROE using Standard & Poor and Electric Edison data, the company has over-earned over $1 billion since 2014.[14] APC's earned ROE ranged from 12.6-13.0% since 2014, up from average ROEs of around 9.7% across the nation.

## ARKANSAS

| | |
|---|---|
| *Earnings Band:* | 50 basis points incorporated into FRP |
| *Shared Earnings:* | FRP adjusts rates; no sharing |

In March 2015, the Arkansas General Assembly passed HB 1655, Act 725[15] to reform utility ratemaking and declare an emergency in the state due to shifting utility rate costs; the need for stable rates; and problems with affordability. The new law permitted public utilities to electively regulate rates under a formula rate review plan (FRP) with an earnings band of 50 basis points. According to statute, when rates exceed the target return rate plus 0.5%, the earned rate for the period will be decreased so that it equals the target return rate. Utilities have flexibility to use a historical year or projected year for the rate review test period. Rate cases may not be filed more frequently than once per year, and increases or decreases may not exceed 4% of each rate class revenue for the 12 calendar months preceding the formula rate review test period. While the earnings band and rate adjustment amounts are fixed, the Arkansas PSC has the authority to set the target return rate that the earnings band is set around.

ENTERGY ARKANSAS. In February 2016, Entergy Arkansas received commission approval for its first FRP,[16] filed in its 2015 rate case proceeding.[17] The docket has subsequently included annual formula rate plan (FRP) adjustments, including the July 2019 report.[18] The 2019 filing requested an increase of base rates by $15.3 million, for effect in January 2020 but did not modify the target return rate, which was described as, "the cost rate for common equity, 9.75%, as established by the Commission in Docket No. 15-015-U [five years prior]." The settlement agreement accepted in December 2019[19] reflected several other adjustments, including a modified adjustment amount for $10.1 million, a one-time credit to the FRP rate in 2020 of $4.9 million to reflect mis-forecasted 2018 revenues.

SWEPCO. In December 2019, the Arkansas PSC issued an order[20] accepting the stipulation agreement in Southwestern Electric Power Company (SWEPCO)'s rate case. The agreement reduced the authorized ROE to 9.45%, down from SWEPCO's initial request for 10.5%, and approved an increase of $53 million, $21.5 million less than the initial request.

[14] July 2020. Energy and Policy Institute. Article: Alabama Power earned $1+ billion in profits over industry average on the backs of customers since 2014. https://e9radar.link/f5ede

[15] House Bill 1655. To Reform Rate Making Of Public Utilities; And To Declare An Emergency. https://e9radar.link/beda0

[16] February 2016, Order No. 18, approving rate adjustments. Docket no. 15-015-U. https://e9radar.link/dpu7

[17] Docket no. 15-015-U. In The Matter Of The Application Of Entergy Arkansas, Inc. For Approval Of Changes In Rates For Retail Electric Service. https://e9radar.link/oxqj

[18] July 2019. Entergy Arkansas, LLC submits their Application for the 2019 Evaluation Report. Docket no. 16-036-FR. https://e9radar.link/87468

[19] December 2019. Order No. 24. The Commission finds that the settlement is just and reasonable. Docket no. 16-036-FR. https://e9radar.link/rfos

[20] December 2019. Order No. 12, Accepting the Settlement Agreement. Docket No. 2019-008-U. https://e9radar.link/hhvj

## FLORIDA

| | |
|---|---|
| *Earnings Band:* | 100 basis points |
| *Shared Earnings:* | None; option to launch investigation |

In 1973, Florida Power Corporation, Florida Power & Light, and Gulf Power Co. were ordered to implement earnings bands of approximately 37.5 basis points (I.e. a range of 13.50-14.75%, a total range of 75 points); other utilities were granted ROE ranges in shortly thereafter[21]. In the mid-1990s, most utilities were granted earnings band of around 100 basis points.

Utilities file monthly reports through the "earnings surveillance report" program, established in 1996 via statute.[22] Utilities "not under an incentive regulation plan or not subject to an earnings cap" are also required[23] to file forecasted earnings surveillance reports before March 1 of each year. Within a month of report filings, any stakeholder (I.e. the PSC, Office of Public Counsel or other party) may petition the PSC for an investigation of the rates and potential sharing mechanisms.

FLORIDA POWER & LIGHT: In November 2016, the PSC approved a stipulation[24] for an $811 million increase in Florida Power & Light (FPL)'s rate case. The four-year rate term reduced the initial request of FPL by more than 50%, driven partly by a reduction in the company's proposed ROE from 11.5% to 10.55%, with a 100bp range. The stipulation also held that FPL may not petition for another base rate increase through the term of the settlement (January 2017-December 2020), and that earnings in excess of 11% or under 9% may warrant a rate investigation.

FPL was granted a unique accounting provision that affects its earnings band in the August 2010 rate case stipulation agreement.[25] In the stipulation, parties granted FPL flexibility "to vary the annual amortization of theoretical depreciation reserve surplus" in order to keep FPL's ROE within the 9-11% range. FPL was permitted[26] to amortize up to $776 million of the total $894 million reserve surplus during the settlement term. This provision allowed FPL to modify its accounting procedures in order to stay within the earnings band. FPL continued this mechanism in its 2016 rate case stipulation.[27] Building off of other depreciation proceedings, FPL was permitted to apply amortized assets ($370 million of the allowed $400 million) to its rates. The 2016 stipulation continued the provision and permitted FPL to amortize up to $1 billion of depreciation reserve surpluses to the depreciation rates for the new rate period in order to maintain a ROE range of 9.6%-11.6%.

DUKE ENERGY FLORIDA: In November 2017, the Florida PSC approved[28] a petition by Duke Energy Florida (DEF) for limited proceeding to approve its 2017 second revised and restated settlement. The

[21] December 2008. Report to the Legislature on Utility Revenue Decoupling. See Appendix C, "Earning Review History." https://e9radar.link/js4g
[22] Rule 25-6.1352, Earning Surveillance Report. https://e9radar.link/3a973
[23] Rule 25-6.1353, Forecasted Earnings Surveillance Report. https://e9radar.link/d1cf7
[24] October 2016. Joint Motion for Approval of Settlement Agreement (approved at the November 29, 2016 commission meeting). Docket no. 160021-EI. https://e9radar.link/a4117
[25] August 2010. Agreed motion for approval of settlement agreement. Docket no. 080677-EI. https://e9radar.link/qbv2
[26] February 2011. Order Approving Proposed Stipulation and Settlement, Denying Motion for Reconsideration, and Denying Petition for a Base Rate Proceeding. Docket no. 080677-EI. https://e9radar.link/owq5
[27] Id., Paragraph 11 and 12. https://e9radar.link/a4117
[28] November 2017. Order Approving 2017 Second Revised and Restated Settlement Agreement, Document No. 09951-2017. Docket no. 20180183-EI. https://e9radar.link/ya4ib

settlement dictated various rate adjustments for 2019-2021, including an authorized ROE of 10.5% with a "range of reasonableness" of +/- 100 basis points. The stipulation dictated that earnings below 9.5% may trigger DEF to file of a rate case; earnings above 11.5% will be reported on a monthly earnings surveillance report for consideration by the commission and other parties. DEF was permitted to increase rates by $67 million each year.

GULF POWER: In May 2017, the Florida PSC approved[29] Gulf Power's most recent rate case stipulation. The proceeding referenced its 2012 settlement agreement and order[30] which included a target ROE of 10.25% with a 100 basis points range; the 2016 case continued this target and range, despite the request for a ROE of 11%. Gulf Power received approval for a rate increase of $62 million.

TAMPA ELECTRIC COMPANY: In November 2017, the Florida PSC approved[31] TECO's 2017 rate case settlement agreement retained the company's existing ROE target of 10.25% with a 100 basis point range. The settlement outlined a "ROE Trigger Mechanism" which acts as a performance-based adder: if TECO's treasury bond yield rate for six consecutive months is at least 4.60%, the ROE shall be increased by 25 basis points (a target of 10.50% for a range of 9.50-11.50%).

## GEORGIA

| | |
|---|---|
| *Earnings Band:* | 100 basis points, increasing to 125bp after 2020 |
| *Shared Earnings:* | 2018-2019, 50/50 customer refund and asset payments; 2020 onward, 20% to utility, 40% to customers, 40% to assets |

In Georgia, ROE earnings bands and targets are determined through rate cases. Georgia Power, the state's primary investor-owned utility, began to use multi-year ratemaking in 1991. In 1998, the PSC established an "earnings dead band" in addition to an earnings sharing mechanism which refunded two-thirds of excess earnings to customers and maintains one third for the company (this was modified in 2019).[32] The company's earnings bands varied between 100-150 basis points since inception. Georgia Power files Annual Surveillance Reports in March of each year to adjust its ROE and other tariffs, and under-earnings may be addressed through an optional Interim Cost Recovery Tariff.

In December 2019, the Georgia PSC approved[33] Georgia Power's 2019 settlement agreement.[34] The PSC approved an earnings band of 9.5-12% (125 basis points, target of 10.75%) and, as part of the stipulation, directed Georgia Power to apply its excess earnings from 2018 and 2019 to regulatory assets, in addition to a separate 2020-2022 ratio:

- For 2018 reported earnings, 50% of the customer share (approx. $51 million) was dedicated to reducing the 2019 storm damage regulatory asset account. The remaining 50% was refunded to customers in 2020 with a special line-item on the bill.

[29] May 2017. Order PSC-17-0178-S-EI approving stipulation and settlement agreement. P. 3. https://e9radar.link/d60ef
[30] April 2012. Order no. PSC-12-0179-F0F-EI, Final Order Granting in Part and Denying in Part Petition for Rate Increase and Approving Stipulations. Page 50-52 for ROE debate and analysis. https://e9radar.link/8dd0e
[31] November 2017. Order PSC-2017-0456-S-EI granting TECO's petition. Docket no. 20170210-EI. https://e9radar.link/x4ly
[32] June 2020. Presentation at the NARUC PBRSWG. Georgia PSC's Experience with Multi-Year Rate Plans. https://e9radar.link/ksrh
[33] December 2019. Short Order Adopting Settlement Agreement as Modified. Docket 42516. https://e9radar.link/9ic5
[34] December 2019. Settlement Agreement. See paragraphs 6, 7, 11, and 12. https://e9radar.link/962d2

- For 2019, Georgia Power agreed to dedicate 50% to customers, and 50% was dedicated to the early retirement of the Stewart County coal investigation regulatory asset.
- For January 2020- December 2022, Georgia Power was permitted an earnings band of 9.50% to 12.00% (125 basis points). Retail earnings above 12% ROE will be dispersed by: 40% to a set of regulatory assets; 40% directly refunded to customers, allocated on a percentage basis to all customer groups; and 20% retained by the Company.

The Company agreed to not file a general rate case unless its calendar year retail earnings are projected to be less than 9.5% ROE. In conjunction with a rate case order, the PSC files an accounting order which authorizes Georgia Power's ROE and other mechanisms. In practice, the PSC often accepts the rate filings as submitted, and has few ex parte restrictions for its proceedings.

## KENTUCKY

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|---|---|
| *Earnings Band:* | None |
| *Shared Earnings:* | None (optional ESM in 2001 was terminated) |

In Kentucky, a reasonable ROE is proposed by the utility, and the PSC analyzes the rate and makes adjustments. Utilities are not bound to any shared earnings procedure, though in January 2000 the commission offered[35] Louisville Gas & Electric (LG&E) an optional Earnings Sharing Mechanism (ESM) plan as an alternative to the performance-based ratemaking requested. The plan set an 11.5% ROE with a deadband of 100 basis points, with 40% of over-earnings dedicated to customers and 60% to the utility. The ESM plan and associated tariff was terminated in June 2004[36] after the commission conducted an audit and determined that "the ESM has not incented LG&E to operate any differently than it would have without an ESM." Since 2004, ESM factors from 2000-2003 have been cited in occasional LG&E cases, but no other Kentucky utilities requested the mechanism.

KENTUCKY UTILITIES/LOUISVILLE GAS & ELECTRIC. KU and LG&E last modified their rates through a Green Tariff adjustment. In April 2019, the commission approved[37] the stipulated rate case outcome, including a ROE of 9.7% applied to capitalization. The ROE reduction resulted in a revenue requirement reduction of $20.1 million. KU's total revenue increased by $58.3 million, a reduction of $54.1 million from KU's initial request; LG&E was given approval for a $2.1 million increase, $32.8 million less than requested. The stipulation also adjusted revenue allocation agreements, net metering agreements, and other items.

DUKE ENERGY KENTUCKY. In April 2020, the Kentucky PSC issued[38] a final order in Duke Energy Kentucky's rate case. The order approved Kentucky's rate increase request for $24.1 million (6.6%), instead of the $44.2 million requested, with a ROE of 9.25%.

KENTUCKY POWER Co. In June 2020, Kentucky Power filed an application[39] for an increase of $70 million due to distribution modernization investments. In testimony,[40] Kentucky Power describes

[35] January 2000. Order on Alternative Ratemaking. Docket no. 98-426. https://e9radar.link/ji90
[36] June 2004. Order accepting the ESM Settlement and other issues. Case no. 2003-00433. https://e9radar.link/rhou
[37] April 2019. PSC Order. https://e9radar.link/np6t
[38] April 2020. Order. Docket no. 2019-00271. https://e9radar.link/f40a6
[39] June 2020. Application of Kentucky Power Company, Section I. Docket No. 2020-00174. https://e9radar.link/v1wa
[40] June 2020. Application, Section III, Testimony Volume 2. See pdf page 212; Direct Testimony of Adrien M. McKenzie. Docket no. 2020-00174. https://e9radar.link/11z1

estimates for similar firms for a ROE range of 9.5-10.8%, though the analysis recommends a ROE of 10.3%. The company requested 10.0% as a "reasonable compromise" between ratepayer concerns and company returns.

Kentucky statute[41] directs utilities to "demand, collect and receive fair, just and reasonable rates." Statute does not address returns/over-earnings. In considering rate cases, the PSC compares the proposed ROE to similar utilities and attempts to balance, "the ability to attract capital at reasonable rates against impact on ratepayers."[42]

## LOUISIANA

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|---|---|
| *Earnings Band:* | Established in each utility's FRP: Entergy has 60 basis points, Cleco has 90, SWEPCO has 50 |
| *Shared Earnings:* | Differs by utility - Entergy has no sharing mechanism; Cleco refunds retains 40% within 85 points above collar, 0% for >85 points above; SWEPCO refunds 100% to customer |

The Louisiana PSC establishes target ROEs in utility formula rate plan proceedings. The PSC typically maintains earnings bands around 50-90 basis points for electric utilities and establishes a target or midpoint ROE. Each utility practices different FRP procedures, and updated FRPs are proposed for every 3-5 years. Annual earnings monitoring reports and are audited by consultants hired by the PSC. Auditors help determine rate adjustments and "reasonable" ROE targets.

The first Formula Rate Plan (FRP) was established by Order No. U-20925 in June 1995,[43] in response to the August 1994 proposal by Louisiana Power & Light (LP&L), which was later rebranded as Entergy Louisiana, LLC).[44] The FRP limited rate increases to no more than 2% per year and established an earnings band of 50 basis points. If earnings were outside the band, any change >5 basis points would result in a rate adjustment. No sharing mechanism was established.

ENTERGY. In earlier rate filings, Entergy employed an earnings band of 80 basis points In May 2020, Entergy filed its Formula Rate Plan Evaluation Plan for the test year ending December 31, 2019.[45] The opening filing noted that the last rider approved a 9.8% Evaluation Period Cost of Equity with +/- 60 basis points. In TY 2019, the company earned 9.7% earned return on equity, which is inside the band and did not warrant an adjustment. The filing requested an increase of revenue by $103 million. Entergy also noted that ongoing force majeure events related to COVID-19 may impact the rates through future filings. Overearnings adjust the rates downward.

CLECO. Since Cleco Power's first FRP in 1996 (docket no. U-21496), the company has employed an earnings band which does not include a lower limit, though earnings under the ROE will not be recovered from customers. In the last two decades, Cleco set target ROEs with "upper limits" 225,

[41] Kentucky Revised Statutes, Chapter 278. Section .030: Rates, classifications and service of utilities to be just and reasonable. https://e9radar.link/2be55
[42] February 2020. Presentation, Utility Ratemaking: The Kentucky PSC Process. Docket no. 2019-00271. https://e9radar.link/emrt
[43] June 1995. Order U-20925, Establishing Formula Rate Plan. Docket no. U-20925. https://e9radar.link/kvky
[44] August 1994. Direct Testimony and Exhibits of Louisiana Power & Light Company. Docket no. U-20925. P. 6. https://e9radar.link/qk8r
[45] May 2020. Entergy Louisiana, LLC Test Year Formula Rate Plan Evaluation Report, Part 1. Docket no. U-3558. https://e9radar.link/d7a3

100, 150, and 175 basis points above target ROEs, between 10-11.25%. Cleco applies an earnings sharing mechanism which refunds 60% of excess earnings to customers if the ROE is between the target and upper limit; above the upper limit, customers are refunded 100% of excess earnings. The most recent rate case filed by Cleco Power in July 2019[46] requested an increase in its target ROE from 10.0% to 11.0% with a dead band of 90 points. Cleco proposed that earnings over 11.9% but less than 12.75% will result in 60% refunded to customers and 40% retained by Cleco; earnings over 12.75% will be refunded entirely to Cleco.[47] This ratio was also approved in the last FRP (docket no. U-32779).

SWEPCO. Southwestern Electric and Power Company (SWEPCO) received approval for its first FRP in August 2008,[48] following the merger of AEP and SWEPCO. In its 2015 FRP, SWEPCO implemented[49] a 50 basis points earnings band (9.5-10.5%) which has been maintained since. SWEPCO uses a target ROE of 9.8%, which creates a non-linear earnings band (I.e. the target is closer to the lower limit of 9.5%). In December 2019, SWEPCO filed a base rate application[50] which cited earnings below the 9.8% target, at 7.8% and 7.0% in 2015 and 2017 test years. SWEPCO did not propose a new ROE but noted that rates should be adjusted upward to adjust for this difference. SWEPCO returns 100% of earnings in excess of the deadband to ratepayers.

If the Louisiana PSC has not rendered a final decision within one year of a utility's filing of an application for an increase, the utility may implement the proposed rate increase only if it files a protective bond or security with the PSC[51]. This provision incentivizes an efficient ratemaking proceeding and keeps rate cases consolidated.

## MISSOURI

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|---|---|
| *Earnings Band:* | None. Recent rate cases have determined a range of earnings for both Ameren and Evergy. |
| *Shared Earnings:* | None |

The Missouri Public Service Commission (PSC) typically authorizes a specific ROE, as opposed to setting a range of earnings. Rate case settlements can feature a stated ROE range so long as all signatory parties agree on the values. There is no procedure for establishing shared earnings or shared savings mechanism to distribute over earnings. As noted by PSC staff, if a utility were to over-earn following a rate case, they would keep all excess earnings until its rates were later adjusted downward.

[46] June 2019. Application for Implementation of Changes in Rates to be Effective July 1, 2020 and Extension of Existing Formula Rate Plan. Docket no. U-35299. https://e9radar.link/uky6

[47] June 2019. Direct Testimony of J. Robert Cleghorn on behalf of Cleco Power LLC. Pp. 19-20. Docket no. 35299. https://e9radar.link/e0bs

[48] August 2008. Order U-23327. Docket no. U-23327, Subdocket A. https://e9radar.link/p0us

[49] August 2016. Order U-32220-B adopting the Stipulated Settlement for the 2013 annual review of SWEPCO's formula rate plan. Docket no. U-32220. https://e9radar.link/14gm

[50] December 2019. Application for Approval of a Change in Rates, Extension of Formula Rate Plan and Other Related Relief; Direct Testimony of Thomas P. Brice, page 11-12. Docket U-35441. https://e9radar.link/dtgv

[51] See the following document for additional overview of the statutory authority of the LPSC: La. R.S. 45:1163.1, Rate increase through posting of a bond. https://e9radar.link/kmqc

AMEREN: A March 2020 PSC order[52] approved Ameren's rate request, determining that an implicit ROE in the range of 9.4% - 9.8% was reasonable, including Ameren's proposed $32 million revenue decrease. Parties initially agreed upon the approved ROE range in negotiation as part of the first rate case stipulation[53] filed in March 2020.

EVERGY: In February 2018, Evergy (previously doing business as Kansas City Power & Light) proposed a rate increase of $59.3 million with a ROE of 9.9%. The proposed ROE fell within a range of return, as described by company witness Hervert,[54] of 9.75% - 10.5%. In September 2016 a Stipulation Agreement[55] was filed which although initially failing to accept an approved earnings range did agree to lower the increase in revenue requirement to $3 million. In September 2016, the PSC approved[56] the settlement, setting a ROE in the range of 9.5% - 9.75%.

Notably, Missouri Senate Bill 564[57], passed in June 2018, allows the state's electric utilities to update rates in between general rate cases in order to account for changes in customer usage due to weather or energy conservation (i.e., a decoupling mechanism). Alternatively, utilities can institute plant in service accounting to defer and recover 85% of total depreciation expense and return on qualifying electric plants placed in-service. In July 2020, as part of Ameren's 2019 rate case, the OPC petitioned the commission to reduce the Fuel Adjustment Clause (FAC) split from 95/5% to 85/15%, asserting that the larger savings split would provide Ameren incentive to keep fuel costs as low as possible. Testimony submitted explained how the FAC could be manipulated to present a rate reduction in a general rate case when in fact it could be a delayed bill increase.[58] The FAC requires Ameren to pass 95% of its "prudently-incurred fuel and purchased power costs," above those included in its base rate, back to customers. Conversely, when fuel and power purchases are lower than what was calculated, customers receive 95% of excess payments, while Ameren retains the 5% of savings. In July 2020, the commission ordered[59] to keep Ameren's FAC mechanism intact at current levels.

## MISSISSIPPI

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|---|---|
| *Earnings Band:* | Earnings band varies by utility in formula rate plan. FRP Entergy 50bp. |
| *Shared Earnings:* | FRP adjusts rates; shared savings mechanism determined by performance-rate formula. |

Base rates for Mississippi's investor-owned utilities are determined annually as part of a formula rate plan (FRP). The FRP determines how earnings are distributed, including the establishment of shared earnings mechanisms based on a pre-determined performance-based formula rate, including metrics for customer satisfaction, reliability, and customer price rating. Mississippi Power Company first

[52] March 2020. Order. Docket No. ER-2019-0335. https://e9radar.link/06f27
[53] March 2020. First Stipulation and Agreement. Docket no. ER-2019-0335. https://e9radar.link/72479
[54] February 2016. Hervert Testimony. Docket No. ER-2016-0156. https://e9radar.link/18f47
[55] September 2016. Stipulation Agreement. Docket No. ER-2016-0156. https://e9radar.link/75072
[56] September 2016. Order Approving Settlement. Docket No. ER-2016-0156. https://e9radar.link/e2a10
[57] Senate Bill 564 (2018). https://e9radar.link/c49dc
[58] December 2019. Testimony, Mantle. Docket no. ER-2019-0335. https://e9radar.link/2f4c0
[59] July 2020. Amended Report and Order. Docket no. ER-2019-0335. https://e9radar.link/52f16

initiated its FRP in 1986, and Entergy in 1992.[60] FRPs are adjusted between rate cases in order to respond to changes in inflation, economic activity, and other utility costs. The utilities file annual updates to determine whether and how their rates should be adjusted within the earnings target. This filing includes a 'Look Back Provision' to compare the Formula Rate year Benchmark Return on Rate Base (BRORB) to the actual Earned Return on Rate Base (EROB). Differences are refunded or charged to customers.

- Entergy uses a Rate of Return on Rate Base Range (ROR Range) Earnings band to determine the level of its rate adjustment; set at plus/minus 0.50% (50 basis points) of the BRORB, or benchmark return, i.e., earnings band, as established by the commission.
- Mississippi Power's earnings band is determined in a 12-month period according it its Projected Retail Return on Investment (PRRI), [61] as filed it the Performance Evaluation Plan (PEP). The PRRI is compared against a "Range of No Change" revenue adjustment to determine whether revenues should be increased, decreased, or remain the same. No adjustments are made for amounts less than $250,00, and no revenue adjustment is to exceed 4% of annual aggregate retail revenues. MPCo's PEP filing requirements were updates in March 2020.

Mississippi Annotated Code Section 77-3-2 (3) (C) (i) and (ii)[62] codify procedures for the Public Service Commission to administer formula type rate of returns; including periodic rate evaluation and data verification. Hearings are required to determine compliance with the formula rate plan for data accuracy when the change in revenues are greater than $200,000, or 4% of annual utility revenues. Miss. Code Ann. § 77-3-37(8) allows for changes in rates to take effect 30 days from the date of the filing, unless considered a "major change;" defined as either: (a) an increase in rates increasing annual revenues by more than $100,000, or two percent (2%); or (b) a change in the rate design which has a significant impact on a class or classes of ratepayers.

ENTERGY MISSISSIPPI: In March 2020, Entergy Mississippi filed its 2020 Formula Rate Plan Evaluation Report (FRP-7, calendar year 2019).[63] The plan rider FRP7 resulted in a change in revenues of $24.58 million. Following the report, Entergy filed its 2019 Look-Back provision, demonstrating a Benchmark Return on Rate Base (BRORB) of 7.242%, which establishes an FRP bandwidth from 6.7% to 7.74% (104 basis points). The look-back falls below the lower limit by 0.02% thereby providing a Point of Adjustment of 6.91%, adjusting revenues by $7.4 million.

MISSISSIPPI POWER COMPANY (MPCo): The MPSC ordered MPCo to suspend its Performance Evaluation Plan (PEP) rate filings for regulatory years 2018, 2019 and 2020 and the company was directed to file a general rate case in 2019.[64] MPCo filed its 2019 rate case in November 2019,[65] calculating a revenue requirement decrease of $5.8 million, with performance rate adjustments based on rate schedule PEP-5A.[66] As ordered, the company's Performance Rating (CPR) will not change from what has been approved in PEP-5A. However, staff and MPCo agreed to revise the existing PEP-5A rate schedule to implement certain amendments, including: changing the filing date for the

[60] May 2016. Christensen Associates: Alternative Electricity Ratemaking Mechanisms Adopted By Other States. https://e9radar.link/db780
[61] January 2015, Mississippi Power Performance Evaluation Plan 5-A. https://e9radar.link/3fb59
[62] Mississippi Annotated Code Section 77-3-2; Declaration of Policy: https://e9radar.link/09ad9
[63] March 2020. FRP-7. Docket no. 2019-UN-219. https://e9radar.link/fa778
[64] February 2020. MPCo Stipulation. Docket no. 2019-UN-219. https://e9radar.link/fa778
[65] November 2019. Easterling Testimony - Rates. Docket no. 2019-UN-219. https://e9radar.link/46351
[66] January 2015. Performance Evaluation Plan (PEP-5A). https://e9radar.link/3fb59

annual PEP rate filing to March of each year; revising filing documentation and data to include more work papers to support the data and calculations (similar to Entergy Mississippi); PEP annual filings will be based upon a historic test year adjusted for "known and measurable" changes; PEP will now provide for the implementation of temporary rates, based on an amount subject to refund or credit to customer accounts, subject to a 2% cap of Evaluation Period Retail Revenues; surcharge or refunds are applied following the resolution of all disputes, if any; commission is designated to allow for the recovery of final-approved revenue requirement as if it had been implemented initially.

Notably, the Mississippi Public Service Commission has had a docket opened since 2014 in order investigate and review the adoption of a uniform formula rate plan for both Entergy and Mississippi Power company. The case has been in continuance since 2018.[67]

## NORTH CAROLINA

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|---|---|
| *Earnings Band:* | No earnings band established |
| *Shared Earnings:* | Earnings kept by utility |

The North Carolina Utilities Commission (NCUC) does not set an earnings band when determining utility rates and returns. Rather, a reasonable ROE is proposed by the utility, sometimes within a range of earnings, which is then subject of a contested case and hearing. Parties file comments, negotiating terms to settlement, which the NCUC rules on or makes adjustments of its own. Article 4 of NC General Statue 62-81[68] determines the procedure for hearings when deciding rate cases, or on "proceedings which substantially affect any utility's overall level of earnings or rate of return." Article 7 of N.C. Gen. Statute § 62-133[69] sets forward the requirements for which the commission is to consider when setting rates. Absence of a rate case settlement, the NCUC will exercise its own judgment to arrive at an independent conclusion for the level of rate of return on equity.

DUKE ENERGY CAROLINAS/DUKE ENERGY PROGRESS: A June 2018 order[70] accepted the stipulation between Public Staff and Duke Energy Carolinas, approving a ROE of 9.9%. As stipulated, the parties agreed that the revenue requirement should earn an overall rate of return of 7.35%; derived from applying an embedded cost of debt of 4.59% and a rate of ROE of 9.9%. Duke recommended a ROE of 10.75%, which was slightly above the midpoint of the recommended range of 10.25% to 11.00%.

Notably, Duke Energy Carolinas and Duke Energy Progress both file quarterly surveillance reports on their financial and operational data.[71] Article 2 of Chapter 62 of N.C. General Statute[72] initiated the reporting program in order to properly evaluate and monitor the financial condition of the companies, allowing the NCUC to stay abreast of changing financial conditions and how they may affect the financial operations of the regulated utilities. As such, each utility provides operational and financial data to allow the NCUC to maintain updated earnings and trends in the major revenue and expense accounts; kept in a position to foresee the improvements or deterioration in the company's

[67] See docket 2014-AD-118.
[68] Article 4 Section 62-81. Special procedure in hearing and deciding rate cases: https://e9radar.link/960f8
[69] Article 7 Statute 62-133:https://e9radar.link/960f8
[70] June 2018 Order: https://e9radar.link/9b9fb
[71] Docket no. M-1 Sub12DEC. Duke Energy Carolinas, LLC Quarterly Financial and Operational Data. https://e9radar.link/b2ade
[72] January 2020. Order requiring filing of financial data. Docket no. M-100, SUB 157. https://e9radar.link/07758

profitability. Public Staff reports that if earnings were to extend beyond the allowable return, they could bring in Duke for a rate review; however, without retroactive ratemaking in the state, Duke would capture any over earnings.

## OKLAHOMA

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|---|---|
| *Earnings Band:* | No earnings band established |
| *Shared Earnings:* | No prescribed methodology |

The Oklahoma Corporation Commission (OCC) does not set an earnings band when determining utility returns. Rather, the utility company proposes a reasonable ROE, which is typically adjusted in settlement, or set on a company-by-company basis at the discretion of the OCC. ROE determination is a matter of the litigated record.[73] The review of utility rates relies on an investigation of the test year; defined as a "mirror view of the past suspended within a limited but definite time frame through which we prophesy its duplication in the future," after making measurable adjustments for changes occurring within six months after the test year pursuant to Oklahoma Statute §284.[74]

OKLAHOMA GAS & ELECTRIC (OGE): In December 2018, noting that they were not earning sufficient operating income to produce a fair and reasonable return, OGE filed for a base rate increase[75] of $77.6 million, with rates sufficient to achieve a 9.90% ROE. Notably, the rate application included the recovery of approximately $600 million to install scrubber technology at two of OGE's coal-fired power units, Sooner and Muskogee. In September 2019, the OCC ordered[76] that the OGE base rates were to remain in-tact, denying the $77.6 million increase, as well as keeping the ROE at its existing level of 9.5%. The OCC did however approve scrubber costs, including Allowance for Funds used During Construction (AFUDC) treatment of $540 million at a full return component, calculated using the commission-approved 9.5% ROE.

PUBLIC SERVICE COMPANY OKLAHOMA (PSO): In August 2018, PSO filed for rate increase of $88 million, including a request to implement a performance based ratemaking model.[77] PSO's proposed Allowable Return on Equity (AROE) of 10.30% included a ROE deadband of 100 basis points, from 9.80% to 10.80%. As proposed, a rate increase would be triggered only if the earned ROE fell below 9.80%. Similarly, a credit to customers would occur if the earned ROE went above 10.80%. 75% of earnings above the upper limit deadband would be returned to ratepayers with the remaining 25% going to shareholders. In March 2019, the Commission issued an Order[78] approving the February Stipulation[79] and subsequent rate increase of $46 million based upon a return on equity of 9.40% and a return on rate base of 6.97%. As stipulated, the parties agreed to drop the PBR component, with PSO agreeing to not again seek commission approval of a PBR rate plan prior to October 2020.

Both OGE and PSO have a lost revenue adjustment mechanisms (LRAM) in order to adjust rates between rate cases to account for the impacts of energy efficiency on utility sales that was not considered in developing the rate case forecasts (i.e., a decoupling mechanism). Additional revenue

[73] August 2020. Interview with Policy Director Brandy Wreath.
[74] Oklahoma Statute. Title 17. Chapter 13A. Section 284. "In its review and examination of an application by a utility to change its rates the OCC shall give effect to known and measurable changes occurring or reasonably certain to occur within six months of the end of the test period upon which the rate review is based." https://e9radar.link/c01b3
[75] December 2018. Application. Case no. PUD 201800140. https://e9radar.link/2594e
[76] September 2019. Order No. 702531. Case no. PUD 201800140. https://e9radar.link/95229
[77] September 2018. Exhibit 2 Schedule PBR. Case no. PUD 201800097. Pp 228 – 230. https://e9radar.link/53eff
[78] March 2019. Order No. 692809. Case no. PUD 201800097. https://e9radar.link/53275
[79] February 2019. Stipulation. Case no. PUD 201800097. https://e9radar.link/a25bf

recovery mechanisms are determined on a case-by-case basis.[80] Oklahoma gas utilities use a PBR metric to review earnings annually, including a bandwidth around allowed return, whereas revenues are adjusted if returns are outside of the bandwidth.

## SOUTH CAROLINA

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|---|---|
| *Earnings Band:* | No earnings band established |
| *Shared Earnings:* | Refunds prescribed by legislative statute |

South Carolina, unlike North Carolina, does not have a statute of least cost when setting electric rates, nor does the Public Service Commission (PSC) set an earnings band when determining utility returns. Like North Carolina, ROE determination is a matter of the evidentiary record, with the PSC determining the appropriate return based on the evidentiary record. South Carolina General Statute § 58-27-810 determines how the PSC sets rates, including a fair return for investors and shareholders. The South Carolina Supreme Court has upheld this reasoning, finding that "the fixing of 'just and reasonable' rates involve the balancing of the investor and the consumer interests, finding that the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated."

Office of Regulatory Staff (ORS) confirmed that the state legislature has empowered the PSC to prescribe refunds in only two specific instances. Pursuant to Code 58-27-870[81], the PSC may order a refund for the difference between new rates under bond and the amount finally approved. Additionally, the PSC can order a reparation for a past charge in excess of the applicable rate under Code s 58-27-960, which states that if the PSC has found after hearing that the electrical utility charged an unreasonable, excessive, or discriminatory amount for electric service, they may order the electrical utility to make due reparation, with interest.[82] The PSC may not be a party to any cause of action.

DUKE ENERGY (DEC/DEP): In November 2018, DEC filed[83] for a revenue increase of $168 million, recommending a range in return on equity of 10.25% to 11% and concluding that a ROE of 10.75% best represented the cost of equity for DEC. Overall, three parties' witnesses addressed the issue of ROE in the rate case, including Duke, ORS, and Walmart. ORS recommended a ROE range of 9.1% to 9.5% with 9.3% as the "appropriate" midpoint. In May 2019, the commission ordered[84] that the most appropriate ROE was 9.5% for both DEC and DEP, as it fell within nine basis points of the national average for all electric utilities. The resulting allowable return results in a company income for return of $390.1 million.

DOMINION/SOUTH CAROLINA GAS & ELECTRIC: As a condition of the Dominion and South Carolina Electric and Gas (SCANA) merger (SCANA), the PSC ordered Dominion to file a general rate case by May 2020 in order to ensure that the actual savings from the merger were reflected in its retail rates. The commission suspended this request in May 2020[85], asserting the difficulty and uncertainty during the COVID-19 pandemic in which Dominion requested a 60-day extension for its new rates to take effect.

[80] April 2008. Case no. PUD 200700449. ID 3710105. https://e9radar.link/1c663

81 Section 58-27-870.Commission action on propose rate changes; refund of excess charges. https://e9radar.link/5b4a2

[82] Section 58-27-960 South Carolina Code of Law. Reparation orders; suits to enforce. https://e9radar.link/dc707

[83] November 2018. Hervert Testimony. Docket No. 2018-319-E. https://e9radar.link/d05ab

[84] May 2019. Order No. 2019-323. Docket 2018-319-E. P. 70. https://e9radar.link/d829b

[85] May 2020. Order 2020-313. Docket no. 2020-125-E. https://e9radar.link/84d67

## WEST VIRGINIA

| | |
|---|---|
| *Earnings Band:* | No earnings band established |
| *Shared Earnings:* | Earnings kept by utility |

West Virginia utilities do not use an earnings band; the PSC rules on a reasonable ROE in each rate case. Utilities file quarterly earnings reports, and the utility may retain 100% of earnings. If the utility is in consistent over-earnings range, the PSC may instigate an investigation of rates. The commission may order the utility to issue a refund, and may also require the utility to enter into a bond to issue rate refunds[86].

APPALACHIAN POWER COMPANY (APCo): APCo last adjusted its base rates in its 2018 rate case[87]. The PSC's February 2019 order[88] approved a settlement to increase rates by $44 million, including $8 million for the jointly-owned Wheeling Power Company. The increase was based on a ROE of 9.75%, which was the same rate from the 2015 rate case. Previous rate increases were approved in 2011 and 2015.

Utilities file annual fuel cost and tariff adjustments in "Expanded Net Energy Cost" (ENEC) proceedings. Tariffs included in the adjustment may include Vegetation Management, Energy Efficiency, and other tariff schedules. The adjustments made in these cases are reimbursed by the ratepayer without any utility profit. APCo's February 2020 ENEC adjustment filing[89] requested an increase in revenues of $82 million to account for true-ups. In contrast, base rate cases evaluate the utility's complete cost of service.

[86] West Virginia Code, Chapter 24. §24-2-4A. (f), Procedure for Changing Rates After June 30, 1981. https://e9radar.link/976ad
[87] Docket no. 18-0646-E-42T. Appalachian Power Company and Wheeling Power Company application to increase rates and charges. http://e9radar.link/caseie2553
[88] February 2019. Commission Final Order, Approving Joint Stipulation. Docket no. RPU-2013-0004. https://e9radar.link/1ejbv
[89] February 2020. Appalachian Power Co. and Wheeling Power Co. Petition to initiate the annual review and to update the ENEC rates currently in effect. Docket no. 20-0262-E-ENEC. https://e9radar.link/br1d

# OTHER NOTABLE STATE POLICY FEATURES

## HAWAII

Investor-owned Hawaiian Electric Companies (HECO) use a performance-based, multi-year ratemaking framework which uses revenue decoupling and revenue adjustment mechanisms (RAM). HECO's rates are subject to a revenue cap and incorporate various performance incentive mechanisms, including Service Quality and Targeted Energy Policy PIMs. HECO's current asymmetrical earnings sharing mechanism was established in an August 2010 rate case order.[90] The mechanism dictates that the first 100 basis points above authorized ROE, 75% retained by utility; if 200 basis points above authorized ROE, 50% retained by utility; and if more than 300 basis points above authorized ROE, 10% retained by utility. The order directs the utilities to file rate cases every three years to evaluate decoupling and RAM inputs.

In April 2018, the Hawaii PUC opened a docket[91] to investigate its transition to increasingly distributed and renewable generation systems through the restructuring of performance based rates. In May 2019, the Hawaii PUC issued a decision[92] to prioritize a variety of policy goals in "Phase 2." The commission directed HECO to create a balanced ESM with a deadband which reflects "target revenues, performance incentive revenues, cost trackers, and other components." In August 2019, HECO submitted its proposal[93] for a 5-year rate plan and associated incentive mechanisms. The proposal included a two symmetrical earnings sharing mechanism options, based on a target ROE of 9.5%. One option outlined five bands to determine sharings (i.e. +/- 100 basis points will act as the no-sharing deadband; +/- 200, 25% to customers and 75% to shareholders; up to band 5, for >800 basis points, which allocates 100% of the amount to customers). The other, more gradual option proposed a 150 basis points deadband in addition to two sharing bands (+/- 300 basis points shares earnings 50/50; >600 basis points allocates 100% of the amount to customers). The proposal also integrated ROE performance into other rate-setting mechanism, such as the "off-ramp" option (if the ROE is differentiated 300-500 basis points in 1-2 years), the cost of capital calculation, and other formulas.

## ILLINOIS

Performance-based formula ratemaking was created in Illinois in 2011, through the passage of the Energy Infrastructure Modernization Act (EIMA).[94] EIMA required the two participating utilities to invest more than $3 billion in various projects (smart grid, low income support, etc.); in return, utilities may implement performance-based formula rates. Statute outlines a ROE with 580 basis points plus the utility's US T-bond yield monthly average from the past calendar year actual results, based off of FERC Form 1. The ROE is given an earnings band of +/- 50 basis points.

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[90] August 2010. Final Decision and Order and Dissenting Opinion. Docket 2008-0274. https://e9radar.link/xd07
[91] Docket no. 2018-0088. Instituting Proceeding to Investigate Performance Based Regulation. https://e9radar.link/fu9q0
[92] May 2019. Decision and Order No. 36326. Docket no. 2018-0088. https://e9radar.link/d5097
[93] August 2019. Initial Comprehensive Proposal of the Hawaiian Electric Companies. Docket no. 2018-0088. https://e9radar.link/2469a
[94] Public Act 97-0616, SB 1652. Energy Infrastructure and Modernization Act. Located in 220 ILCS 5/16-108.5. https://e9radar.link/b0932

Utilities file updates annually to set rates for the upcoming year, determined over a 240 day process.[95] In the rate review, the commission will also review the performance metrics, including potential penalties for 30-38 basis points for failure to meet certain metrics. The Formula Rate Case methodology also does not implement a rate design determination other than following statute and precedent. Utilities reconcile their rates at the end of the year, reflecting an interest rate based on the ICC-approved weighted average cost of capital (WACC) each year.

## IOWA

In the late 1990s, FERC ruled that Iowa and other states could not require utilities to pay more than set "avoided cost" rates for renewable energy. In reaction to this order, Iowa implemented new mechanisms to encourage renewable energy development, including advance ratemaking principles, enacted in 2001.[96] Outside of advance ratemaking, Iowa utilities use three-year Multi-Year Rate Plans (MRPs) without earnings bands. A revenue sharing (i.e. earnings sharing) mechanism was established in a June 1997 stipulation which required MidAmerican to return 50% of its earnings above a ROE of 12%, based on a target ROE of 11%.[97] This was adjusted in March 2014, when the IUB approved[98] a rate case settlement which established a ROE of 10%, and an earnings sharing mechanism for 80% customer refund if the ROE were above 11%, and 100% customer refund if ROE is over 14%. The target ROE was continued at 11%. MidAmerican files annual revenue sharing reports in February of each year.

## MASSACHUSETTS

Massachusetts utilities have transitioned to performance-based ratemaking. In October 2019, the DPU approved[99] the joint National Grid rate case for a combined increase of $90.1 million with a ROE of 9.6%. National Grid was given a 200 basis point deadband, and 25% of earnings above the collar are kept by the utility. The order approved a new performance-based ratemaking formula and cost of service awards for various policy priorities. The rate plan will cover five years, with annual adjustments made according to benchmarking studies.

The Massachusetts DPU approved Eversource's revenue requirements prior to ruling on other elements of performance-based rate design. In its revenue requirement order in November 2017,[100] the commission approved a 10.0% ROE with a 200 basis point deadband. 75% of earnings above the collar are retained by the utility. The rate term was set for five years, pending that the actual ROE does not fall more than 200 basis points below the approved ROE.

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[95] September 2017. Presentation at the NARUC Staff Subcommittee on Accounting & Finance Meeting: Overview of Formula Rates in Illinois. https://e9radar.link/hipu

[96] House File 577, General Assembly 79 (2001-2003) session. Sec. 476.53, Electric Generating and Transmission Facilities. https://e9radar.link/0czq

[97] February 2001. Order Accepting Refund Report. Docket no. APP-96-1 and RPU-96-8. https://e9radar.link/oasv

[98] March 2014. Order Approving Settlement, With Modifications, and Requiring Additional Information. Docket no. RPU-2013-0004. https://e9radar.link/e4i8

[99] September 2019. Order. Docket no. 18-150. https://e9radar.link/l0x

[100] November 2017. Order Establishing Eversource's Revenue Requirement. Docket no. 17-05. P. 341. https://e9radar.link/0irg

**MONTANA**

In April 2019, the Montana State Legislature passed HB 244,[101] directing the allocation of cost sharing when implementing "cost-tracking adjustments" for the state's investor owned utilities. The legislation amends Montana Annotated Code Title 69, Chapter 3, Part 3 (69-3-331)[102] to determine ratemaking procedure for cost tracking and recovery. As amended, cost tracking adjustments, including for purchases from qualifying facilities and for fuel adjustments clauses are split at 90% spend to the customer and 10% from the utility, if cost sharing is required. A cost tracking adjustment may not include a deadband.

**WASHINGTON**

As part of a Puget Sound Energy (PSE) 2015 rate case, the Washington Utilities and Transportation Commission (UTC) determined a reasonable ROE for PSE was between 9.3% - 10%, settling on an ROE of 9.8%.[103] In determining the most appropriate return, the UTC considered PSE's established earnings sharing mechanism, whereas rate plan earnings require PSE to share 50/50 with customers any earnings above the authorized rate of return. Customers do not share any portion of the costs to PSE of earnings that are less than authorized.

## COVID-19 AND REGULATORY IMPACTS

Clearly, the impacts of the COVID-19 pandemic are both profound and unknown. Utilities have had to adopt more expensive operational practices to keep workers safe, more customers aren't able to pay their bills, and electricity sales have dropped.

The Energy Information Agency (EIA) forecasts that electricity consumption in the United States during 2020 will fall by over 4%. The commercial sector is expected to decline by 7%.[104] Throughout the nation, the pattern of declining sales is compounded by the expectation that consumer will suffer from economic hardship, leading to massive economic impacts and anticipated revenue that will be uncollectible.

In the face of these conditions, states are addressing the economic impacts in various ways. For example, some states have accelerated customer refunds that were scheduled to be return over the course of several years in recognition of the economic hardships established by COVID. Others are establishing regulatory assets that can be recovered over the course of several years, lessening the immediate impacts to customers. In other cases, utilities have experienced lower than anticipated fuel costs, which has prompted regulatory commissions to take steps to return these funds to consumers.

In Alabama, the Alabama Power Company filed its Energy Cost Recovery report[105] in July for the month of June, revealing $112 million of over-recovered fuel costs due to low oil and gas prices.

[101] HB 244. 2019 Legislation: https://e9radar.link/nvoo
[102] Montana Annotated Code. Title 69. Chapter 3. Part 3: https://e9radar.link/11208
[103] June 2015. Final Order. Docket No. UE-121697 p. 5: https://e9radar.link/c07de
[104] EIA, Short-Term Energy Outlook, July 7, 2020. https://www.eia.gov/outlooks/steo/
[105] July 2020. June 2020 Energy Cost Recovery Report. Docket no. 18148. https://e9radar.link/52d3a

Responding to public concern, in August the company issued a request[106] for accounting authority to refund $100M to customers for the over-recovery.

In May 2020, the Georgia Public Service Commission issued approval[107] of an $81M, 17.2% fuel-rate reduction for Georgia Power over the next two years in compliance with a May stipulation agreement. Since the last fuel-rate adjustment, Georgia Power noted a 300% increase of renewables in its energy mix. The fuel cost stipulation noted that in March 2020, Georgia Power over-recovered $44M, and directed Georgia Power to institute an Interim Fuel Rider to reduce the 2020 FCR Summer rates.

In May 2020, the Mississippi Public Service Commission (PSC) approved[108] for an interim adjustment to Entergy Mississippi's Energy Cost Factor in order to credit $50 million of over-recovered fuel costs to customers in summer months. The factor was filed for effect for June-September, after which the interim adjustment will terminate and the current net ECF will resume. The adjustment will result in a decrease of $9.71 per month on average over the four-month period.

In August 2020, the Minnesota Public Utility Commission (PUC) approved[109] Minnesota Power's April 2020 petition to adjust its rates in response to COVID-19, effectively withdrawing its rate case and refunding $12 million of interim rate charges to customers. The recalculated rates will result in an additional $35.8 million (to be offset by $25.8 million in updated value) needed for recovery in a future rate case. Additionally, in June 2020 the Minnesota PUC approved[110] Xcel's April 2020 proposal to reduce its 2020 fuel forecast and monthly cost charges by $25 million over the period of June-August 2020

In March 2020, the Washington Utilities and Transportation Commission (UTC) approved[111] a rate case settlement for Avista Corp. which included a fast-tracked customer refund for the Energy Recovery Mechanism (ERM) bill rebate ($3.3 million); a total of $51 million in refunds were accelerated to mitigate the impacts of COVID-19. As a result, Avista electric customers will not see a rate increase this year.

These examples highlight actions that regulators have taken to ensure that any refunds, rate reductions or similar steps that can put funds into consumers hands are being accelerated. Such actions suggest that legislators may support similar actions or directives that relieve immediate customer hardship. In the face of these known customer impacts, it may be prudent to examine ways to mitigate the shock to customers.

[106] August 2020. Request Approval of Accounting Authorization for Alabama Power Company. Docket no. U-5344. https://e9radar.link/08f5e

[107] May 2020. Order Adopting Stipulation. Docket no. 43011. https://e9radar.link/8ec58

[108] May 2020. Order approving the Interim Adjustment. Docket no. 2013-UN-178. https://e9radar.link/426k

[109] August 2020. Order Approving Petition and Resolving Rate Case With Conditions. Docket no. GR-19-442. https://e9radar.link/woub

[110] June 2020. Order approving Xcel's rate adjustment. Docket no. 40-437. https://e9radar.link/4c973

[111] March 2020. News Release. State regulators fast track $51 million in refunds. Docket no. 190334. https://e9radar.link/4e665

## CONCLUDING REMARKS

The process of determining appropriate and fair utility rates requires a careful balance of risk and reward, as well as attention to a wide range of complicated financial mechanisms particular to state's regulatory environment, precedent and history. In nearly all jurisdictions – including Virginia – the rates that are presented to consumers are a complicated amalgam of traditional ratebase regulation, single-issue cost adjustments and other mechanisms that address specific investments or initiatives. As a result, context and deliberation are assumed to be critical components of the ratemaking process. Isolated mandates established by legislation remove that context.

The prescriptive nature of the two specific aspects examined in the investigation – the earnings band and over-earnings retention mechanism – set Virginia apart from the comparable states included in this review. While these mechanisms per se are not unique, it would seem that other states defer these decisions to an engaged, deliberative process hosted by their regulatory commission. This observation is particularly relevant given the complicated nature of ratemaking, especially as it has evolved over the past several decades.

In general, these provisions appear untethered from any specific performance metrics (such as those typically associated with performance-based rates) or the organized structure of a formula rate or multiyear rate plan.

It may be the case that these components are both appropriate and effective tools of utility regulation in Virginia. However, the best regulatory practices in the states reviewed (and, indeed, across the country) suggest that these isolated requirements established by the legislature are anomalous – precisely because they are established by the legislature outside of administrative process that includes the opportunities to present evidence, question assumptions and generally conform to norms established by administrative law proceedings.

# GLOSSARY OF TERMS

| | |
|---|---|
| *Basis Points (bp)* | Unit of measure for the percentage change in a value or rate of financial instruments. One basis point equates to one hundredth of one percent, or 0.01%. |
| *Collar* | A collar is an established range of possible positive or negative returns and provides a hedge against possible losses or excess earnings. |
| *Deadband* | A deadband – also known as an "earnings band" – is a range of potential utility earnings in which no rate adjustments will be made. The deadband surrounds the authorized earned return measure (ROE). If returns falls outside of this pre-determined range, rates will be increased (or decreased) to achieve the target return. For example, a 100 basis point deadband denotes a 50 basis point band on either end of the target ROE. |
| *Earnings band* | In Virginia, defined such that in a triennial review case as part of the Re-Regulation Act, a utility's rates may be increased or decreased only if the utility's earnings exceed a certain "earnings band" of 70 basis points (0.7%) above or below its authorized combined rate of return.<br><br>For example, statute gives Dominion permission to retain 30% of the over earnings that are above the 70 basis points collar are retained by shareholders; 70% are credited to customers Dominion's authorized ROE is 9.2%. So, for example, if Dominion is found to have earned revenues of $100 million above 9.9%, shareholders keep $30 million and customers get $70 million. |
| *Earnings Sharing Mechanism* | Rate-setting mechanism that allows for rate adjustments outside of general rate case proceedings when actual ROEs would otherwise fall outside of specified bands around authorized ROEs. No rate adjustment is made when actual ROEs fall within the band; and rates are adjusted to share between customers and shareholders the excess or deficient earnings outside of the band. Earnings sharing mechanisms help hold down procedural costs of assuring that utilities' actual ROEs do not stray far from authorized ROEs due to the operation of automatic rate change mechanisms or to changing business conditions. |
| *Formula Rate Plan* | The use of predetermined formulas to calculate automatic rate adjustments to keep the utility's actual ROE within or near a specified band around the authorized ROE. Formula rate plans reduce the frequency and costs of rate cases, reduce utilities' financial risk and thereby reduce their costs of capital, allow customers to gain an early share of any cost efficiencies that the utility may develop between rate cases, allow rates to more closely track changes in electricity market conditions, and make rate changes more gradual over time. As of 2016, only four states, mostly in the south, have formula rate plans for electric utilities. |
| *Multi-Year Rate Plan* | Escalates rates over time according to assumptions about the rates of escalation of specified utility costs, an FRP adjusts rates to meet banded ROE targets, perhaps adjusted according to measures of performance such as customer satisfaction and local distribution system reliability. Multi-year rate plans thus focus on the utility's costs, while FRPs focus on ROEs. |

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