

HOUSE BILL REPORT

E2SHB 1301

As Passed House:
March 9, 2013

Title: An act relating to creating clean energy jobs in Washington state through renewable energy incentives.

Brief Description: Creating clean energy jobs in Washington state through renewable energy incentives.

Sponsors: House Committee on Finance (originally sponsored by Representatives Morris, Ryu, McCoy, Hudgins, Morrell and Pollet).

Brief History:

Committee Activity:

Technology & Economic Development: 1/29/13, 2/14/13 [DPS];
Finance: 2/25/13, 2/28/13 [DP2S(w/o sub TED)].

Floor Activity:

Passed House: 3/9/13, 58-39.

Brief Summary of Engrossed Second Substitute Bill

- Provides a voucher entitling eligible applicants to receive renewable energy investment cost recovery incentive payments for a term of ten years, and streamlines application procedures.
- Moves program administration from the Department of Revenue to an agency to be designated by the Governor.
- Authorizes qualifying utilities to claim an additional tax credit for electricity generated by a utility-owned solar energy system with a capacity of up to 100 kilowatts installed on the premises of a residential or commercial retail electric customer.
- Authorizes the Utilities and Transportation Commission to allow utilities to recover in tariffs the cost of certain distributed solar energy systems.
- Establishes performance benchmarks, review by the Joint Legislative Audit and Review Committee, and reporting requirements.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

HOUSE COMMITTEE ON TECHNOLOGY & ECONOMIC DEVELOPMENT

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 10 members: Representatives Morris, Chair; Habib, Vice Chair; Crouse, Assistant Ranking Minority Member; Freeman, Hudgins, Maxwell, Morrell, Stonier, Tarleton and Wylie.

Minority Report: Do not pass. Signed by 5 members: Representatives Smith, Ranking Minority Member; Dahlquist, Kochmar, Vick and Zeiger.

Staff: Jasmine Vasavada (786-7301).

HOUSE COMMITTEE ON FINANCE

Majority Report: The second substitute bill be substituted therefor and the second substitute bill do pass and do not pass the substitute bill by Committee on Technology & Economic Development. Signed by 8 members: Representatives Carlyle, Chair; Tharinger, Vice Chair; Fitzgibbon, Hansen, Lytton, Pollet, Reykdal and Springer.

Minority Report: Do not pass. Signed by 5 members: Representatives Nealey, Ranking Minority Member; Orcutt, Assistant Ranking Minority Member; Condotta, Vick and Wilcox.

Staff: Jeffrey Mitchell (786-7139).

Background:

I. The Renewable Energy Investment Cost Recovery Incentive Program.

In 2005 the Legislature created a Renewable Energy Cost Recovery Incentive Program (Program) to encourage individuals and businesses to purchase and install renewable energy systems. Under the Program, an individual, business, local government, or Community Solar project that owns and operates an eligible renewable energy system (system) may apply to receive annual incentive payments from the applicant's electric utility. These payments, in the form of a production incentive for each kilowatt-hour of electricity produced, help subsidize the cost incurred in purchasing and installing the system. The utility connected to the system, referred to in the statute as the "light and power business," receives a tax credit from the Department of Revenue against its Public Utility Taxes equal to the incentive payments that it makes under the Program. A utility is allowed a credit against its public utility tax (PUT) for incentives paid, capped annually at \$100,000 or 0.5 percent of its taxable power sales, whichever is greater.

Eligible systems produce electricity from solar, wind, or anaerobic digestion and are typically installed on or near residential and commercial buildings to which they supply electricity. As such, the renewable energy systems are a type of distributed generation, in which energy is produced at or near the intended place of use, reducing demand for energy from the electric grid. To connect to a utility's electric grid, distributed generators must enter an interconnection agreement with the connecting utility and must enter into a contract or transaction to sell electricity to the utility. A number of state and federal laws govern these

transactions, the sale and purchase of electricity, and the development of distributed generation resources.

Community Solar Projects.

In 2009 the Program was expanded to provide incentives for "Community Solar" projects. Community Solar projects include: (1) solar energy systems placed on local government property that are owned by local individuals, households, or nonutility businesses; (2) utility-owned solar energy systems voluntarily funded by the utility's ratepayers in exchange for credits on their utility bills; and (3) company-owned solar energy systems, where the owner is a limited liability company, a cooperative, or a mutual corporation or association.

Payments.

Utilities, denominated as "light and power businesses," are responsible for providing incentive payments to the owners of eligible systems. Incentive payments are capped at \$5,000 annually per applicant. For each kilowatt-hour of energy produced, an eligible system owner may receive incentive payments of at least 15 cents, and Community Solar projects are eligible to receive incentives at twice that rate. To promote the use of equipment manufactured in Washington, multipliers are used to enhance the base rates, depending upon the degree and type of system components that are manufactured in Washington.

Incentive payments are applied for annually and there is no statutory guarantee that a person or entity receiving the incentive payment in any given year will continue to receive a payment the following year.

Cap on Total Credits Available.

If the amount of requests for incentive payments exceeds the amount of funds available for PUT credit to the utility, the incentive payments to applicants must be reduced proportionally. Incentive payments to participants in a utility-owned Community Solar project may only account for up to 25 percent of the total allowable credit. Incentive payments to participants in a company-owned Community Solar project may only account for up to 5 percent of the total allowable credit.

Measuring and Reporting Electricity Production.

Each year, a participant in the Program must reapply for the incentive, providing a statement of the amount of kilowatt hours generated by the system in the prior fiscal year. The energy output is measured by a production meter that records the amount of electricity generated.

Duration of Program.

The Program expires June 30, 2020.

II. Tariff Setting by the Utilities and Transportation Commission.

The Utilities and Transportation Commission (Commission) regulates the rates and services of private (i.e. investor-owned) utility companies. The Commission has a statutory duty to determine and set rates that are fair, just, and reasonable to consumers, and sufficient to enable the company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risks assumed. The Commission hears rate cases in a formal, legal setting, with an opportunity for interested parties to submit evidence for the Commission to consider in issuing its decision.

The Commission determines whether utility expenses and investments are prudent before allowing a utility to recover the cost of such investments through rates. In addition, the Commission determines the company's "rate base" and an appropriate rate of return that a utility may recover for its investments. Investor-owned utilities are not prohibited by law from acquiring specific generation assets, like photovoltaic systems that generate electricity based on solar power. However, when an investor-owned utility acquires a resource, the Commission determines the extent to which the utility may recover its investment through its rates. In current practice, the Commission considers the prudence of an investment based on the information available at the time the company made its decision to acquire a resource.

When an investor-owned utility seeks to sell an asset, including a distributed generation facility, the Commission has a statutory directive to require the utility to demonstrate a net benefit to customers from the asset's sale, if the asset is "necessary and useful".

Investor-owned utilities serve about 45 percent of customers in the state, while municipal utilities, public utility districts and various consumer-owned utilities serve the other 55 percent. The Commission does not regulate publicly-owned electric utilities, nor does it regulate small, independent generators that do not hold themselves out to provide electric service the general public.

III. Utility-Led Financing of Renewable Energy Systems and the Energy Independence Act. Washington, like many other states, has a renewable portfolio standard (RPS). Washington's RPS requires electric utilities serving more than 25,000 retail customers in the state to meet renewable energy targets or pay penalties. The Energy Independence Act (EIA) requires utilities to use "eligible renewable resources or acquire equivalent renewable energy credits," or a combination of both, to meet annual targets of at least 3 percent of load by January 1, 2012, 9 percent by January 1, 2016, and 15 percent by January 1, 2020.

While the EIA does not require utilities to acquire any particular quantity of distributed generation, it does allow a utility to claim a double credit for distributed generation if the utility: (1) owns or has contracted for the distributed generation and the associated renewable energy credits; or (2) has contracted to purchase the associated renewable energy credits.

All electric utilities in Washington with 25,000 customers or more, including those not subject to regulation by the Commission, must develop integrated resource plans, defined as "an analysis describing the mix of generating resources and conservation and efficiency resources that will meet current and projected needs at the lowest reasonable cost to the utility and its ratepayers". When investor-owned utilities develop these plans, an assessment of the costs of available distributed generation is included in the "least cost resource modeling" conducted by that utility.

Summary of Engrossed Second Substitute Bill:

I. The Renewable Energy Investment Cost Recovery Incentive Program.

The Engrossed Second Substitute House Bill changes the existing Renewable Energy Investment Cost Recovery Incentive Program (Program) in the following ways:

Eligibility to Receive Incentive Payments.

The Engrossed Second Substitute House Bill expands eligibility to receive incentive payments, by authorizing any "person" who is the meter holder and owner of an eligible renewable energy system (system) to apply to receive annual incentive payments from its utility. "Person" means "any individual, receiver, administrator, executor, assignee, trustee in bankruptcy, trust, estate, firm, copartnership, joint venture, club, company, joint stock company, business trust, municipal corporation, political subdivision of the state of Washington, corporation, limited liability company, association, society, or any group of individuals acting as a unit, whether mutual, cooperative, fraternal, nonprofit, or otherwise and the United States or any instrumentality thereof".

No person may receive incentives for electricity generated in excess of the net kilowatt-hours consumed annually at the metered location. Retail electric customers are limited to receiving incentive payments for systems with a generating capacity of five kilowatts or less. Meter holders who are not retail electric customers may receive incentive payments for systems with a generating capacity of 100 kilowatts or less. Total incentive payments are capped at \$25,000 per year per eligible system.

Vouchers.

Program administration is moved from the Department of Revenue to an agency designated by the governor (Agency). The Agency is authorized to issue vouchers entitling a recipient to receive incentive payments for a term of ten years. No vouchers may be issued after June 30, 2023. The voucher is transferrable to a new meter holder as long as the new meter holder is also a person eligible to receive incentive payments. The award of a voucher creates a contractually enforceable promise on behalf of the state to authorize the utility to receive a credit against its public utility taxes equal to the annual incentive payments made by the utility in any fiscal year.

Eligible Systems.

The size of eligible systems is limited to five kilowatts for a residential retail electric customer, and 100 kilowatts for an entity that is not a residential retail electric customer, and the annual recovery is capped at \$25,000 per year per eligible renewable system. An owner of a system who is already receiving renewable energy investment cost recovery incentive payments prior to July 1, 2013, may apply to receive a voucher entitling the person to receive incentive payments until June 30, 2023.

Incentive Rates.

Existing incentive rates are retained. On July 1, 2018, new base rates and multipliers may go into effect, applicable to vouchers issued after that date, to reflect decreases in the capital costs of purchasing and installing a system, changes in the levelized costs of such systems, or other factors. The Agency may adjust rates sooner, if requests for the incentive exceed 50 percent of the funds available for crediting the participating utilities.

Statewide Cap.

The total credits available statewide to public utilities is the aggregate of 0.5 percent of each participating utility's annual taxable power sales in the immediately preceding calendar year. If not enough credits are available to meet demand for the incentives, despite the provision

allowing the Agency to adjust rates downward once requests for the incentive exceed half of the available credits, credits are allocated on a first-come, first-served basis.

Community Solar.

Community Solar projects continue to receive a higher base rate for incentive payments than other Program participants, with the total recovery for any applicant in a Community Solar project capped at \$5,000 per year. System size for Community Solar projects receiving the incentives appears to be capped at 100 kilowatts.

Systems Financed by Third Parties other than Utilities.

After December 31, 2015, the Agency may authorize systems owned by third parties other than utilities to qualify for the Program, if such authorization is in compliance with other applicable law or rule and consistent with the legislature's objectives.

Performance Milestones.

Performance milestones are established for assessing the effectiveness of the tax policy, including increased utilization of the available tax credits, a 100 percent increase in the number of solar energy systems installed and receiving the incentive, a growth in solar and renewable-related employment, a decrease in the levelized cost of the systems receiving the tax preference, and leveraging of nonstate funds. The Department of Revenue must collect data and report annually to the Legislature on progress toward achieving the performance milestones. The Joint Legislative Audit and Review Committee must assess the performance of the incentives in 2019.

II. Utility-led Financing of Solar Energy Systems.

A qualifying utility is authorized to claim a tax credit for electricity generated by a solar energy system with a capacity of 100 kilowatts or less that is owned by the utility and installed on the premises of a residential or commercial retail electric customer of the utility. "Qualifying utility" means a "consumer-owned" or "investor-owned" electric utility that serves more than 25,000 customers in the State of Washington. A "consumer-owned" utility means a municipal electric utility formed under Title 35 RCW, a public utility district formed under Title 54 RCW, an irrigation district formed under chapter 87.03 RCW, a cooperative formed under chapter 23.86 RCW, or a mutual corporation or association formed under chapter 24.06 RCW, that is engaged in the business of distributing electricity to more than one retail electric customer in the state. An "investor-owned utility" means a company owned by investors that meets the definition of RCW 80.04.010 and is engaged in distributing electricity to more than one retail electric customer in the state.

Credits that may be claimed pursuant to this program by any individual qualifying utility are capped at 0.5 percent of the qualifying utility's taxable power sales or \$100,000, whichever is greater. These credits are additional to those provided to compensate utilities for incentive payments made under the Program.

The qualifying utility may claim a tax credit that is equivalent to the amount of incentive payments a Community Solar project with the same attributes would have been eligible to receive under the Program. In addition, the qualifying utility retains ownership of the environmental attributes of the solar energy system. In other words, the solar energy system may be counted by the utility toward its annual targets under the Energy Independence Act.

Performance milestones are established for utility-financed systems, including increased utilization of available tax credits at a growth rate of 5 percent each year for the first five years of the program, and an improved ability of consumers to install systems on their real property, regardless of their financial ability to fully fund the up-front installation costs for a system. Requirements are established for information that must be provided to a customer in a contract to lease or otherwise purchase power from a utility-owned system. Qualifying utilities must report to the Joint Legislative Audit and Review Committee the average price per kilowatt-hour of electricity generated by the utility-financed systems.

III. Cost Recovery by Utilities of Certain Distributed Solar Energy System Investments.

The Utilities and Transportation Commission (Commission) is authorized, upon request by an electrical company, to approve a tariff allowing the company to recover, from its ratepayers, the costs incurred in acquiring, installing, operating, and maintaining "cost-effective distributed solar energy systems" at the premises of retail electric customers.

"Cost-effective distributed solar energy system" means: a solar energy system with a generating capacity of not more than five kilowatts, when the meter holder is a residential retail electric customer, and 100 kilowatts, when the meter holder is a commercial retail electric customer; which at the time the system is placed in the rate base, is reasonably expected to generate energy that is less than or equal in cost to the cost of the "lowest reasonable cost eligible renewable resource," as determined by the utility's integrated resource plan.

This provision makes the following changes to the Commission's current practices:

- Shifts, from the utility to the Commission, the burden of proving that the company's proposed tariff filing would be fair, just, reasonable, and sufficient without customer contribution.
- Defines generation assets (distributed solar energy systems) as no longer "necessary and useful" once the company has recovered its costs under the tariff. As a result of this definition, the utility can transfer these assets without meeting the statutory requirement that the utility must demonstrate a net benefit to customers from the sale of the asset, before the asset can be transferred.
- Directs the Commission to establish a cost basis for a distributed solar energy system, considering the return on common equity and cost of debt incurred for the single asset, instead of following the current practice of establishing the return on common equity and cost of debt incurred for the utility as a whole.
- Changes the definition of cost effective used by the Commission in evaluating a resource choice.
- Requires the Commission to measure the cost-effectiveness of a solar energy system at the time it is placed in the rate base, instead of at the time the company makes a decision to purchase the solar energy system.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect on July 1, 2013.

Staff Summary of Public Testimony (Technology & Economic Development):

(In support) The current Renewable Energy Investment Cost Recovery Incentive Program (Program) helped attract a clean energy manufacturing sector to the state, but it has been underperforming, in terms of the difference between what the state has made available as credits and what is getting utilized. This legislation is intended to improve utilization of the tax credit and minimize bureaucracy. It will increase jobs for installers and manufacturers in the State of Washington.

The renewable energy sector has been growing in the state even during a "great recession," when every other sector except biotechnology has been in decline. The purpose is to create a solar manufacturing industry in the State of Washington. When the Columbia hydroelectric power system was built, it was the most expensive facility in the world in that marketplace. Sometimes a careful balance is required, between leaving the development of an industry to market forces, and paving the path for what is going to be the next big thing. The current administration of the tax credit by the Department of Revenue, with inconsistent rulings, has created instability, halting millions of dollars of product from being distributed. The move to the Washington State Housing Finance Commission (WSHFC), with decades of experience in leveraging federal incentives, dealing with tax credit structures in complex projects, and administering programs with different financing schemes, is a key step forward. The move to a Competitive Pool should also improve program implementation, and help open up solar technology to food banks, colleges, and others who have been unable to participate in the existing Community Solar programs.

(In support with concerns) The solar manufacturing and installation sector needs a program like this where the incentive payback is linked to when your system was installed, not when a government program expires. When it comes to job creation, Community Solar programs is not where the jobs come from. The original intent of Community Solar programs was to allow schools to have solar projects while investors can still get a return on the investment, but it is subject to federal security laws. True job creation does not come from the large installations but from the small residential installations. Community Solar projects are already eligible for other federal incentives. Encouraging aspects of the proposed legislation include the streamlining of paperwork, improvement of program administration, and the recognition that the primary job creator is in the fields, with installation of these systems. But predictability is key and must be considered when drafting changes to the incentive program, and it is better when a significant change is planned a year or more in advance, so there is adequate time to prepare. It is also important to make sure that enough credits are retained in Phase II to promote the full growth of the residential solar programs. The WSHFC is a self-funded organization so needs authority to charge a fee to cover its administrative costs.

(With concerns) Extending the current cost recovery program is an understandable goal since it will expire in 2020. From the perspective of public utility districts and rural electric cooperatives, any change from current voluntary participation to mandatory participation in the Program would be of concern. It is unclear how this ensures that five years down the line, a system can still get a 10-year incentive. If you move to 10-year contracts, it is unclear what obligation a utility has if the state stops funding the Program. There needs to be a comparable commitment from the state to reimburse the utilities, and provide security to

utilities that are required to sign that contract. In the current Program, utilities have a safety valve that every year, a utility can drop out if funding dries up. It is hoped that Community Solar programs can continue to exist and be successful. It is very popular out in the smaller, rural communities where people can band together and buy shares. On a technical note, the bill moves away from requiring the use of a utility-grade meter; these meters have proven to be an accurate way of gauging power generation, so it would be preferable to continue to provide for the use of them, even if alternative metering methods as well. The start date for incentive payments should be linked to when a meter is installed. The proposed legislation does not reflect an incentive rate that declines over time as the energy becomes more affordable, reflecting anticipated efficiencies in technology development and scale. The credit allocation formula and the "market correction factor" are making the Program harder to understand and explain, undermining predictability, and confusing customers.

(Opposed) None.

Staff Summary of Public Testimony (Finance):

(In support) This bill does not expand the fiscal scope of the program; however, it addresses some operational issues. The Department of Revenue did not want to continue to administer the program. The Commission is probably the best agency to address deal structures. There are two solar manufacturers that were not here before the passage of the original act. Washington is one of the top 10 to 15 states for solar energy related jobs. Very little of the program is being utilized. This bill makes changes that will hopefully lead to a higher utilization of the program. There is a second proposed substitute in the works that addresses lease arrangements, which has been an issue. It also addresses some of the trade issues. The proposed second substitute also addresses some issues regarding the administration of the program by the Commission. This bill is a job driver. The underlying statute has worked to create jobs. The Commission is a better fit to administer the program. The 10-year payments and the increased cap are good changes by creating stability. This program is one of the direct contributors to the great success of my business. This bill not only helps solar but green technology in general.

(With concerns) There are considerable concerns about the impact to businesses, customers, and taxpayers. There are several built-in cost drivers: the considerable increase in the cap, the extension of the program for another ten years, and the expansion of the program by the creation of an additional pool of projects.

(Opposed) None.

Persons Testifying (Technology & Economic Development): (In support) Representative Morris, prime sponsor; Kelly Samson, Hek Energy; Majken Ryherd, Silicon Energy; and Kim Herman, Housing Finance Commission.

(In support with concerns) Dever Kuni, South Sound Solar.

(With concerns) Dave Warren, Washington PUD Association; Kathleen Collins, PacifiCorp; Kent Lopez; Nancy Atwood and Jake Wade, Puget Sound Energy; and Victoria Lincoln, Association of Washington Cities.

Persons Testifying (Finance): (In support) Representative Morris, prime sponsor; Majken Ryherd, Silicon Energy; Jim Justin, Itek Energy; and Brian Heather, Solterra Systems.

(With concerns) Nancy Atwood, Puget Sound Energy.

Persons Signed In To Testify But Not Testifying (Technology & Economic Development): None.

Persons Signed In To Testify But Not Testifying (Finance): None.