

# HOUSE BILL REPORT

## ESHB 1589

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### As Passed Legislature

**Title:** An act relating to supporting Washington's clean energy economy and transitioning to a clean, affordable, and reliable energy future.

**Brief Description:** Supporting Washington's clean energy economy and transitioning to a clean, affordable, and reliable energy future.

**Sponsors:** House Committee on Environment & Energy (originally sponsored by Representatives Doglio, Fitzgibbon, Berry, Alvarado, Bateman, Ramel, Peterson, Lekanoff, Hackney, Macri and Kloba).

### Brief History:

#### Committee Activity:

Environment & Energy: 2/6/23, 2/13/23 [DPS].

#### Floor Activity:

Passed House: 3/6/23, 52-44.

Passed House: 1/22/24, 52-45.

Senate Amended.

Passed Senate: 3/1/24, 27-22.

House Concurred.

Passed House: 3/5/24, 50-45.

Passed Legislature.

### Brief Summary of Engrossed Substitute Bill

- Requires the Utilities and Transportation Commission (UTC) to adopt , by July 1, 2025, a consolidated planning process for a large combination utility that combines the gas and electric utility planning processes.
- Requires a large combination utility to file, by January 1, 2027, an integrated system plan that achieves the obligations of all plans consolidated into the integrated system plan, and that achieves additional specified obligations.

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

- Requires the UTC to establish by rule a cost test for emissions reduction measures to be used by large combination utilities for the purpose of determining the lowest reasonable cost of decarbonization and electrification measures in integrated system plans.
- Authorizes a large combination utility to seek a certificate of necessity from the UTC to construct a new nonemitting or renewable generation or transmission facility, to make a significant investment in existing facilities, or to enter into a power purchase agreement for the purchase of nonemitting or renewable electric energy.
- Authorizes a large combination utility to recover financing costs in base rates on construction work in progress for capital improvements prior to the assets being considered used and useful.
- Requires the UTC to approve, in connection with an approved integrated system plan, an accelerated depreciation schedule that depreciates all existing gas plants by January 1, 2050.
- Authorizes the UTC to approve the merger of the electric and gas rate bases of a large combination utility if the UTC finds that the proposal will result in a net benefit to customers of the large combination utility and if the merger includes reasonable rate protections for low-income natural gas and electric customers.
- Requires a large combination utility, when proposing electrification within an area in which a consumer-owned utility provides electrical service, to include a process for outreach to the consumer-owned utility.
- Requires, for any project in an integrated system plan with a cost of more than \$10 million, that the large combination utility certify to the UTC that any work associated with the project will be constructed in a way that includes community workforce agreements or project labor agreements, the payment of prevailing wages, and apprenticeship utilization requirements.

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## HOUSE COMMITTEE ON ENVIRONMENT & ENERGY

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 9 members: Representatives Doglio, Chair; Mena, Vice Chair; Berry, Duerr, Fey, Lekanoff, Ramel, Slatter and Street.

**Minority Report:** Do not pass. Signed by 6 members: Representatives Dye, Ranking Minority Member; Ybarra, Assistant Ranking Minority Member; Abbarno, Barnard, Couture and Goehner.

**Staff:** Robert Hatfield (786-7117).

**Background:**

Utilities and Transportation Commission.

The Utilities and Transportation Commission (UTC) is a three-member commission with broad authority to regulate the rates, services, and practices of a variety of businesses in the state, including four natural gas companies. The UTC must ensure rates charged by these companies are fair, just, reasonable, and sufficient.

Greenhouse Gas Emission Reduction Limits.

In 2020 the Legislature updated statewide greenhouse gas (GHG) emissions reduction limits to 45 percent below 1990 levels by 2030, 70 percent below 1990 levels by 2040, and 95 percent below 1990 levels, as well as net-zero emissions by 2050.

Clean Energy Transformation Act.

In 2019 the Legislature enacted the Clean Energy Transformation Act (CETA), which requires Washington's electric utilities to meet 100 percent of their retail electric load using non-emitting and renewable resources by January 1, 2045. Additionally, the CETA requires electric utilities to eliminate coal-fired resources from their allocation of electricity by December 31, 2025, and to make all retail sales of electricity GHG neutral by January 1, 2030.

Integrated Resource Plans.

All investor-owned and consumer-owned electric utilities in the state with more than 25,000 customers must develop integrated resource plans. An integrated resource plan must include a number of components, such as 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. Integrated resource plans must be updated every two years. Investor-owned utilities (IOUs) must submit their plans to the UTC.

Multiyear Rate Plan.

Every general rate case filing of a gas or electric utility before the UTC must include a proposal for a multiyear rate plan. The UTC may by order after an adjudicative proceeding, approve, approve with conditions, or reject, a multiyear rate plan proposal made by a utility, an alternative proposal made by one or more parties, or any combination of these. The UTC's consideration of a multiyear rate plan proposal is subject to the same standards as other related filings, including that it be in the public interest and that the rates be fair, just, reasonable, and sufficient.

Clean Energy Action Plan.

An IOU must adopt a 10-year clean energy action plan for implementing the CETA at the lowest reasonable cost and at an acceptable resource adequacy standard that identifies the specific actions to be taken by the IOU consistent with its long-range integrated resource

plan.

#### Climate Commitment Act.

In 2021 the Legislature passed the Climate Commitment Act (CCA) and directed the Department of Ecology (Ecology) to implement a cap-and-invest program to reduce GHG emissions consistent with the statewide statutory emissions limits.

Starting January 1, 2023, covered entities must either reduce their emissions or obtain allowances to cover any remaining emissions. The total number of allowances will decrease over time to meet statutory limits. Allowances can be obtained through quarterly auctions, or bought and sold on a secondary market. Some utilities and industries will be issued no-cost allowances. The cap and-invest-program must track, verify, and enforce compliance through the use of compliance instruments. A compliance instrument is an allowance or offset credit issued by Ecology or a trading program that has linked with Washington's cap and-invest-program. One compliance instrument is equal to one metric ton of carbon dioxide equivalent.

#### Utility regulatory fees.

A combination utility must pay to the UTC a regulatory fee equal to 0.1 percent of the first \$50,000 of gross operating revenue, plus 0.4 percent of any gross operating revenue in excess of \$50,000.

#### **Summary of Engrossed Substitute Bill:**

##### Integrated System Plan.

By July 1, 2025, the UTC must complete a rule-making proceeding to implement consolidated planning requirements for gas and electric services for large combination utilities. A large combination utility is an electrical company and gas company that serves more than 800,000 retail electric customers and 500,000 retail gas customers in Washington as of June 30, 2024.

The consolidated planning process must incorporate the elements of individual plans and targets prepared pursuant to multiple statutory obligations, including:

- the Energy Independence Act;
- the Clean Energy Transformation Act;
- gas company conservation targets;
- electric utility resource plans and clean energy action plans;
- transportation electrification plans;
- multi-year rate plans; and
- pipeline safety and replacement plans.

By January 1, 2027, large combination utilities must file an integrated system plan. The UTC must set a timeline for future integrated system plans, and they must be updated on a regular basis. Large combination utilities that file integrated system plans are no longer

required to file separate plans that are required in an integrated system plan. The statutorily required contents of any plan consolidated into an integrated system plan must be met by the integrated system plan.

The integrated system plan must, among other specified objectives:

- achieve the obligations of all plans filed under the integrated system plan;
- provide a range of forecasts of projected customer demand;
- include scenarios that achieve gas utility and electric utility emissions reductions equal to their proportional share of emissions reductions under the statewide GHG emissions reduction limits;
- include scenarios with emissions reduction targets for both gas and electric operations for each emission reduction period that account for interactions between gas and electric systems;
- achieve 2 percent of electric load annually with conservation and energy efficiency resources, unless the UTC finds a higher target is cost effective, however the UTC may accept a lower level of achievement if it determines that the requirement is neither technically nor commercially feasible;
- assess commercially available conservation and efficiency resources, including demand response and load management, to achieve the 2 percent conservation and energy efficiency target for the 20 year planning horizon;
- achieve annual demand response and demand flexibility equal to or greater than 10 percent of winter and summer peak electric demand, unless the UTC finds a higher target is cost effective;
- include low-income electrification programs;
- provide a comparative evaluation of supply side resources, delivery system resources, and conservation and efficiency resources using lowest reasonable cost as a criterion;
- include a 10-year clean energy action plan for implementing CETA at the lowest reasonable cost and at an acceptable resource adequacy standard;
- establish that, consistent with the CCA, a large combination utility has consigned to auction for the benefit of ratepayers the maximum permissible number of allowances and prioritize, first, revenues derived from the auction of allowances to programs that eliminate the cost burden for low-income ratepayers and, second, electrification programs benefitting residential and small commercial customers; and
- report on the progress toward implementing the recommendations in the previously filed integrated system plan.

When evaluating the lowest reasonable cost of decarbonization measures in an integrated system plan, large combination utilities must apply a risk reduction premium that accounts for the applicable allowance ceiling price pursuant to the CCA.

A large combination utility must consider the social cost of GHG emissions, determined by the UTC, when developing integrated resource plans and clean energy action plans. A large combination utility must incorporate the social cost of GHG emissions as a cost adder when evaluating and selecting conservation policies, programs, and targets; developing integrated

system plans and clean energy action plans; and evaluating and selecting intermediate-term and long-term resource options.

The UTC must establish, by rule, a cost test for emissions reduction measures achieved by large combination utilities to comply with state clean energy and climate policies. The cost test must be used for determining the lowest reasonable cost of decarbonization and electrification measures in integrated system plans at the portfolio level, and for any other purpose determined by UTC rules.

#### Integrated System Plans—Approval.

The UTC must approve, reject, or approve with conditions, an integrated system plan within 12 months of its filing. For good cause shown, the UTC may extend the time by 90 days for a decision on an integrated system plan filed on or before January 1, 2027. When determining whether to approve, reject, or approve a plan with conditions, the UTC must evaluate whether the plan is in the public interest. In doing so, the UTC must take into account the following factors, among others:

- the equitable distribution and prioritization of energy benefits and reduction of burdens to vulnerable populations, highlight-impacted communities, and overburdened communities;
- long-term and short-term public health, economic, and environmental benefits and the reduction of costs and risks;
- energy security and resiliency;
- whether the integrated system plan would achieve a proportional share of reductions in GHG emissions for each emissions reduction period on the gas and electric systems; and
- whether the integrated system plan would result in a reasonable cost to customers.

#### Accounting for Green House Gas Attributes.

Large combination utilities must work in good faith with other specified stakeholders to develop market structures and mechanisms that account for the GHG attributes of wholesale electricity generation when such electricity is sold into organized markets.

#### Certificate of Necessity.

A large combination utility may submit an application to the UTC seeking a certificate of necessity in order to:

- construct a new renewable or nonemitting electric generation or transmission facility;
- make a significant investment in an existing renewable or nonemitting electric generation or transmission facility; or
- enter into a power purchase agreement for the purchase of renewable or nonemitting electric energy or capacity for a period of five years or longer.

In order to qualify for a certificate of necessity, the construction project, investment, or purchase must:

- cost \$100 million or more;

- require the utility to begin incurring significant portions of these costs more than five years before the facility is estimated to be in service; and
- allocate all or a portion of the costs to retail customers in this state.

Applications for a certificate of necessity must be submitted in conjunction with a large combination utility's integrated system plan, but a large combination utility may submit an application outside of the integrated system plan process for a time-sensitive project.

A large combination utility submitting an application for a certificate of necessity may request one or more of the following:

- a certificate of necessity that the power to be supplied or transmitted as a result of the proposed construction, investment or purchase is needed;
- a certificate of necessity that the size, fuel type, and other design characteristics of the existing or proposed electrical generation or transmission facility or the terms of the power purchase agreement represent the most appropriate and reasonable means of meeting that power need;
- a certificate of necessity that the estimated purchase or capital costs of and the financing plan for the existing or proposed electric generation or transmission facility, including costs of siting and licensing a new facility or the costs of power from the facility, are reasonable; or
- a request to (1) recognize, accrue, and defer the allowance for funds used during construction, and (2) recover financing interest costs in base rates on construction work in progress for capital improvements approved prior to the assets being considered used and useful.

The UTC may approve, reject, or approve with conditions an application if it is in the public interest and the construction, investment, or purchase complies with the UTC's administrative rules governing electric resource procurement. In a certificate of necessity, the UTC may specify the estimated costs for construction or investment in a facility, the estimated price for a purchase of an existing facility or power pursuant to a power purchase agreement.

If the UTC denies any relief requested by a large combination utility the utility may withdraw its application for a certificate of necessity or proceed with the proposed construction, purchase, investment, or power purchase agreement under its ordinary course of business without a certificate of necessity and the assurance granted under a certificate of necessity.

The large combination utility must file reports to the UTC regarding the status of any project granted a certificate of necessity, including updates about costs and schedule at intervals determined by the UTC.

If the assumptions underlying an approved certificate of necessity materially change, a large combination utility must request, or the UTC or potential intervenor on its own motion may



initiate, a proceeding to review whether it is reasonable to complete an unfinished project with a certificate of necessity. In the order approving the certificate of necessity, the UTC must list the assumptions underlying an approved certificate of necessity.

If the UTC finds that the completion of the project is no longer reasonable, it may modify or cancel approval of the certificate of necessity. The UTC may also allow recovery of reasonable costs already incurred or contracted for and limit future cost recovery to those that could not be reasonably avoided. The existing authority of the UTC to ascertain and determine the fair value for rate-making purposes of the property of any large combination utility is not amended, modified, or repealed.

A supplier of electric generation that seeks to provide electric generation energy or capacity resources to a large combination utility may submit a written proposal to the UTC as an alternative to the construction, investment, or purchase proposed under a certificate of necessity.

The entity submitting an alternative proposal to a certificate of necessity has standing to intervene and request reasonable discovery in the contested case proceeding. The UTC may consider the cost of the alternative proposal and specified qualifications of the submitting entity. However, this provision does not authorize the UTC to order or otherwise require a large combination utility to adopt any alternative proposal submitted.

#### Depreciation Schedules and Consolidated Energy Rate Base.

In any multiyear rate plan filed by a large combination utility, the combination utility must include an updated depreciation study that reduces the gas rate base consistent with an approved integrated system plan, and the UTC may adopt depreciation schedules that accelerate cost recovery and reduce rate base for any gas plant. In any multiyear rate plan, the UTC must approve a depreciation schedule that depreciates all gas plants in service as of July 1, 2024, no later than January 1, 2050. When considering future multiyear rate plans, the UTC may adjust depreciation schedules for gas plants to address affordability, as long as all gas plants in service as of July 1, 2024, are fully depreciated by 2050.

In any multiyear rate plan proposed by a combination utility, the utility may propose a merger of the regulated gas and electric operation into a single rate base. The UTC may approve the merger of electric and gas rate bases, if it finds the proposal will result in a net benefit to customers of the combination utility.

For a combination utility that has merged gas and electricity rate bases, the utility must monetize benefits received from any applicable federal and state tax and other incentives for the benefit of customers. These benefits must be separately accounted for and amortized on a schedule designed only to mitigate the rate impacts to customers after the rate bases are combined.

#### Rebates, Incentives, and Education.



Beginning January 1, 2025, no large combination utility may offer any form of rebate, incentive, or other inducement to residential gas customers to purchase any natural gas appliance or equipment. Until January 1, 2031, this requirement does not apply to:

- electric heat pumps that include natural gas backups; or
- commercial and industrial customers.

Additionally, beginning January 1, 2031, a large combination utility may not include electric heat pumps with gas backups as part of its electrification programs.

By November 1, 2025, a large combination utility must initiate and maintain an effort to educate its ratepayers about the benefits of electrification and the availability of rebates, incentives, or other inducements to purchase energy efficient electric appliances and equipment.

#### Geographically Targeted Electrification.

Geographically targeted electrification is the transition of a portion of large combination utility gas customers with an intent to electrify heating loads of these customers and, in conjunction, to reduce capital and operational costs of gas operations.

When an integrated system plan proposes geographically targeted electrification of all or a portion of a large combination utility's service area and one or more consumer-owned utilities provide electric service to the same service area, the integrated system plan must include a process for outreach to all of these consumer-owned utilities.

Consumer-owned utilities are encouraged to:

- work with large combination utilities providing gas service within their service areas to identify opportunities for electrification;
- account for the costs of GHG emissions, set total energy savings and GHG emissions reduction goals, and develop and implement electrification programs in collaboration with combination utilities providing service; and
- include an electrification plan or transportation electrification program as part of collaboration with combination utilities.

#### Project Labor Agreements.

For any project in an integrated system plan that is part of a competitive solicitation and costs more than \$10 million, the large combination utility must certify to the UTC that any work on the project will include community workforce agreements or project labor agreements, the payment of area standard prevailing wages, and apprenticeship utilization requirements.

The project labor agreement provisions do not supersede current electrician licensing laws or the Washington Industrial Safety and Health Act.

#### Rulemaking.

The UTC may adopt rules to ensure the proper implementation and enforcement of the act.

Utility Regulatory Fees.

A combination utility must pay to the UTC a regulatory fee equal to 0.1 percent of the first \$50,000 of gross operating revenue, plus 0.5 percent of any gross operating revenue in excess of \$50,000.

Title.

The act may be known and cited as the Washington Decarbonization Act for Large Combination Utilities.

Severability Clause.

The act contains a severability clause.

Emergency Clause.

The act contains an emergency clause and takes effect immediately.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill contains an emergency clause and takes effect immediately.

**Staff Summary of Public Testimony:**

(In support) This bill represents a complementary policy to the Clean Energy Transformation Act and the Climate Commitment Act, both of which set aggressive decarbonization goals for gas and electric utilities. It will be a steep hill to climb to achieve those goals. This bill provides the right tools for Puget Sound Energy (PSE) to achieve those goals in the most cost effective way possible. The bill ensures PSE will have a balanced portfolio between purchased and owned resources. The bill would allow PSE to equitably distribute the benefits and burdens of electrification and decarbonization. It used to be that if the rates for everyone were the same, that was considered equitable, but some of those past assumptions are being reexamined and more equitable ways of approaching rates are being considered.

Climate change disproportionately affects low-income and BIPOC communities. The bill is an important step in reducing natural gas expansion. Natural gas in the residential sector is currently responsible for almost half of Seattle's current carbon emissions. Electrification will cause a load increase, so it is important to work to prepare the electrical grid.

The bill prioritizes creation of family wage jobs through the use of project labor agreements and community workforce agreements.

It is important to transition to a clean energy economy, and businesses must be involved in that transition.

Buildings represent the fastest-growing sector of greenhouse gas emissions in Washington. The bill provides a pathway for the transition to clean energy. Recently adopted building codes require heat pumps. There is support for limiting the expansion of natural gas infrastructure. Converting from natural gas to electricity is a challenge. Some cities are promoting heat pump conversions in a number of ways, including through funding and streamlined permitting.

This bill is bold, complicated, and necessary. As natural gas sales decline, gas utilities will be unable to survive on their gas revenues. The bill provides a merger of the natural gas and electric rate bases. One policy question to address is whether the natural gas rate base should be shifted to other consumers of PSE, or whether the rate base should be shifted to the electric utilities that provide electricity to areas that get their natural gas, but not their electricity, from PSE.

The bill provides a pathway for incentivizing electric transmission and generation facilities. There is important labor and workforce language in the bill. The bill provides both certainty and opportunity.

(Opposed) There need to be some changes to make the bill workable. There are significant consumer protection concerns with the bill. There is no meaningful cost protection for customers related to the decarbonization and electrification plans. Nothing in the bill limits what PSE can spend on these plans, and cost control measures are very important to consumers. The requirement that PSE get 60 percent of its electricity from resources that PSE owns will increase costs to customers. Also, requiring a rate of return to PSE for its power purchase agreements is a windfall to PSE.

There is strong opposition for the anti-competitive provisions regarding electricity in the bill. There is intense interest in how to decarbonize the power structure. Carving out 60 percent of the clean energy market to be owned by one utility sacrifices the integrity of the whole sector in order to keep one utility whole. The bill gives PSE a profit center on each contract it enters into, with no benefit to customers. The bill undermines the premise of competition. Utilities received major advantages in the Inflation Reduction Act, including making it easier to monetize federal tax credits.

(Other) Natural gas is a fossil fuel, and decarbonizing a gas utility is a challenging endeavor. There is much work to be done on the bill, and the devil is in the details. It is important that the bill allow the Utilities and Transportation Commission the authority to manage costs and ensure greenhouse gas reductions. If this bill is done right, it could provide a national model for transitioning utilities to electricity. Natural gas prices are one of the largest drivers of utility rates, and gas prices have been increasing significantly recently. It is important to understand the low-income provisions in the bill.

There need to be mandatory emissions reduction targets in the bill.

The bill should have language that calls for a reporting element with regard to labor usage.

Avista has a company goal of being carbon-neutral in natural gas by 2045. Full electrification for Avista would require doubling its current electrical consumption. Gas backup heat pumps are helpful. It is important to maintain the resilience and reliability of the electrical grid while advancing decarbonization goals in a cost sensitive way.

There is a recognition that there is a commitment to have the bill apply only to PSE, and no one else. The provisions in the bill do not work for a gas-only utility. There is a need to address how to handle rates in those areas where customers get their electricity from PSE but their gas from someone else. It is important to make sure the state does not create overburdened customers as a result of this bill.

It is important to ensure that labor standards and safety standards are met.

Hospitals are required to maintain redundant power services, so there needs to be a slight change in the wording of the bill. Hospitals have to have access to reliable power. As currently written, hospitals would not be able to access new gas connections. New hospitals, or current hospital in new locations, would need to have access to natural gas connections.

It is important to think through what it looks like to decarbonize the energy sector. There are both climate impacts and health impacts to burning natural gas inside the home. It is critical to begin planning now to make sure the transition to clean energy is affordable for all customers. The mechanisms in the bill are new, and it is important to continue to talk through their implementation.

There is support for the intent of the bill. One concern is that the bill provides certainty to the utility company, but there is a need to make changes to provide assurances to customers, including emissions reduction and cost control. The bill does not address protections for low-income customers, which is important to do.

The transition to clean energy needs to consider impacts on people, including people who manage the energy delivery system.

**Persons Testifying:** (In support) Representative Beth Doglio, prime sponsor; Mendy Droke, Seattle City Light; Sam Hem, Northwest Regional Council Sheet Metal, Air, Rail and Transportation Workers Local 66; Ken Johnson, Puget Sound Energy; Jim Lazar, Regulatory Assistance Project; Matthew Hepner, Certified Electrical Workers of Washington; Donny Donovan, International Association of Machinists and Aerospace Workers 751; and Jay Arnold, City of Kirkland.

(Opposed) Sommer Moser, Alliance of Western Energy Consumers; and Spencer Gray, Northwest and Intermountain Power Producers Coalition.

(Other) John Worthington; Anna Lising, Office of the Governor; Dave Danner, Utilities and Transportation Commission; Jennifer Ziegler, National Construction Alliance; Zosia Stanley, Washington State Hospital Association; Kurt Swanson, Washington State Association Plumbers and Pipefitters; Charlie Brown, Northwest Natural and Cascade Natural Gas; Christine Reid, International Brotherhood of Electrical Workers 77; Lauren McCloy, Northwest Energy Coalition; Kelly Hall, Climate Solutions; and John Rothlin, Avista.

**Persons Signed In To Testify But Not Testifying:** None.