September 11, 2022

VIA ELECTRONIC FILING

Mr. Bernard Logan, Clerk
c/o Document Control Center
State Corporation Commission of Virginia
Tyler Building - First Floor
1300 East Main Street
Richmond, Virginia 23219

RE: Reconsideration of Order on Application of Virginia Electric and Power Company for approval and certification of the Coastal Virginia Offshore Wind Commercial Project and Rider Offshore Wind

Case No. PUR-2021-00142

Dear Mr. Logan:

Enclosed for filing in the above-captioned proceeding is the **Direct Testimony of David W. Schnare, Esq. Ph.D.**, which consists of a 7 page Response to the Commission's August 25, 2022, Order inviting additional comment regarding issues raised in Virginia Electric and Power Company's August 22, 2022, Petition for Limited Reconsideration, provided on behalf of the **Thomas Jefferson Institute for Public Policy**.

Please do not hesitate to call if you have any questions in regard to the enclosed (571-243-7975).

Sincerely,

/s/ David W. Schnare

David W. Schnare, Esq. Ph.D.

Enclosure

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION

APPLICATION OF VIRGINIA ELECTRIC AND POWER COMPANY For approval and certification of the Coastal Virginia Offshore Wind Commercial Project and Rider Offshore Wind, pursuant to § 56-585.1:11, § 56-46.1, § 56-265.1 et seq., and § 56-585.1 A 6 of the Code of Virginia	Case No. PUR-2021-00142

TESTIMONY OF DAVID W. SCHNARE, Esq. Ph.D.
on behalf of
THE THOMAS JEFFERSON INSTITUTE FOR PUBLIC POLICY

September 11, 2022

In response to the prolix August 22, 2022, Petition for Limited Reconsideration filed by the Virginia Electric and Power Company ("VEPCO"), the State Corporation Commission's August 25, 2022, Order distilled the issues raised by VEPCO to the fundamental question: to what extent may the presumption of reasonably and prudently incurred costs in Code § 56-585.1:11 C. 1. be rebutted. Restated, what latitude does the Commission have in determining whether costs incurred are reasonable and prudent. At core, this question is grounded in the essential question the Commission routinely faces – to what degree should the investors of a private utility, as opposed to the utility's customers, bear the risks associated with a project.

Taking into account the dictates of the Constitution of Virginia, the Code of Virginia and case law, the Commission retains the authority to balance the risks and may do so through the lens of some form of a performance guarantee. When its investors, through filings of VEPCO, make the claim that the average annual turbine availability of the Project will equal or exceed 97% or the Project's net capacity factor will exceed 37% on a three-year rolling average basis, they establish an expectation that the costs associated with meeting those performance levels are both reasonable and prudent. Compared with the actual efficiency data of offshore wind projects, VEPCO predictions operate outside of the reasonable expectations of their customers and the Commission, and would result in an unjust shift of risk from the investors to VEPCO's customers.

THE LIMITS OF CODE § 56-585.1:11 C. 1.

VEPCO asserts that Virginia Code § 56-585.1:11 C.1. ("1:11 C.1.") establishes a three-pronged test that, if met, statutorily determines that costs "associated with" offshore wind projects are presumed "reasonable and prudent" and are the "exclusive" conditions the SCC is permitted to consider. VEPCO argues that consideration of anything other than those three

conditions constitutes adding an additional condition for cost recovery, citing to *Appalachian Power Co. v. State Corp. Comm'n*, 284 VA. 695, 707 (2012).[1]

A plain reading of 1:11 C.1 dispels VEPCO's take on this issue. The statute clearly authorizes the SCC to "determine the reasonableness and prudence of such costs" but limits that determination to matters other than the three conditions laid down in 1:11 C.1. In other words, having examined the cost recover request and found VEPCO has met the three conditions, the SCC then examines the request to determine whether those costs are "otherwise unreasonably and imprudently incurred."[2] Indeed, the statute further specifically directs the SCC to look beyond the three enumerated presumptions and "give due consideration to (a) the Commonwealth's renewable portfolio standards and carbon reduction requirements, (b) the promotion of new renewable generation resources, and (c) the economic development benefits of the project for the Commonwealth, including capital investments and job creation."[3]

Nothing in 1:11 C.1 limits the SCC from considering additional, rational, conditions when determining whether the cost recovery request is "otherwise" unreasonable and imprudent.

***APPALACHIAN POWER CO.* (2012) IS NOT APPOSITE**

VEPCO cites to *Appalachian Power Co. v. State Corp. Comm'n* arguing that rules of statutory construction prohibit adding language to or deleting language from a statute. The facts of *Appalachian Power* (2012) are, however, distinctly different from the instant case. In *Appalachian Power* (2012), the Court was interpreting a statute that ***mandated*** the Commission approve a utilities petition for a rate adjustment clause. Indeed, Code § 56–585.1(A)(5)(e), at

[1] Petition of Virginia Electric and Power Company for Limited Reconsideration at 11-12.
[2] Virginia Code § 56-585.1:11 C.1
[3] *Id.*

issue in *Appalachian Power* (2012), specifically states that the Commission "shall" approve a utilities petition if the stipulated conditions are met.

In contrast, 1:11 C.1 does no more than establish a baseline set of conditions to be presumed as reasonable and prudent. If these conditions are not met, the SCC is free to find the cost request unreasonable and imprudent. If, however, the conditions are met, the SCC is then required to consider additional elements and is not limited to only those identified in 1:11 C.1. Rather, the statute opens 1:11 C.1. with the clear mandate to "determine the reasonableness and prudence of any such costs" and, unlike Code § 56–585.1(A)(5)(e), does not mandate rate approval if the three conditions are met.

A PERFORMANCE GUARANTEE OF A NET 42% CAPACITY FACTOR IS A NECESSARY AND APPROPRIATE CONDITION

VEPCO argues that the SCC lacks authority to establish a performance guarantee but fails to cite to authority on which to base its argument. In fact, the opposite is true. The SCC is required to establish some means to ensure costs are just and reasonable. Code § 56–585.1(C) provides:

> Except as otherwise provided in this section, the Commission shall exercise authority over the rates, terms and conditions of investor-owned incumbent electric utilities for the provision of generation, transmission and distribution services to retail customers in the Commonwealth pursuant to the provisions of Chapter 10 (§ 56–232 et seq.), including specifically § 56–235.2.

Code §56-235.2 establishes a requirement VEPCO failed to mention was explicitly established as a statutory requirement in *Appalachian Power* (2012), that the SCC must set "just and reasonable rates as directed in Chapter 10 of Title 56 of the Code." [4] In making the "just and reasonable" determination, the Commission is restricted to approve only those costs it "finds

[4] *Appalachian Power Co. v. State Corp. Comm'n*, 733 S.E.2d 250, 256 (Va. 2012)

reasonably can be *predicted* to occur"[5] (*emphasis added*). In its Final Order, the Commission found that "[t]he lifetime revenue requirement and levelized cost of energy estimates *presented by the Company are based on a projection* that CVOW, once in operation, will achieve a net 42% capacity factor."[6] (*Emphasis added*.) Indeed, VEPCO does not retreat from its expectation that the Project will achieve an *average* annual net capacity factor of 42% *over the 30-year life of the Project*."[7] (*Emphasis in the original.*)

VEPCO wants the Commission to ignore the predictions it made, ignore the duty to base its "just and reasonable" determination on what can "reasonably be predicted to occur," and instead adopt an agreement (stipulation) made by some, but not all interested parties, and by no one representing the customers. This would be *ultra vires*.

As well, the Constitution of Virginia not only authorizes, but mandates "the interests of the consumers of the Commonwealth are represented" by the Commission.[8] And, it has long been settled, and the Supreme Court has recognized that

> a rate may be so low or so high as to be unjust and unreasonable as a matter of law. But between these there is a field, a rather wide field, of legislative discretion as to what is a just and reasonable rate. It is clear, we think, that the Constitution of Virginia vests the State Corporation Commission of Virginia primarily with the power and duty to exercise the legislative discretion of the Commonwealth within these limits.

N. W. Ry. Co. v. Commonwealth, 162 Va. 314, 323 (Va. 1934).

THE COMMISSION MUST BALANCE INVESTOR EXPECTATIONS AGAINST CUSTOMER INTERESTS AND THUS MUST HAVE A PERFORMANCE GUARANTEE

As stated in the opening paragraph of this Testimony, and obviously well understood by the Commission, state corporation commissions have the duty to balance the interests of

[5] Virginia Code § 56-235.2 (A).
[6] State Corporation Commission's August 25, 2022, Final Order in the matter of PUR-2021-00142 at p. 8.
[7] Petition of Virginia Electric and Power Company for Limited Reconsideration at 21.
[8] Constitution of Virginia, Article IX, Sec. 2.

investors against the interests of a utility's customers.[9] In Virginia, this balancing is manifest on the face of the relevant statute, allowing for rates not in excess of actual costs and a fair rate of return on investments. *And see*, Virginia Code § 56-585.1 & § 56-235.3 (fair rate of return) and § 56-234 (A) & § 56-235.2 (just and reasonable rates).

By definition, a rate is imprudent and unreasonable when it incorporates costs that arise because VEPCO and its investors made investments based on too rosy a set of assumptions and predictions. VEPCO claims it's project will have average annual turbine availability of 97% or greater and agrees to this in the stipulation. There is no reasonable basis for this estimate. *Onshore* wind turbines average 96 to 99 percent availability. In comparison, *offshore* turbines have been found to be available only 80 to 84 percent of the time.[10] VEPCO does not, however, hang its hat on availability.

VEPCO wishes to low-ball its expectations in a manner that makes them both unreasonable and imprudent by using a three-year rolling average net capacity factor of 37%. In contrast, the International Energy Agency found that in 2018, offshore wind projects realized between 38 to 43% of rated capacity.[11] The Commission's ordered rate of 42% is within the historical capability of offshore wind, is the basis for VEPCO's rate projections and is a reasonable and prudent performance expectation.

VEPCO and its investors cannot have it both ways – a hedge against the likelihood of below expectations and a windfall from customers when that likelihood becomes manifest. The

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[9] *See*, *e.g.*, *Farmland Industries v. Kansas Corp. Comm'n*, 943 P.2d 470, 490 (Kan. Ct. App. 1997) ("KCC had to balance the interests of investors and customers")

[10] Ceveaso, D., et al., "*Reliability, availability, maintainability data review for the identification of trends in offshore wind energy applications*", Renewable and Sustainable Energy Reviews 136 (2021) 110414, Table 11, p. 15. *See*, https://doi.org/10.1016/j.rser.2020.110414 (*accessed* 9-8-2022).

[11] IEA, "Offshore Wind Outlook 2019" p. 20. *See* https://iea.blob.core.windows.net/assets/495ab264-4ddf-4b68-b9c0-514295ff40a7/Offshore_Wind_Outlook_2019.pdf (Capacity factor describes the average output over the year relative to the maximum rated power capacity.) (*Accessed* 9/8/2022.)

investors must decide whether to use reasonable expectations as the basis for cost recovery or must choose not to make the investment. A statutory balancing of the burden of risk on what is clearly a highly risky investment lays that burden on the investors, not the customers.

CONCLUSION

For the reasons given above, and taking into account the dictates of the Constitution, the statutes and case law, the Commission retains the authority to determine what constitutes an unreasonable and improvident cost and may do so through the lens of the performance guarantee as memorialized in the August 5, 2022, Final Order.

Submitted by:

/s/ David W. Schnare

David W. Schnare, Esq. Ph.D.