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AND THE LAW OF PUBLIC UTILITIES

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Final Report of
A Study of the Impacts of Regulations
Affecting the Acceptance of
Integrated Community Energy Systems

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ABSTRACT

This report contains a detailed description of the laws and programs of the State of Washington governing the regulation of public energy utilities, the siting of energy generating and transmission facilities, the municipal franchising of public energy utilities, and the prescription of rates to be charged by utilities including attendant problems of cost allocations, rate base and operating expense determinations and rate of return allowances. These laws and programs are analyzed to identify impediments which they may present to the implementation of Integrated Community Energy Systems (ICES). This report is one of fifty-one separate volumes which describe such regulatory programs at the federal level and in each state as background to the report entitled "Community Energy Systems and the Law of Public Utilities -- Volume One: An Overview." This report also contains a summary of a strategy described in Volume One -- An Overview for overcoming these impediments by working within the existing regulatory framework and by making changes in the regulatory programs to enhance the likelihood of ICES implementation.

PREFACE

One response to current concerns about the adequacy of the nation's energy supplies, in addition to reducing consumption of energy, is to make more efficient use of existing energy resources. The United States Department of Energy (DOE) has funded research, development and demonstration programs to determine the feasibility of applying proven cogeneration technologies in centralized energy systems, known as Integrated Community Energy Systems (ICES), to provide heating, cooling and electrical services to entire communities in an energy conserving and economic manner.

The relevant "community" which will be appropriate for ICES development will typically consist of a combination of existing or potential energy "wasters" -- i.e., installations with large energy conversion facilities which, when operated in a conventional manner, exhaust usable amounts of waste heat or mechanical energy -- and existing and potential energy users -- i.e., industrial, commercial, institutional or residential structures which obtain electricity and gas from a traditional central utility and convert part of it on site to space heating and cooling purposes.

In most current applications, energy conversion facilities burn fuels such as coal, oil or natural gas to produce a

single energy stream such as process steam or electricity for various industrial processes or for sale to other parties. In the conversion process, substantial amounts of energy may be wasted. For example, it has been estimated that from 60 to 75 percent of the potential energy available in fuel burned to generate electricity is lost in the process of generating and delivering the electricity.

The technology exists, however, to produce and utilize more than one energy stream from most energy conversion processes so that the input of a given amount of fuel could lead to the production of far more usable energy than is generally true in most steam production processes. This technology is the foundation of the ICES concept. Current examples of the technology can be found on university campuses, industrial or hospital complexes and other developments where a central power plant provides not only electricity but also thermal energy to the relevant community.

It is generally assumed by DOE that ICES will be designed to produce sufficient thermal energy to meet all the demands of their communities and that they will be interconnected with existing electric utility grids. Through such an interconnection, an ICES would be able to purchase electricity when its community's need for electricity exceeds the amount which could be produced from the level of operations needed to meet the community's thermal needs. In addition, when operations to meet thermal needs result in generation of more electricity than

necessary for the ICES community, the ICES would be able to sell excess electricity to the grid.

ICES may take a variety of forms, from a single owner-user, such as a large industrial complex or university campus, where all energy generated is used by the owner without sales to other customers, to a large residential community in which central power plant produces heat and electricity which is sold at retail to residents of the community. Since successful operation of an ICES presupposes that the ICES will be able to use or sell all energy produced, it can be anticipated that all ICES will at some point seek to sell energy to customers or to the electric utility grid from which the electricity will be sold to customers. By their very nature ICES are likely to be classified as public utilities under the laws of many, or even all, states.

Ross, Hardies, O'Keefe, Babcock & Parsons has undertaken a contract with the Department of Energy to identify impediments to the implementation of the ICES concept found in existing institutional structures established to regulate the construction and operation of public utilities. These institutional structures have been developed in light of policy decisions which have determined that the most effective means of providing utility services to the public is by means of regulated monopolies serving areas large enough to permit exploitation of economies of scale while avoiding wasteful duplication of production and delivery facilities. These existing institutional structures have led to an

energy delivery system characterized by the construction and operation of large central power plants, in many cases some distance from the principal population centers being served.

In contrast, effective implementation of ICES depends to some extent upon the concept of small scale operations supplying a limited market in an area which may be served by other suppliers of utility services. ICES may in many instances involve both existing regulated utilities and a variety of non-utility energy producers and consumers who have not traditionally been subject to public utility type regulation. Implementation of the ICES concept will also require a variety of non-traditional relationships between existing regulated utilities and non-regulated energy producers and consumers.

The purpose of this report is to generally describe the existing scheme of public utility regulation as it is likely to relate to the development and operation of an ICES, the construction of ICES facilities and the determination of relevant cost of service, rate of return and rate structure for the sale and purchase of energy by an ICES. Attention is given to the problems of the entry of an ICES into an energy market which has traditionally been characterized by a form of regulated monopoly where only one utility has been authorized to provide a particular service in a given area.

This report is one of a series of reports covering the law of each of the 50 states and the federal government and should be read in conjunction with Volume One in this series entitled Community Energy Systems and the Law of Public Utilities: An Overview. That volume provides a national overview of the regulatory programs described in detail for the particular state covered by this report. It also provides an analysis of the impediments to effective implementation of the ICES concept and a series of recommendations for responding to those impediments. In many jurisdictions legal issues similar to those likely to arise in the implementation of the ICES concept have not previously been faced. Thus, this series of reports cannot give definitive guidance as to what all of the answers are with respect to all issues which may face ICES implementation. However, by having an understanding of the issues which may arise in the course of an effort to implement ICES, an ICES developer will be better equipped to seek solutions.

Ross, Hardies, O'Keefe, Babcock & Parsons has been assisted in this study by Professor Edmund Kitch, Professor of Law at the University of Chicago Law School; Deloitte, Haskins & Sells, independent public accountants; and Hittman Associates, Inc., engineering consultants.

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We wish to acknowledge the efforts of numerous individuals who have assisted in the preparation of the series of reports which make up the Study of the Impacts of Regulations Affecting the Acceptance of ICES. A number of lawyers and paralegal personnel of Ross, Hardies, have assisted in the research, writing, critiquing, rewriting, proofreading and other efforts including Drew Kaplan; Linda Arbetman; Cheryl K. Hachman; Barbara L. Ross; Joel F. Bonder; Sally H. Newton; Susan N. Stearns; Richard F. Babcock; Donald W. Graves; Theda C. Snyder; Patricia J. Crowe; Susan E. Merritt; Eileen A. Muench; Elizabeth West; Catherine B. Lipscomb; Margaret R. Hessler; and Elizabeth Walter.

Preparation of reports covering regulatory programs in every state has taken considerable research effort and we are grateful to a group of law students who spent not only countless hours in libraries, but also a great deal of time on telephones contacting public officials around the country to secure information about utility regulatory programs. Among the students were Marchall Seeder; Carl Anderson; Locke E. Bowman, III; James G. Bullard; Bruce W. Dewald; Norman B. Julius; Bruce S. Klafter; Ruth B. Kleiman; Suzanne Metzel; Terrence J. Molinari; Alison Moss; Rose M. Urban; Garth D. Wilson; Linda Yi; Shell Bleiweiss and Neal Heriaud.

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CHAPTER 1
EXECUTIVE SUMMARY

I. REGULATION OF PUBLIC UTILITIES

The authority to regulate utilities in Washington is vested in the Utilities and Transportation Commission (Commission), which is comprised of three members appointed by the Governor, with consent of the senate to serve for terms of six years. Municipalities are given a limited role in the regulation of public utilities. In general, municipalities retain authority to make and enforce orders regarding rates, services, and regulations affecting any telephone line, gas plant, electrical plant, or water system owned or operated by the municipality.

The Commission exercises regulatory authority over public utilities, which are defined by statute to include companies providing, among other things, electrical, gas, irrigation, telegraph, telephone and water services. The Commission does not, however, regulate heating, steam, refrigeration or sewer services. The Commission regulates direct and indirect sales to the general public. Rural electric cooperatives are thus not subject to Commission regulation because they serve only their members, and not the general public. The production of energy for strictly private use is also exempt from regulation. For a water system to be subject to Commission jurisdiction, it must serve at least 60 customers. However, there are no comparable quantitative figures for other types of utility service. Cogeneration

facilities employed for the generation of electricity for private use (or use by tenants) or for sale to electric companies or governmental agencies engaged in the sale of such energy, are also exempt from Commission regulation.

The Commission is authorized by statute to regulate, in the public interest, the rates, services, facilities and practices of all public utilities. More specifically, it is empowered to regulate rates for sales, capitalization, issuance of securities, systems of accounts, rates for depreciation, mergers and consolidations, affiliate transactions, agreements, transfers, abandonments, and standards of service. The Commission does not, however, regulate the construction or siting of new electrical plants or expansion of existing plants, nor the extension of electrical service to new customers.

Certain tax incentives are available to promote the development of cogeneration facilities. This program is administered by the Department of Revenue in conjunction with the Energy Office.

Certificates of public convenience and necessity must be obtained by gas companies prior to commencing operations. The Commission also has authority to prescribe the exchange area boundaries for telephone companies. However, the Commission is not empowered to issue certificates or prescribe boundaries for electric companies. The Commission has no apparent policy regarding competition.

Service area disputes are generally prevented by a statute which provides for voluntary service area agreements

between privately owned electric utilities or electric co-operatives which are subsequently ratified and made binding by the Commission.

Public utilities may abandon service only upon complying with the Commission's notice requirements and upon demonstrating certain circumstances enumerated in the Commission's regulations.

A public utility may petition for a rehearing of a Commission order or may apply for a writ of review of the order by the Superior Court of Thurston County. Review of the Commission's decision is on the record. Further appeal may be taken to the State Supreme Court.

II. SITING ENERGY FACILITIES

Standards for siting of energy facilities in Washington are provided in the Washington statutes and in Title 463 of the Administrative Code. The Siting Act created the Energy Facility Site Evaluation Council (Council), the chairman of which is appointed by the Governor with the advice and consent of the senate. The Council makes recommendations to the governor regarding applications for site certification. These recommendations, once ratified, totally preempt the siting powers of other state and local agencies.

The Council has jurisdiction over the siting of energy facilities, meaning energy plant or transmission facilities. The form of ownership of a utility does not affect Council jurisdiction. The Council has jurisdiction over preparation for new construction, replacement of existing facilities, and extension

of existing facilities, as well as monitoring the effects arising therefrom. The Council also ensures compliance with the National Pollution Discharge Elimination System Permit Program and the State Environmental Policy Act.

The administrative regulations of the state outline the requirements of applications for site certification. Local and state authorities must be notified by the Council of site proposals. The Council must also conduct a public hearing, at which time it must determine whether the proposed site is consistent with land use plans and zoning ordinances. If inconsistent, the Council will stay consideration of the application in order to permit the applicant to negotiate with local authorities. If negotiations fail, the Council must hold a contested case hearing.

The Siting Act provides that rejection of an application for a certificate is final. Judicial review, however, is available to any aggrieved party. Appeal is made to a district court and is confined to the record.

In passing on a siting application, the Council considers the public need for the facility and the environmental impact of the proposed facility. The Council also considers whether the applicant has complied with local land use plans and zoning ordinances.

Only power plants meeting the 250,000 kilowatt minimum requirement fall under the Council's jurisdiction. Other plants have their applications approved under the Environmental Coordination Procedures Act, with the Department of Ecology co-

ordinating the application process through state agencies. Among the agencies issuing permits under the Coordination Act are the Department of Ecology, the local planning authorities, the Department of Commerce and Economic Development, the Department of Natural Resources, and the Interagency Committee for Outdoor Recreation. The Coordination Act also provides that all certificates must comply with the Shoreline Management Act.

III. FRANCHISING OF PUBLIC UTILITIES

The authority to grant franchises for the use of public streets and highways in connection with providing utility service in Washington is vested by statute in municipalities, counties, and the State Highway Commission. The procedure for granting franchises and the type of grant awarded differ with each class of granting authority. Cities are divided into first, second, third and fourth classes. In addition, there are specific provisions for optional forms of local government. Special provisions affect the electric and street railroad franchises in each class of city. Pipeline and wire line franchises upon county roads are granted by county governments. The State Highway Commission controls franchises upon state highways.

Franchises may not be granted for purely private purposes. Second class cities may only grant franchises to railroad or other public service purposes. A certificate of public convenience and necessity is not a prerequisite to obtaining a franchise. However, there are no other pertinent

criteria or franchise qualifications delineated in the Washington statutes or case law.

While there are no judicial decisions regarding the maximum duration of a franchise, it is doubtful that a perpetual franchise can be granted in Washington. The statutes do not enumerate conditions that will result in the automatic surrender of a franchise, although a franchise was forfeited by a grantee's failure to perform the terms stipulated in a bond it had executed in accepting the grant. Grants of exclusive franchise privileges are expressly prohibited by statutes applying to second class cities, counties, and the Commission. The other applicable franchising statutes are silent on the issue of exclusivity.

IV. UTILITY RATE REGULATION

The statutes of Washington vest authority to regulate rates of public utilities in the Commission. The Commission has rate jurisdiction over investor-owned utilities, but not cooperative or publicly-owned utilities. The Commission prescribes the National Association of Regulatory Utility Commissioners system of accounts for electric and gas utilities.

The Commission may schedule hearings on the reasonableness of existing rates or proposed changes in rates, and pending a hearing may suspend the effective date of proposed rates for a period of up to ten months.

In determining a utility's rate base, the Commission

uses a historical test year and a fair value method of valuation. The Commission includes only "used and useful" utility property in the rate base, and traditionally, has excluded construction work in progress. Recently, however, the Commission has included construction work in progress for major long-term projects related to power production facilities. The Commission has not prescribed any particular method of rate base allocation for different services provided by a single facility.

The Commission has not stated a general test for what expenses may be included in the cost of service, although it does use as a starting point the revenues and expenses recorded on a company's books. The Commission does, however, examine expenditures to determine their propriety and reasonableness as an expense item. The Commission has also not specified any particular method of allocation of joint expenses.

The Commission allows a utility to normalize tax benefits where it has been barred from requiring flow-through treatment of depreciation under the federal tax laws. Otherwise, the Commission prefers the flow-through method. The Commission treats investment tax credits similarly.

In determining the rate of return that a utility may be allowed, the Commission uses the discounted cash flow method. The Commission has not enunciated any risk factors which would justify awarding a higher than normal rate of return, although it has on occasion considered short-term market fluctuations. The Commission has not made adjust-

ments in utilities' return on equity to serve as an incentive.

The Commission has given little indication as to what criteria it uses to set rates to customers, although it has recently made moves to a more flattened rate structure in an effort to promote energy conservation. Lifeline rates are not required under the statutes of Washington.

The Commission has authority to control the issuance of securities by utilities. However, there do not appear to be any reported cases delineating standards applied in determining whether to approve issuances.

CHAPTER 2

REGULATION OF PUBLIC UTILITIES IN WASHINGTON

I. PUBLIC AGENCIES WHICH REGULATE PUBLIC UTILITIES

The Washington State Constitution grants authority to the legislature to regulate railroads and other common carriers as well as telegraph and telephone companies in the state.^{1/} No section of the constitution expressly provides for the regulation of electric, gas, water or heating utilities.

The authority to regulate public utilities is vested generally in the Utilities and Transportation Commission (Commission), formerly designated as the Public Service Commission.^{2/} The Commission is composed of three members appointed by the governor, with the consent of the senate.^{3/} The term of office for commissioners is six years.^{4/}

Recently enacted legislation provides for the implementation of tax incentives to encourage the development of cogeneration facilities in the state.^{5/} This plan is to be administered by the Department of Revenue in conjunction with the Energy Office.^{6/}

II. JURISDICTION OF THE COMMISSION

The services regulated by the Commission are described in the general powers provision of the Public Utilities Act. The Commission is required to:

Regulate in the public interest, as provided by the public service laws, the rates, services, facilities, and practices of all persons engaging within this state in the business of supplying any utility service or commodity to the public for compensation, and related activities; including, but not limited to, electrical companies, gas companies, irrigation companies, telegraph companies, telephone companies, and water companies.

In addition, the Commission is generally required to exercise the powers and perform the duties required under Title 81 of the Washington statutes and to make such rules and regulations as may be necessary to carry out its powers and duties. Electrical, water and gas services, among others, are expressly subject to regulation.^{8/} Despite the broad phrase "including, but not limited to. . .," the Commission does not exercise jurisdiction over heating, steam refrigeration, or sewer services.^{9/}

The Washington statutes limit the regulatory role of the Commission with respect to telephone, gas or electric plant or water systems owned and operated by any city or town. The Commission is denied authority:

[T]o make or enforce any order affecting rates, tolls, rental, contracts or charges or service rendered, or the adequacy or sufficiency of the facilities, equipment, instrumentalities or buildings, or the reasonableness of rules or regulations made, furnished, used, supplied or in force affecting any telephone line, gas plant, electrical plant or water system owned and operated by any telephone, line, electrical plant or water system owned and operated by any city or town. 11/

Except for this express limitation on the commission's regula-

tory powers, all other provisions in the Utilities Act apply to public utilities owned by a city or town.^{11/}

The utility functions subject to regulation include the transmission, distribution and sale of natural gas, the manufacture, transmission, distribution and sale of other types of gas, the generation, transmission, distribution and sale of electricity and the storage, distribution, sale or diversion of water.^{12/}

There must be a sale for a function to be subject to jurisdiction. The Commission has general regulatory power over all persons in "the business of supplying any utility service or commodity to the public for compensation."^{13/} The definition of "electric plant" and "water system" use the words "for hire."^{14/}

Sales directly to the public are clearly jurisdictional. The status of indirect sales is less definite. However, the Commission appears to be authorized by statute to regulate indirect sales as well:

Every gas, water or electrical company owning, operating or managing a plant or system for the distribution and sale of gas, water or electricity to the public for hire shall be and be held to be a public service company as to such plant or system and as to all gas, water or electricity distributed or furnished therefrom, whether such gas, water or electricity be sold wholesale or retail or be distributed wholly to the general public or in part as surplus gas, water or electricity to manufacturing or industrial concerns or to other public service companies or municipalities for redistribution. ^{15/}

This statutory provision indicates that both direct and indirect sales by a jurisdictional utility will be subject to Commission regulation. In Dept. of Public Works v. West Coast Power Co.,^{16/} the Commission held that wholesale electric power was subject to regulation. The case involved two logging companies that jointly built a power plant for the purpose of furnishing electricity only to themselves for use in their mills at Shelton, Washington. Upon discovering they had a large surplus of power, the joint owners made a series of contracts with another pulp mill and with no less than three electric utilities for the provision of electric energy.^{17/} The result of these contracts was that over seventy-five percent of the electricity generated by the loggers was sold to others.^{18/} Rejecting the logger's contention that their wholesale power contract with the West Coast Power Company was not subject to regulation, the Commission declared:

It seems to the Board that if the jurisdiction of the Department is to be made effective, it must extend to every phase of the furnishing of public service, including (in the case of electrical service) both generation and distribution. If this is not the case, the Department's jurisdiction can be escaped and the public authority mocked by the mere device of creating separate legal entities to cover successive steps in the process of furnishing public service. The contention on the part of the joint owners that they are engaged in the production of logs and lumber and never intended to and do not want to be engaged in the furnishing of public service does not alter the fact that they are engaged in the furnishing of such service. That fact

and not their declaration and desire determines their status.^{19/}

Despite the statutory authority and this administrative precedent, the Commission nevertheless does not generally regulate electric sales except to ultimate consumers, according to staff counsel.^{20/}

The Public Utilities Act requires that utility service be furnished to the "public."^{21/} Another provision requires that:

Every gas company, electrical company or water company, engaged in the sale and distribution of gas, electricity or water, shall, upon reasonable notice, furnish to all persons and corporations who may apply therefor and be reasonably entitled thereto, suitable facilities for furnishing and furnish all available gas, electricity and water as demanded.^{22/}

The statute does not define what constitutes "public." However, the Washington Supreme Court discussed this issue in Clark v. Olson.^{23/} In this case, the defendant operated a water system serving ten homes which he had built and sold and nine other neighboring homes. All customers were provided with water service for a nominal charge. The plaintiffs filed suit when defendant refused to allow them to tap into his system. The trial court held for plaintiff, on the ground that defendant operated a public utility and was obligated to serve all who requested service. The supreme court reversed reasoning that the defendant had not held himself out as willing to serve the public, but, rather, offered water "as an accommodation."

Rural electric cooperatives are not subject to Commission regulation because they serve their members only, and not the general public. In Inland Empire Rural Electrification, Inc. v. Dep't of Public Service,^{24/} the court reasoned that:

A corporation becomes a public service corporation, subject to regulation by the department of public service, only when, and to the extent that, its business is dedicated or devoted to a public use. The test to be applied is whether or not the corporation holds itself out, expressly or impliedly, to supply its service or product for use either by the public as a class or by that portion of it that can be served by the utility, or whether, on the contrary, it merely offers to serve only particular individuals of its own selection. 25/

The court found that the electric cooperative involved had strictly adhered to the legal requirements of cooperative corporations in the state of Washington, concluding that:

It does not have the character of an independent corporation engaged in business for profit to itself at the expense of a consuming public which has no voice in the management of its affairs and no interest in the financial returns. Its members do not stand in the relation of members of the public needing the protection of the public service commission in the matter of rates and service supplied by an independent corporation.

On the contrary, it functions entirely on a cooperative basis, typifying an arrangement under and through which the users of a particular service and the consumers of a particular product operate the facilities which they themselves own. The service, which is supplied only to

members, is at cost, since surplus receipts are returned ratably according to the amount of each member's consumption. There is complete identity of interest between the corporate agency supplying the service and the persons who are being served. It is a league of individuals associated together in corporate form for the sole purpose of producing and procuring for themselves a needed service at cost. In short, so far as the record before us indicates, it is not a public service corporation. 26/

In Sunset Shingle Co. v. Northwest Electric & Water Works, 27/ the court was called upon to construe the meaning of the term "public." This case involved an action arising from a breach of contract between a mill and a privately owned utility. For several years the mill had operated its own auxiliary steam plant for supplying electricity for its machinery and lighting and steam for its dry kilns. 28/ Desiring better service, the mill entered a contract with a local utility whereby the utility received a site for a new plant and waste from the mill as fuel in exchange for furnishing steam heat and electricity to the mill. 29/ The utility also promised to make any needed repairs of the mill's machinery. 30/ The new plant was built and put into service, but the mill alleged that the utility failed to furnish electricity and steam heat in the full measure required by the terms of the contract. 31/ It appeared that the utility diverted power generated by the new plant to supply its other customers in the town. 32/ At trial the utility raised the affirmative defense that the mill contract was void. 33/ The utility argued that it was a public service

corporation, that the contract in question was for the rendering of a public service, and that the contract was an unlawful discrimination in favor of the mill as against the utility's public service customers, in violation of the public service statutes.^{34/}

Reversing the trial court decision in favor of the utility, the court recognized that not all contracts made by public utilities were necessarily public service contracts:

. . .[I]t does not follow that every act and thing done by respondent, even though it be in a sense service rendered to a person or corporation in compliance with the terms of some contract made by it with such person or corporation, is a public service subject to the regulatory provisions of our public service statutes. In controversies such as this the question is not so much as to whether or not the corporation is a public service corporation--a general term often of very loose application when discussing public service problems--but whether or not the service in question is a public service. ^{35/}

The court went on to conclude that the new plant was not "dedicated to the public" so far as the disputed service to the mill was concerned.^{36/}

The Public Utilities Act expressly provides that the class of water companies subject to Commission jurisdiction "shall not include any water system serving less than sixty customers where the average annual gross revenue per customer does not exceed one hundred twenty dollars per year."^{37/} There are no comparable quantitative figures

for other types of utility service.

The production of energy for strictly private use is exempt from regulation.^{38/} However, there has been no definitive ruling on the question of whether production of energy for use of the producer's tenants only is subject to Commission regulation.

The Washington statutes exclude from the definition of electrical company any:

company or person employing a cogeneration facility solely for the generation of electricity for its own use or the use of its tenants or for sale to an electrical company, state or local public agency, municipal corporation, or quasi municipal corporation engaged in the sale of distribution of electrical energy but not for sale to others, unless such company or person is otherwise an electrical company. ^{39/}

"Cogeneration facility" is defined as:

any machinery, equipment, structure, process or property, or any part thereof, installed or acquired for the primary purpose of the sequential generation of electrical or mechanical power and useful heat from the same primary energy source or fuel. ^{40/}

Any individual natural person, not otherwise engaged in the business of power production, who generates power by a non-polluting, renewable energy source is also exempted from all statutes and rules regulating the generation of power.^{41/} These individuals are authorized to sell this power to the utility servicing the property on which the power is generated at a price agreed upon by the parties.^{42/}

III. POWERS OF THE STATE AGENCIES

A. The Commission

The Commission is generally authorized by statute to regulate, in the public interest, the rates, services, facilities and practices of all public utilities.^{43/}

The Commission is given authority by statute to regulate rates for sales to the public;^{44/} rates for sales to a party for resale to the public;^{45/} capitalization;^{46/} issuance of securities;^{47/} systems of accounts;^{48/} the fixing of proper and adequate rates of depreciation;^{49/} mergers and consolidations;^{50/} affiliated interest transactions;^{51/} service area agreements between utilities;^{52/} sales or leases of utility property;^{53/} transfer of franchises or property;^{54/} abandonment of service;^{55/} and standards of service.^{56/}

With respect to electric utilities, the Commission does not regulate construction or siting of new plants, or expansion of existing plants.^{57/} Extension of electric service to new customers is not subject to Commission jurisdiction.^{58/}

B. Department of Revenue

Any person or company which constructs and operates a cogeneration facility may apply to the Department of Revenue for a tax credit certificate. This application must

contain the estimated or actual cost and specifications of the cogeneration facility.^{59/} The Department shall provide the Energy Office with a copy of the application. The Energy Office must approve the application within sixty days if it determines that construction of the facility began after the effective date of this Act (September 1, 1979), the facility is designed primarily for cogeneration and is suitable, reasonably adequate and meets the intent and purposes of the chapter.^{60/} When the application is approved by the Energy Office, the Department of Revenue must issue the requested certificate if it finds that the cost data submitted is accurate.^{61/}

When a certificated facility is operational, its operators are entitled to a credit against their business and occupation taxes. The credit will be in the amount of two percent of the cost of the facility in each year the certificate is in effect.^{62/} "Cost" is defined as:

only the cost of a cogeneration facility which is in addition to the cost that the applicant otherwise would incur to meet the applicant's demands for useful heat. "Cost" does not include expenditures which are offset by cost savings, including but not limited to savings resulting from early retirement of existing equipment.^{63/}

The credit may not exceed fifty percent of the taxes payable in any reporting period and may not exceed fifty percent of the cost of the cogeneration facility.^{64/}

In addition, certificated cogeneration facilities are exempt from property taxation for seven years after the

facility becomes operational or until the certificate is
revoked, whichever is first.^{65/}

IV. AUTHORITY TO ASSIGN RIGHTS TO PROVIDE SERVICE IN A GIVEN AREA

The Commission does not issue certificates of
public convenience and necessity to electric utilities.^{66/}
The statute does require that gas companies obtain a certi-
ficate from the Commission prior to commencing operation.^{67/}
The certificate issued to a gas company delineates its
service area.^{68/} Similarly, the Commission has power to
prescribe the exchange area boundaries or territorial boundaries
for telephone companies.^{69/} Exchange area boundaries are
contained in maps approved by the Commission in conjunction
with tariff schedules.^{70/} Yet despite these parallels in
other utility services, the Commission has not been empowered
to issue certificates nor to prescribe service areas for
electrical companies.^{71/}

Competition between electric utilities has never
been a serious problem in Washington. The state's three
major, privately owned utilities are established in different
regions of the state, Puget Sound Power & Light is located
in the Puget Sound area, the Washington Water Power Company
in the northeast,^{72/} and Pacific Power & Light, generally to
the southeast. There is some overlapping between service
areas of municipal and privately owned electric utilities.^{73/}
Undesirable competition is largely left to each municipality
to regulate through its power to grant franchises.^{74/}

A statutory mechanism to preclude service area disputes was adopted by the legislature in 1969. This mechanism has been used only two or three times.^{75/} This statute provides for voluntary service area agreements between privately owned electric utilities or electric cooperatives to be ratified and made binding by the Commission. As the statement of legislative intent explains:

The legislature hereby declares that the duplication of the electric lines and service of public utilities and cooperatives is uneconomical, may create unnecessary hazards to the public safety, discourages investment in permanent underground facilities, and is unattractive, and thus is contrary to the public interest and further declares that it is in the public interest for public utilities and cooperatives to enter into agreements for the purpose of avoiding or eliminating such duplication. ^{76/}

The electric suppliers that may take advantage of the statute are defined as follows:

(1) "Public utility" means any privately owned public utility company engaged in rendering electric service to the public for hire, any public utility district engaged in rendering service to residential customers and any city or town engaged in the electric business.

(2) "Cooperative" means any cooperative having authority to engage in the electric business. ^{77/}

The mechanism for reaching binding agreements is described by the following section of the statute:

In aid of the foregoing declaration of policy, any public utility and any cooperative is hereby authorized to enter

into agreements with any one or more other public utility or one or more other cooperative for the designation of the boundaries of adjoining service areas which each such public utility or each such cooperative shall observe, for the establishment of procedures for orderly extension of service in adjoining areas not currently served by any such public utility or any such cooperative of duplicating utility facilities, which agreements shall be for a reasonable period of time not in excess of twenty-five years: Provided, That the participation in such agreement of any public utility which is an electrical company under RCW 80.04.010, excepting cities and towns, shall be approved by the Washington utilities and transportation commission. 78/

While there is no general statutory provision requiring Commission approval of abandonment of service by public utilities, gas and electric companies can discontinue service to individual customers only under certain circumstances enumerated in Commission regulations. 79/

Service may be discontinued for nonpayment of bills, unauthorized use of gas or electricity, willful waste of energy, tampering with company property and other similar improper actions on the part of the customer. 80/ Service can be discontinued only after complying with notice requirements provided in the Commission rules. 81/

V. JUDICIAL REVIEW OF COMMISSION DECISIONS

Any public service company affected by a Commission order may petition for a rehearing. Such a petition must be filed within ten days after service of the order to be reconsidered. 82/ Petition for rehearing, however, is not a

prerequisite to seeking judicial review.

Any party affected by a Commission order may apply for a writ of review of the order by the superior court of Thurston county. Application for review must be made within thirty days after service of the order. If reconsideration has been denied then the application for a writ of review by the court must be made within thirty days after service of the order of denial.^{83/} Appeals to the superior court are heard without a jury and based on the record as certified by the Commission.^{84/}

Further appeals are governed by the following provision: "The Commission, any public service company or any complainant may, after the entry or judgment in the superior court in any action of review, prosecute an appeal to the supreme court or the court of appeals of the state of Washington as in other cases."^{85/}

FOOTNOTES

1. Wash. Const. art. 12, §18.
2. Wash. Rev. Code Ann. §80.04.010 et seq. (West 1962 and West Supp. 1980).
3. Id. §80.01.010 (West 1962).
4. Ibid.
5. Wash. Laws of 1979, Chapter 191, §§1-9.
6. Id. §3.
7. Wash. Rev. Code Ann. §80.01.040(3) (West 1962).
8. Id. §80.01.040.
9. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to the Commission, Telephone conversation, 8/11/78.
10. Wash. Rev. Code Ann. §80.04.500 (West Supp. 1980)
11. Ibid.
12. Id. §80.04.010.
13. Id. §80.01.040 (3) (West Supp. 1980).
14. Id. §80.04.010 (West Supp. 1980).
15. Id. §80.28.120 (West 1962).
16. Dep't of Public Works v. West Coast Power Co.,
5 P.U.R. N.S. 204, 222 (1934).
17. Id. at 222-23.
18. Id. at 223.
19. Id. at 222.
20. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to Commission, Telephone conversation, 8/11/78. A noteworthy precedent for ICES development is found in the nine cogeneration plants operated by pulp mills in the state of Washington. The 40-megawatt cogeneration facility at Longview, Washington boasts the largest electric output of any of these plants; one of the facilities is rated at 68 megawatts, but it is not fully operational. The plants direct the heat and some of the electricity to the lumber operations themselves and feed surplus electric power into the Bonneville Power Administration grid. (Mr. P. Juhasz, Industrial-Commercial Energy Program

Coordinator, Wash. State Energy Office, Telephone conversation, 8/1/78). The Weyerhaeuser Company own three cogeneration plants in Washington for which contracts have been made with Alcoa, Inc. and other metallurgical firms for the furnishing of electric power. Bonneville acts as an agent in these contracts, providing storage, load shaping, and transmission in exchange for a service fee. The Washington Utilities and Transportation Commission has made no attempt to regulate any aspect.

(Mr. R. Tallman, Head of Thermal Power Section, Bonneville Power Administration, Telephone conversation, 8/4/78; Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to Wash. Utilities & Transp. Comm'n, Telephone conversation, 8/11/78.)

21. Wash. Rev. Code Ann. §80.01.040(3) (West 1962).
22. Id. §80.28.110.
23. 177 Wash. 237, 31 P.2d 564 (1934).
24. Inland Empire Rural Electrification, Inc. v. Dep't of Public Service, 199 Wash. 527, 92 P.2d 258 (1939).
25. Id. 92 P.2d at 262-63.
26. Id. 92 P.2d at 263-64.
27. Sunset Shingle Co. v. Northwest Elec. & Water Works, 118 Wash. 416, 203 P. 978 (1922).
28. Id. 203 P. at 980.
29. Ibid.
30. Ibid.
31. Id. 203 P. at 982.
32. Ibid.
33. Ibid.
34. Ibid.
35. Ibid.
36. Id. 203 P. at 982-93.
37. Wash. Rev. Code Ann. §80-04.010 (West Supp. 1980).
38. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to the Commission, Telephone conversation, 8/11/78.

39. Wash. Rev. Code Ann. §80.04.010 (West Supp. 1980).
40. Ibid.
41. Id. §80.28.010.
42. Ibid.
43. Wash. Rev. Code Ann. §80.01.040 (West 1962).
44. Id. §80.28.020.
45. Id. §80.28.120.
46. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to the Commission, Telephone conversation, 8/11/78.
47. Wash. Rev. Code Ann. §80.08.020- .070 (1962); Wash. Admin. Code 480-100-036 (1976).
48. Wash. Admin. Code §480-100-031 (1976).
49. Wash. Rev. Code Ann. §80.04.350 (West 1962).
50. Id. §80.12.120.
51. Id. §80.16.020; Wash. Admin. Code §480-100-036 (1976).
52. Wash. Rev. Code Ann. §54.48.030 (West Supp. 1980).
53. Id. §80.12.020- .030 (West 1962).
54. Ibid.
55. Wash. Admin. Code §480-100-156, -071 (1976).
56. Wash. Rev. Code Ann. §80.28.030, -.040 (West 1962).
57. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to the Commission, Telephone conversation, 8/11/78.
58. Ibid.
59. Wash. Rev. Code Ann. §82.35.030(1) (West Supp. 1980).
60. Id. §82.35.030(2).
61. Id. §82.35.030(3).
62. Id. §82.35.050.
63. Id. §82.35.020.(4).

64. Id. §82.35.050(3,4).
65. Wash. Laws of 1979, Chapter 191, §90.
66. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to the Commission, Telephone conversation, 8/11/78.
67. Wash. Rev. Code Ann. §80.28.190 (West Supp. 1980).
68. Ibid.
69. Id. §80.36.230 (West 1962).
70. Mr. F.P. Hayes, Asst. Att'y Gen., Staff Counsel to the Commission, Telephone conversation, 8/11/78.
71. Ibid.
72. Ibid.
73. For example, in or near the communities of Tacoma, Sumas, and Blaine. Mr. F.P. Hayes, supra.
74. Ibid.
75. Ibid.
76. Wash. Rev. Code Ann. §54.48.020 (West Supp. 1980).
77. Id. §54.48.010.
78. Id. §54.48.030.
79. Wash. Admin. Code §§480-090-071, 480-100-071 (Supp. 6/30/76).
80. Ibid.
81. Ibid.
82. Wash. Rev. Code Ann. §80.04.165 (West 1962).
83. Id. §80.04.170.
84. Ibid.
85. Id. §80.04.190 (West Supp. 1980).

CHAPTER 3

SITING OF ENERGY FACILITIES IN WASHINGTON

I. PUBLIC AGENCIES WHICH ADMINISTER SITING LAWS

Comprehensive laws and rules relating to the siting of energy facilities in Washington are provided in the Washington statutes^{1/} and in Title 463 of the Washington Administrative Code. The Siting Act, passed in 1970, created a Thermal Power Plant Evaluation Council which, as a result of recent legislation, has been renamed the Energy Facility Site Evaluation Council (Council). At least seven power plants have been approved under the Siting Act.^{3/}

The chairman of the Council is appointed by the governor with the advice and consent of the senate. The chairman serves for a term coextensive with the term of the governor and may be removed for cause.

Council membership is composed of a representative from each of the following departments:

- (a) Department of Ecology
- (b) Department of Fisheries
- (c) Department of Game
- (d) Department of Parks and Recreation
- (e) Department of Social and Health Services
- (f) State Energy Office
- (g) Department of Commerce and Economic Development
- (h) Utilities and Transportation Commission
- (i) Office of Program Planning and Fiscal Management
- (j) Department of Natural Resources
- (k) Planning and Community Affairs Agency
- (l) Department of Emergency Services
- (m) Department of Agriculture¹¹
- (n) Department of Highways ^{4/}

Local governments also have a role in the Council:

(4) The appropriate county legislative authority of every county wherein an application for a proposed site is filed shall appoint a member or designee as a voting member to the council. The member or designee so appointed shall sit with the council only at such times as the council considers the proposed site for the county which he represents and such member or designee shall serve until there has been a final acceptance or rejection of such proposed site. 5/

Cities in which an energy plant are proposed to be located have similar authority to appoint a member to the Council. 6/

Port districts appoint a nonvoting member to the Council where applications for proposed port facilities are under consideration. 7/

The Council makes recommendations to the governor as to the approval or rejection of applications for site certification. 8/ Recommendations of the Council that are ratified by the governor totally preempt the siting powers of other state and local agencies. 9/

The Washington Attorney General has issued an opinion that certification by the governor of an energy facility permits construction and operation at the location specified irrespective of contrary provisions of a local zoning code. 10/ In another opinion, the Attorney General stated that certification of a thermal power plant approved by the governor authorizes the withdrawal of public waters required for use in operating the power plant. 11/

II. JURISDICTION OF THE COUNCIL

The Council has jurisdiction over the siting of "energy facilities," which means an energy plant or transmission facility. So far as here relevant, the term "energy plant" includes the following facilities together with their "associated facilities":

(a) Any stationary thermal power plant with generating capacity of two hundred fifty thousand kilowatts or more and floating thermal power plants of fifty thousand kilowatts or more, including associated facilities;

(b) Facilities which will have the capacity to receive liquified natural gas in the equivalent of more than one hundred million standard cubic feet of natural gas per day, which has been transported over marine waters;

* * *

(d) Any underground reservoir for receipt and storage of natural gas as defined in RCW 80.40.010 capable of delivering an average of more than one hundred million standard cubic feet of natural gas per day;

. . . . 12/

"Thermal power plant," for the purpose of certification, means any electrical generating facility using any fuel, including nuclear materials, for distribution of electricity by electric utilities. 13/

"Transmission facility" is defined to include only gas and petroleum pipeline systems. 14/ However, the definition of "associated facilities" includes certain electric transmission lines as well as other related facilities:

"Associated facilities" means storage, transmission, handling, or other related and

supporting facilities connecting an energy plant with the existing energy supply, processing, or distribution system, including, but not limited to, communications, controls, mobilizing or maintenance equipment, instrumentation, and other types of ancillary transmission equipment, off-line storage or venting required for efficient operation or safety of the transmission system and overhead, and surface or subsurface lines of physical access for the inspection, maintenance, and safe operations of the transmission facility and new transmission lines constructed to operate at nominal voltages in excess of 200,000 volts to connect a thermal power plant to the northwest power grid: Provided, that common carrier railroads or motor vehicles shall not be included. 15/

The form of ownership of a utility does not affect Council jurisdiction. 16/

The Siting Act provides the Council with jurisdiction over preparation for new construction, replacement of existing facilities, and extension of existing facilities. "Construction" means on-site improvements, excluding exploratory work, 17/ which cost in excess of two hundred fifty thousand dollars.

With regard to the extension or enlargement of facilities, another section of the statute explains:

The provisions of this chapter shall apply to . . . the reconstruction or enlargement of existing energy facilities where the net increase in physical capacity or dimensions resulting from such reconstruction or enlargement meets or exceeds those capacities or dimensions set forth in RCW 80.50.020(7) and (17), as now or hereafter amended The provisions of this chapter shall not apply to normal maintenance and repairs which do not increase the capacity or dimensions of the facility beyond those set forth in RCW 80.50.020(7) and (17). 18/

The statute has a grandfather clause exemption:

Applications for certification of energy facilities made prior to July 15, 1977 shall continue to be governed by the applicable provisions of law in effect on the day immediately preceding July 15, 1977 with the exceptions of RCW 80.50.190 and 80.50.071 [regarding disposition of fees] which shall apply to such prior applications and to site certifications prospectively from July 15, 1977. 19/

The above quotation is part of the most recent amendment to the Siting Act. To be entirely exempt from earlier versions of the statute as well, construction (as defined above) must have commenced prior to February 23, 1970. 20/

The authority of the Council is not limited to initial siting approvals. The Council also has the power:

To prescribe the means for monitoring of the effects arising from the construction and the operation of energy facilities to assure continued compliance with terms of certification. . . .
Provided, That any on site inspection required by the council shall be performed by other state agencies pursuant to interagency agreement:
Provided further, That the council shall retain authority for determining compliance relative to monitoring. 21/

The statute authorizes the Council "[t]o adopt, promulgate, amend, or rescind suitable rules and regulations. . . . to carry out the provisions of this chapter, and the policies and practices of the council in connection therewith." 22/

Rules have been adopted so that compliance with the National Pollutant Discharge Elimination System (NPDES) Permit Program is incorporated into the siting process. 23/

Applications to the Council must be accompanied by appropriate NPDES applications. 24/

After holding public hearings, the Council may issue or deny an NPDES permit. 25/ Guidelines have also been

adopted to coordinate the State Environmental Policy Act (including requirements for submitting Environmental Impact Statements) with the Siting Act.^{26/} Certain utility-related actions are exempt from Environmental Impact Statement requirements. These include construction of "[a]ll electric facilities, lines, equipment or appurtenances, not including substations, with an associated voltage of 55,000 volts or less."^{27/} Other rules adopted do not appear to define further the scope of Council jurisdiction.

There has been one court case concerning the Siting Act, Skagitonians Concerned about Nuclear Plants v. Evans.^{28/} Other aspects of the case are still being litigated, but the judge has entered a preliminary ruling upholding the constitutionality of the Siting Act.^{29/}

As noted above, the Council totally preempts the authority of state and local agencies; certification by the Council stands in lieu of any permit or certificate required by any agency or political subdivision of the state.^{30/} Certain procedural obligations of the Council with respect to compliance with local land use plans and zoning ordinances are noted below.

III. CERTIFICATION PROCESS

1. Application

The required contents of applications for site certification are outlined in detail in administrative regulations.^{31/} Applications must include an analysis of alternate

sites. ^{32/}

2. Notices

Notice and publication requirements are the responsibility of the Council. Local and state authorities must be notified when site proposals are filed, or in advance of hearings, as specified. ^{33/} Informational releases to the news media are prescribed. ^{34/}

3. Initial Hearing, Contested Case Hearing

The Council must conduct a public hearing in the county of the proposed site within sixty days of receipt of an application. ^{35/} A public hearing must also be held prior to issuance of a Council recommendation to the governor. ^{36/} Additional public hearings may be conducted as deemed appropriate. ^{37/}

The Council is to determine at the initial public hearing whether or not the proposed site is consistent and in compliance with county or regional land use plans or zoning ordinances in effect as of the date of application. If the Council determines that the proposed site does conform with such plans and ordinances, the county or regional planning authority may not thereafter change them so as to affect the proposed site. ^{38/}

Administrative regulations outline the procedure in case the Council determines that the site of a proposed energy facility or any portion of a site is not consistent with existing land use plans or zoning ordinances in effect

at the date of the application:

(1) As a condition necessary to continue processing the application, it shall be the responsibility of the applicant to make the necessary application for change in, or permission under, such land use plans or zoning ordinances, and make all reasonable efforts to resolve the noncompliance.

(2) All council proceedings on the application for certification may be stayed at the request of the applicant during the period when the plea for resolution of noncompliance is being processed by local authorities.

(3) The applicant shall submit regular reports to the council regarding the status of negotiations with local authorities on noncompliance issues. 39/

Where negotiations with local authorities fail, the rules provide that, if an applicant elects to continue processing the application, he must file a written request for state preemption, as authorized by the Washington Administrative Code, within ninety days after completion of the public hearing required by statute, or later if mutually agreed by the applicant and the Council. 40/ The request shall address the following:

(1) That the applicant has demonstrated a good faith effort to resolve the noncompliance issues.

(2) That the applicant and the local authorities are unable to reach an agreement which will resolve the issues.

(3) That alternate locations which are within the same county and city have been reviewed and have been found unacceptable.

(4) Interests of the state as delineated in RCW 80.50.010. 41/

At this point, the Council must hold a "contested case hearing" to determine whether to recommend to the

governor that the state preempt local plans or ordinances. ^{42/}

The Council must report to the governor its recommendations as to the approval or rejection of an application for certification within twelve months of receipt of the application, or such later time as is mutually agreed by the Council and the applicant. If the Council recommends approval of an application for certification, it must submit a draft certification agreement with the report. The Council is to include conditions in the draft certification agreement to implement the provisions, provided by statute, ^{43/} including, but not limited to, conditions to protect state or local governmental or community interests affected by the construction or operation of the energy facility, and conditions designed to recognize the purpose of laws or ordinances, or rules or regulations promulgated thereunder, which are to be preempted or superseded. ^{44/}

Within sixty days of receipt of the Council's report the governor is to take one of the following actions:

- (a) Approve the application and execute the draft certification agreement; or
- (b) Reject the application; or
- (c) Direct the council to reconsider certain aspects of the draft certification agreement. ^{45/}

The Council is to reconsider such aspects of the draft certification agreement by reviewing the record of the application, or if necessary reopening the contested case to receive additional evidence. The Council then must resubmit the draft certification to the governor incorporating

any amendments deemed necessary by reconsideration. The governor, within 60 days, must either approve or reject the application. The certification agreement becomes binding upon execution by the governor and the applicant.^{46/}

The Siting Act provides that the rejection of an application for a certificate is final, and contains no procedures for rehearing. However, the Siting Act incorporates by reference the Washington Administrative Review Act, which provides that if a party invokes any provisions for rehearing which the agency has established by rules, then the party must wait until the agency acts upon the rehearing request before seeking judicial review.^{47/} Judicial review is available to any aggrieved party. It is conducted by a district court, sitting without a jury, and is confined to the record, except in cases of alleged irregularities in procedure.^{48/}

The court may either affirm the agency's decision or remand the case. The court may also reverse the decision if the rights of the petitioners have been prejudiced because the administrative findings are:

- (a) in violation of constitutional provisions; or
- (b) in excess of the statutory authority or jurisdiction of the agency; or
- (c) made upon unlawful procedure; or
- (d) affected by other error of law; or
- (e) clearly erroneous in view of the entire record as submitted and the public contained in the act of the legislature authorizing the decision or order; or
- (f) arbitrary or capricious. ^{49/}

IV. CERTIFICATION STANDARDS

The statement of legislative intent provided in the Siting Act establishes certain broad goals to be achieved in siting energy facilities:

It is the policy of the state of Washington to recognize the pressing need for increased energy facilities, and to ensure through available and reasonable methods, that the location and operation of such facilities will produce minimal adverse effects on the environment, ecology of the land and its wildlife, and the ecology of state waters and their aquatic life.

It is the intent to seek courses of action that will balance the increasing demands for energy facility location and operation in conjunction with the broad interests of the public. Such action will be based on these premises:

(1) To assure Washington state citizens that, where applicable, operational safeguards are at least as stringent as the criteria established by the federal government and are technically sufficient for their welfare and protection.

(2) To preserve and protect the quality of the environment; to enhance the public's opportunity to enjoy the esthetic and recreational benefits of the air, water and land resources; to promote air cleanliness; and to pursue beneficial changes in the environment.

(3) To provide abundant energy at reasonable cost. 50/

Apparently these criteria apply to all types of facilities subject to Council jurisdiction. The Council has complete leeway to balance the factors within the framework of the 51/ Siting statute.

With regard to overriding inconsistent local land use restrictions, Council rules establish certain criteria to be considered. The Council attempts to determine that the applicant has demonstrated a good faith effort to

resolve noncompliance issues; that the applicant and local authorities are unable to reach an agreement which will resolve the issues; that alternative locations within the same county and city have been found unacceptable, and that due care for the "interests of state" (as defined in the statement of legislative intent) has been taken into consideration.^{52/}

If the Council approves the request to override restrictions, it is to include conditions in the draft certification agreement which give consideration to the state or local governmental or community interests affected by the construction or operation of the energy facility. The Council is also to consider the purposes of the laws, ordinances, rules or regulations which will be preempted or superseded.^{53/}

V. LOCATION AND PLANNING OF DEVELOPMENTS GENERALLY

A. Environmental Coordination Procedures Act

In order for a power plant to fall under the Council's jurisdiction, it must meet a 250,000 kilowatt minimum requirement for stationary thermal power plants. Hence, many power plants will not be subject to the preemptory provisions of the Washington Siting Act. The Council has been asked informally whether a smaller unit might be brought under the statute by a voluntary process.^{54/} The answer to this question was described as "up in the air."^{55/} The plain language of the statute, however, would seem to give little support to

a theory of voluntary submission to Council jurisdiction, and, thus, small projects may be forced to seek approvals and permits from numerous separate agencies and local government units.

The Washington legislature has enacted an Environmental Coordination Procedures Act, (Coordination Act)^{56/} to expedite the approval process for facilities not subject to the Council's jurisdiction.^{57/} The procedures of the Coordination Act are optional for developers of smaller energy facilities.^{58/} By submitting a master application under the Act to the state Department of Ecology, a developer may request issuance of all "permits" necessary prior to construction and operation of the project.^{59/} "Permit," as defined by the Coordination Act, is not an all-encompassing term:

"Permit" means any license, permit, certificate, certification, approval, compliance schedule, or other similar document pertaining to any regulatory or management program related to the protection, conservation, or use of, or interference with, the natural resources of land, air or water in the state, which is required to be obtained from a state agency prior to constructing or operating a project in the state of Washington. Permit shall also mean a substantial development permit under RCW 90.58.140 and any permit, required by a local government for a project, that the local government has chosen to process pursuant to RCW 90.62.100 (2) as now or hereafter amended. Nothing in this chapter shall relate to a permit issued by the department of labor and industries or by the utilities and transportation commission; nor to the granting of proprietary interests, in publicly owned property such as sales, leases, easements, use permits and licenses. ^{60/}

"State agency," for the purposes of the Coordination Act, means any state department, commission, board or other agency of the state however titled. "State agency" also means: (a) any local or regional air pollution control authority established under chapter 70.94 RCW and (b) any local government when said government is acting in its capacity as a decision maker on an application for a permit pursuant to RCW 90.58.140.^{61/} According to one commentator, the last sentence in the definition of "permit" excludes a number of authorizations necessary for construction on public lands from coverage under the Coordination Act:

The effect, and apparently the purpose, of that exclusion is to exempt from ECPA most of the programs and activities of the Department of Natural Resources and of its official head, the Commissioner of Public Lands The Commissioner has important authority, exercised through "permits," over the tide, shore and other lands of the state. ^{62/}

"Person," for purposes of the Act, "means any individual, municipal, public, or private corporation, or other entity however denominated, including a state agency and county."^{63/}

B. Coordination Act Application Procedures

Any person proposing a project may submit a master application to the Department of Ecology (Department) requesting the issuance of all permits necessary prior to the construction and operation of the project. The Department provides a master application; the application requires

specific information as to the location and the nature of the project, including any discharges of wastes and any uses of or interferences with, natural resources contemplated. ^{64/}

Upon receipt of a completed application, the Department notifies in writing each state and local agency having a possible interest in the project. The notification from the Department is to include a copy of the master application, together with the date by which the agency is to respond. Each notified agency must respond to the Department, advising:

(a)(i) whether the agency does or does not have an interest in the master application, and (a)(ii) if the response to (a)(i) of this subsection is affirmative, the permit program or programs under the agency's jurisdiction to which the project described in the master application is pertinent, and whether, in relation to the master application, a public hearing as provided in RCW 90.62.050 and 90.62.060 would or would not be of value taking into consideration the overall public interest ^{65/}

The Department then sends application forms relating to the permit programs identified in the agency responses to the applicant with a direction to complete and return them to the Department within a reasonable time. Each completed application returned to the Department is transmitted by it to the appropriate agency for its decision. ^{66/}

Public notice of the application is provided by the Department at the applicant's expense. ^{67/} Unless responses from state agencies unanimously indicate that no public hearing is necessary in the public interest, such a hearing

must be held within fifteen days of the date of last publication of the notice.^{68/} Each agency having a permit application before it must be represented at the public hearing.^{69/} The director of the Department is chairman of the hearing.^{70/}

Review of the denial of a state agency permit is available at the administrative level in the form of a "de novo quasi judicial hearing," conducted by the Pollution Control Hearings Board, or Shorelines Hearings Board, or both Boards jointly, depending on the location and type of project involved.^{71/} Review of denials of local government units, however, is to be "in the same manner as would apply had the local government not utilized the procedures provided by this chapter."^{72/}

C. Agencies and Permits

The following is a brief outline of some of the agencies and permits that may be involved in siting a power plant not subject to the Siting Act and the jurisdiction of the Council. Most of these agencies would be "state agencies" and would issue "permits" under the Coordination Act.

1. Environmental Agency

The chief state environmental agency is the Department of Ecology (Department). The Department, in conjunction with Regional Air Pollution Control Authorities, has jurisdiction over sources of air emissions. The Department or the board of any Regional Air Pollution Control Authority may require notice of the construction, enlargement, or re-

placement of any new air contaminant source.^{73/} The Department or regional authority, as appropriate, may approve or dis-^{74/}approve the construction by issuance of an order. The Department and the Regional Air Pollution Control Authorities have jurisdiction to grant variances from air pollution standards.^{75/}

The Department is designated as the state water pollution control agency for purposes of issuing NPDES permits.^{76/} The Department issues permits for waste disposal systems;^{77/} for appropriation of surface water when required;^{78/} for withdrawal of ground water.^{79/} Sewerage facilities approval and oil discharge permits are also the responsibility of the Department.^{80/}

2. Planning Authorities

Counties are empowered to create a county planning commission or planning department.^{81/} County planning commissions are responsible for drafting a comprehensive plan for the orderly physical development of the county.^{82/} Comprehensive plans must include a land use element proposing general location and extent of the uses of land for commerce, industry, public buildings, and other categories of public and private land use.^{83/} Comprehensive plans may include an optional public services and facilities element showing general plans for local utilities and rights of way, easements, and facilities for such services.^{84/} Once a comprehensive plan is approved by motion and certified by the board of

county commissioners, the planning commission may prepare official controls, including zoning ordinances and subdivision controls, to implement the objectives of the comprehensive plan.^{85/} The board of county commissioners is responsible for issuing building permits within the county, except within cities therein which maintain their own building permit program.^{86/}

Municipalities may also set up planning commissions.^{87/} City planning commissions also prepare comprehensive plans for physical development to ensure, among other things, "the adequate provision of transportation, water, sewerage and other public uses and requirements."^{88/} The city council, upon recommendation of the commission, may adopt ordinances to regulate and restrict the location, use, and design of buildings and structures within the city.^{89/}

Washington law provides for the establishment of other planning authorities to act on a metropolitan or regional basis. A metropolitan municipal corporation may be created for the performance of certain functions by vote of the residents of populous metropolitan areas.^{90/} Where authorized by election, a metropolitan municipal corporation may perform the function of metropolitan comprehensive planning.^{91/} A metropolitan municipal corporation may prepare a recommended comprehensive land use and capital facilities plan and may review proposed zoning ordinances or comprehensive plans of component cities and counties.^{92/} It does not appear, however,

that a metropolitan municipal corporation has power to veto ordinances or plans of component cities and counties, nor to prohibit developments in conflict with its own master plans.

A county or city may join with one or more other counties, cities, towns, or specified districts to form and organize a regional planning commission.^{93/} "Such regional planning commission may carry on a planning program involving the same subjects and procedures provided by this chapter for planning by counties, provided this authority shall not include enacting official controls other than by the individual participating municipal corporations."^{94/}

The Department of Commerce and Economic Development (DCED) is responsible for preparing a state comprehensive plan to facilitate regional and local government planning.^{95/} DCED acts as a consultative, coordinating, and advisory agency. It does not appear DCED has power to prohibit development that does not conform to the state comprehensive plan.^{96/}

At the state level, overall responsibility for environmental planning, and protecting areas of critical concern is vested in the Department.^{97/}

The Department of Natural Resources is responsible for policy in management and disposition of public lands.^{98/} A clause in the Coordination Act may exempt the permitting authority of the Department of Natural Resources from the provisions of the Act.^{99/}

The Interagency Committee for Outdoor Recreation

is charged with preparing comprehensive plans for the development of outdoor recreation resources in the state, but the committee appears to lack power to prohibit specific developments.^{100/}

Washington statutes also provide that no person, firm or agency may knowingly dig into or excavate an historic or archaeological site without written permission from the state historic preservation officer.^{101/}

3. Shoreline Management Act

The Coordination Act provides that "approval of an application for certification as provided in this section shall not eliminate any requirements of the Shoreline Management Act of 1971 . . ."^{102/} The Shoreline Management Act (Shoreline Act) requires all counties, incorporated cities, and towns with shorelines to develop master programs for their shorelines and to submit them to the Department for approval.^{103/} "Shorelines" is given a broad definition that includes not only the Pacific coast, but "all of the water areas of the state, including reservoirs, and their associated wetlands, together with the lands underlying them."^{104/}

Local governments have authority under the Shoreline Act to prohibit the siting of various facilities and uses on shorelines of the state through the adoption of master programs. "The master programs shall include, when appropriate, . . .[a] circulation element consisting of the location and extent of existing and proposed . . . public utilities and

facilities"^{105/} "No substantial development shall be undertaken on shorelines of the state without first obtaining

a permit"^{106/} Permits are to be issued only if the development is in compliance with the master program.^{107/}

"Substantial development' shall mean any development of which the total cost or fair market value exceeds one thousand dollars"^{108/} Local governments must establish a program, consistent with rules adopted by the Department, for the administration of the permit system.^{109/}

FOOTNOTES

1. Wash. Rev. Code Ann. ch. 80.50 (West Supp. 1980).
2. Id. §80.50.030.
3. Mr. W. L. Fitch, Executive Secretary of the Council, Telephone conversation, 8/1/78.
4. Wash. Rev. Code Ann. §80.50.030(2)(3) (West Supp. 1980).
5. Id. §80.50.030(4).
6. Id. §80.50.030(5).
7. Id. §80.50.030(6).
8. Id. §80.50.100.
9. Id. §§80.50.110, 80.50.120.
10. Op. Att'y. Gen., No. 1 (Wash. 1977).
11. Op. Att'y Gen., No. 10 (Wash. 1975).
12. Wash. Rev. Code Ann. §80.50.020(14) (West Supp. 1980).
13. Id. §80.50.020(9).
14. Id. §80.50.020(7).
15. Id. §80.50.020(6).
16. Mr. W. L. Fitch, Executive Secretary of the Council, Telephone conversation, 8/1/78.
17. Wash. Rev. Code Ann. §80.50.020(13) (West Supp. 1980).
18. Id. §80.50.060(1)(2).
19. Id. §80.50.060(3).
20. 1970 Wash. Laws 1st Ex. Sess. ch. 45, §6.
21. Wash. Rev. Code Ann. §80.50.040(11) (West Supp. 1980).
22. Id. §80.50.040(1).
23. Id. §90.48.262(2) (West Supp. 1980).
24. Wash. Admin. Code §463-38-031 (1977).
25. Id. §§463-38-042, 463-38-050.
26. Id. §§463-47-010 to 463-46-910 (1976).

27. Id. §463-46-170(18).
28. Superior Court, Thurston County, Wash., No. 56273, (Valley Reporting Service, April 6, 1978).
29. Ibid.
30. Wash. Rev. Code Ann. §§80.50.110; 80.50.120 (West Supp. 1980).
31. Wash. Admin. Code §§463-42-101 to 463-42-620 (1977).
32. Id. §463-42-150.
33. Id. §463-22-060, 463-26-020, 463-30-110.
34. Id. §463-26-030, 463-30-090, 463-38-041.
35. Wash. Rev. Code Ann. §80.50.090(1) (West Supp. 1980).
36. Id. §80.50.090(3).
37. Id. §80.50.090(4).
38. Id. §80.50.090(2).
39. Wash. Admin. Code §463-28-030(1977).
40. Wash. Rev. Code Ann. §80.50.090 (West Supp. 1980).
41. Wash. Admin. Code §463-28-040.
42. Id. §463-28-060.
43. Wash. Rev. Code Ann. §80.50.100(1) (West Supp. 1980).
44. Ibid.
45. Id. §80.50.100(2).
46. Ibid.
47. Wash. Rev. Code Ann. §34.04.130(1) (West Supp. 1980).
48. Id. §34.04.130 (5).
49. Id. §34.04.130(6).
50. Id. §80.50.010.
51. Mr. W.L. Fitch, Executive Secretary of the Council, Telephone conversation, 8/1/78.
52. Wash. Admin. Code §463-28-040 (1977).

53. Id. §463-28-070.
54. Mr. W.L. Fitch, Executive Secretary of the Council, Telephone conversation, 8/1/78).
55. Ibid.
56. Wash. Rev. Code Ann. ch. 90.62 (West Supp. 1980).
57. Id. §90.62.030.
58. Id. §90.62.010.
59. Id. §90.62.040(1).
60. Id. §90.62.020(4).
61. Id. §90.62.020(8).
62. Corker, The Environmental Coordination Procedures Act of 1973, 49 Wash. L. Rev. 463, 478 (1974).
63. Wash. Rev. code Ann. §90.62.020(5) (West Supp. 1980).
64. Id. §90.62.040(1).
65. Id. §90.62.040(2).
66. Id. §90.62.040(3)(4).
67. Id. §90.62.050(1).
68. Ibid.
69. Id. §90.62.060(2).
70. Ibid.
71. Id. §90.62.080(1)(2).
72. Id. §90.62.080(5)(a).
73. Id. §70.94.152 (West 1975); Wash. Admin. Code §173-400-110 (1976).
74. Wash. Rev. Code Ann. §70.94.152(1) (west 1975).
75. Id. §70.94.181.
76. Id. §90.48.260, 262 (West Supp, 1980); Wash. Admin. Code §173-220-040 (1976).
77. Wash. Rev. Code Ann. §§90.48.160 to 180 (West Supp. 1980).

78. Id. §§90.03.10 (West 1962); 43.21A.060(2) (West Supp. 1980).
79. Id. §90.44.050 (West 1962).
80. Id. §§90.48.110 to .343.
81. Id. §36.70.030, .040 (West 1964).
82. Id. §36.70.320 (West Supp. 1980).
83. Id. §36.70.330(1) (West 1964).
84. Id. §36.70.350(5).
85. Id. §§36.70.020(11), .450, .550, .560, .750.
86. Id. §36.21.050.
87. Id. §35.63.020.
88. Id. §35.63.090.
89. Id. §35.63.080.
90. Id. §35.58.070.
91. Id. §35.58.310.
92. Ibid.
93. Id. §36.70.060.
94. Ibid.
95. Id. §43.31.210 (West 1970).
96. Ibid.
97. Id. §43.21A.020 (West Supp. 1980).
98. Id. §43.30.150.
99. See Part V, A. for a detailed discussion of the Coordination Act.
100. Wash. Rev. Code Ann. §43.99.122 (West 1970).
101. Id. §27.53.060 (West Supp. 1980).
102. Id. §90.62.100(4).
103. Id. §§90.58.070, .090.

104. Id. §90.58.030(2)(d).

105. Id. §90.58.100(2).

106. Id. §90.58.140(2).

107. Id. §90.58.140(1).

108. Id. §90.58.030(3)(e).

109. Id. §90.58.140(3).

CHAPTER 4

FRANCHISING OF PUBLIC UTILITIES IN WASHINGTON

I. AUTHORITY TO GRANT FRANCHISES

Express grants of franchising authority are found in numerous sections of the Washington statutes. Governmental units authorized to grant franchises to use public streets and highways include counties, all municipalities, and the state Highway Commission.^{1/} For some of these grants, the entity that may receive a franchise is specified by statute (Highway Commission franchises).^{2/} For other franchises, the class of potential grantees is undefined (franchises granted by first class cities).^{3/} Some grants may apparently be for specifically listed utility services only (franchises by third class cities).^{4/} For another type of grant, the utility services that may be franchised are described by the broad phrase "railroad or other public service purposes" (franchises by second class cities).^{5/} Still another franchising statute requires that the board of county commissioners must deem a franchise "to be for the public interest (county franchises)."^{6/} These franchising statutes will be considered in detail below.

II. PROCEDURES FOR GRANTING FRANCHISES

The procedure for granting franchises and the type of grant that may be awarded differ for each class of granting authority. There are significant special provisions

affecting electric and street railroad franchises.

A. Municipalities

1. First Class Cities

Franchising authority for first class cities is described generally in the following statute:

Any city of the first class shall have power... (7) To lay out, establish, open, alter, widen, extend, grade, pave, plank, establish grades, or otherwise improve streets, alleys, avenues, sidewalks, wharves, parks, and other public grounds, and to regulate and control the use thereof, and to vacate the same, and to authorize or prohibit the use of electricity at, in, or upon any of said streets, or for other purposes, and to prescribe the terms and conditions upon which the same may be so used, and to regulate the use thereof.^{7/}

No special procedure is mentioned for the granting of franchises by first class cities. Procedures for adoption of ordinances by first class cities are also unspecified by the statute. Presumably, the applicable procedures are described in each city charter. If the city charter so provides, franchising may be granted by "direct legislation by the people through the initiative and referendum" procedure.^{8/}

2. Second Class Cities

General franchising power for second class cities is contained in this brief provision: "The city council of each second class city shall have power and authority...[to] permit the use of the streets for railroad or other public service

purposes."^{9/} Procedures for grants of franchises are given in the following statute:

No franchise or privilege shall be created or granted by the city council otherwise than by ordinance nor shall it be passed on the day of the introduction nor for thirty days thereafter and then only upon the affirmative vote of two-thirds of the councilmen elected. The city council may fix the rates and tolls to be charged within the city by any public service corporation enjoying a franchise granted by the city subject to review by any court of competent jurisdiction as to the reasonableness thereof. The city council may require a bond in a reasonable amount from any person or corporation obtaining a franchise from the city conditioned for the faithful performance of the conditions and terms of the franchise and providing a recovery on the bond in case of failure to perform the terms and conditions of the franchise.^{10/}

Requirements for notice are contained in the following provision:

No ordinance granting a franchise or privilege and no ordinance amending a prior ordinance granting a franchise or privilege shall be passed until it has been published in at least one issue of the official newspaper of the city....^{11/}

3. Third Class Cities

Third class cities may grant franchises pursuant to the following statute:

The city council of each third class city shall have power...(10) To permit, under such restrictions as it may deem proper, and to grant franchises for... laying of gas and water pipes and steam mains and conduits for underground wires, and to permit the construction

of tunnels or subways in the public streets, and to construct and maintain and to permit the construction and maintenance of telegraph, telephone and electric lines therein.12/

Third class cities may grant franchises either by ordinance or by resolution approved by at least five of the seven members of the city council at a regular meeting at least five days after its first introduction before the council.13/

4. Towns

Municipal corporations of the fourth class are known as towns.14/ Towns are empowered to grant franchises by the following statute:

The council of said town shall have power...(12) To grant franchises or permits to use and occupy the surface, the overhead and the underground of streets, alleys and other public ways, under such terms and conditions as it shall deem fit, for any and all purposes, including but not being limited to the construction, maintenance and operation of railroads, street railways, transportation systems, water, gas and steam systems, telephone and telegraph systems, electric lines, signal systems, surface, aerial and underground tramways....15/

The procedure is similar to that applicable to franchises granted by third class cities.16/

5. Municipalities with Special Forms of Government

The regular form of government for Washington municipalities is the mayor-council form of government. This form of government was assumed in the aforementioned statutes

governing first, second, and third class cities and towns.

A city having a population of 2,000 and less than 30,000 may^{17/} organize as a city under the commission form of government.

In cities with the commission form of government, a special statute governs the granting of franchises:

No franchise or right to occupy or use the streets, highways, bridges, or other public places shall be granted, renewed, or extended except by ordinance and every such ordinance complete in the form in which it is finally passed shall remain on file with the city clerk for at least one week before final passage and if the franchise or grant is for interurban or street railways, gas or waterworks, electric light or power plants, heating plants, telegraph or telephone systems or other public service utilities, the ordinance must be submitted to a vote of the people at a general or special election and approved by a majority of those voting thereon.^{18/}

Cities with the commission form of government are the only municipalities in which ratification by the voters is required by statute for a valid grant of a franchise.

Another optional form of municipal government is the council-manager plan. Any city or town having a population of less than 30,000 may be organized as a council-manager city or town.^{19/} There is no special statute governing franchises in municipalities with this form of government. One statute provides, however, that:

A city or town organized under the council-manager plan shall have all the powers which cities of its class have and shall be governed by the statutes applicable to such cities to the extent to which they are appropriate and not in conflict with the provisions specifically applicable to cities organized under the council-manager plan.20/

A final optional form of government is a code city, which results in the broadest powers of local self-government.21/

Code cities have broad authority to grant franchises:

Every code city shall have authority to permit and regulate under such restrictions and conditions as it may set by charter or ordinance and to grant nonexclusive franchises for the use of public streets, bridges or other public ways, structures or places above or below the surface of the ground for railroads and other routes and facilities for public conveyances, for poles, conduits, tunnels, towers and structures, pipes and wires and appurtenances thereof for transmission and distribution of electrical energy, signals and other methods of communication, for gas, steam and liquid fuels, for water, sewer and other private and publicly owned and operated facilities for public service. The power hereby granted shall be in addition to the franchise authority granted by general law to cities.22/

The procedures for granting such franchises are similar to those described for third class cities.23/

6. Counties

Pipeline and wire line franchises upon county roads are granted by the county government:

Any board of county commissioners may grant franchises to persons or private or municipal corporations to use the right of way of county roads in their respective counties for the construction and maintenance

of waterworks, gas pipes, telephone, telegraph, and electric light lines, sewers and any other such facilities.^{24/}

A similar provision pertains to franchises upon county bridges.^{25/} The statute contains extensive requirements concerning public notice of, ~~or~~ hearing upon, any proposed franchise.^{26/} If, after the hearing, the board deems it to be "for the public interest" to grant the franchise in whole or in part, it may make and enter a resolution to that effect.^{27/} The meaning of the phrase "for the public interest" was the subject of one litigated dispute involving a county franchise.^{28/} The power of the county to grant a franchise to an electric cooperative offering service to its members only was contested by a group of local residents and by a privately-owned electric company doing business elsewhere in the county.^{29/} The court held that the phrase "for the public interest" should not be taken to mean "for public use," the phrase associated with enterprises able to exercise the right of eminent domain.^{30/} The degree to which the public interest was benefited by rural electric cooperatives was said to have been an administrative matter for the Board of County Commissioners whose discretion was not to be interfered with by the courts.^{31/}

7. Highway Commission

The State Highway Commission ("Commission") has control over franchises upon state highways. The Commission has the power:

[t]o grant franchises to persons, associations, private or municipal corporations, the United States government or any agency thereof, to use any state highway for the construction and maintenance of water pipes, flume, gas pipes, telephone, telegraph and electric light and power lines and conduits, trams or railways, and any structures or facilities which are part of an urban public transportation system owned or operated by a municipal corporation, agency or department of the state of Washington other than the highway commission, and any other such facilities.^{32/}

Not sooner than fourteen days after compliance with the statute's extensive public notice requirements:^{33/}

...if the highway commission or such persons as it may designate deems it to be for the public interest, the franchise may be granted in whole or in part, with or without hearing under such regulations and conditions as the commission may prescribe, with or without compensation, but not in excess of the reasonable cost for investigating, handling and granting the franchise.^{34/}

There are similar provisions for grants of franchises upon bridges owned or operated by the state jointly with another governmental unit, and for franchises upon toll bridges, toll roads, and toll tunnels.^{35/} The Commission may simply issue a revocable permit rather than grant a franchise in cases of utility construction that extends no more than 300 feet along a state highway.^{36/}

8. Electric Franchises

Washington law has special provisions for grants of electric franchises:

The legislative authority of the city or town having control of any public street or road, or, where such street or road is not within the limits of any incorporated city or town, then the board of county commissioners of the county wherein such road or street is situated, may grant authority for the construction, maintenance and operation of transmission lines for transmitting electric power, together with poles, wires and other appurtenances, upon, over, along and across any such public street or road, and in granting such authority the legislative authority of such city or town, or the board of county commissioners, as the case may be, may prescribe the terms and conditions on which such transmission line and its appurtenances, shall be constructed, maintained and operated upon, over, along and across such road or street, and the grade or elevation at which the same shall be constructed, maintained and operated....^{37/}

The words "[t]he legislative authority of the city or town" in the provision quoted above were once interpreted by the courts to mean that grants of electric franchises by city councils were never subject to referendum.^{38/} In Washington Power Co. v. Rooney, where a Spokane ordinance awarded a privately owned utility both a franchise to furnish steam heat and a franchise to furnish electricity, it was held that the ordinance was void as containing two incongruous subjects. The court reasoned that a city charter provision making all franchise ordinances subject to referendum did not apply to electric franchises by virtue of the statutory phrase "[t]he legislative authority of the city or town."^{40/} "...[W]e will

assume that the power to grant an electric franchise is ...vested exclusively in the mayor and city council, as constituting the legislative authority of the city...[and that] all other franchises for the conduct of business in the city's streets are subject to referendum."^{41/}

The legislature acted quickly to eliminate this apparent anomaly. In 1941 a statute was enacted making electric franchises subject to the same municipal referendum requirement as other franchises where popular referendum is permitted under a city charter.^{42/} The statutory referendum provisions for franchises may be summarized as follows:

- a. First class cities with mayor-council form of government: all franchises are subject to referendum if so provided by city charter. ^{43/}
- b. Cities with commission form of government: all franchises must be approved by referendum. ^{44/}
- c. Electric franchises granted by municipalities: subject to referendum pursuant to general laws of the state or as may be provided by city charter. ^{45/}

Grants of electric franchises by counties are governed by procedures similar to, though not identical with, those governing other county franchises.^{46/}

In Washington Trust & Produce Co. v. City of Yakima, a power company argued that a contract between itself and a city for the furnishing of overhead street lighting service to the city was a franchise to use the streets for general

business purposes.^{47/} No ordinance granting a franchise had been submitted to the voters as required by the city charter and by the statute governing cities with the commission form of government.^{48/} Rejecting the power company's contention, the court explained:

A franchise, in the sense in which we are now considering that term, connotes the right of a public utility to make use of the city streets for the purpose of carrying on the business in which it is generally engaged, that is, of furnishing service to members of the public generally. When, however, a city undertakes, as in this instance, to supply a public need, and to that end purchases the necessary service from the utility, the city is to be regarded as merely authorizing the use of the streets as an incident to the delivery of service to itself, and not as granting a franchise to use the streets for general business purposes.^{49/}

III. CRITERIA TO BE USED IN EVALUATING A FRANCHISE REQUEST

Washington Fruit and Produce Co. v. City of Yakimo

employed the phrase "furnishing service to members of the public generally" to describe the business of a public utility eligible for a franchise.^{50/} Nevertheless, it cannot be said that franchises are limited only to those holding themselves out as ready and willing to serve all members of the public. For example, State ex rel. York v. Board of Commissioners^{51/} held that an electric cooperative offering service to its members only could be granted a franchise by a county. In that case, however, the court based its ruling on the statutory phrase "for the public interest," applicable to county

franchises only, so the court's holding on electric cooperatives may not be controlling for grants by other franchising authorities.^{52/}

Franchises apparently may not be granted for purely private purposes. In another case the Seattle Board of Public Works granted a brewery a permit to construct a railway spur in a street for the purpose of furnishing supplies to the brewery and shipping products therefrom.^{53/} Holding the permit void on the ground that only the city council had the power to grant franchises for use of the streets, the court suggested in dictum that such a grant would have been invalid under any circumstances.^{54/} "The city could not authorize a private corporation to put a railroad track for its own use upon a public street."^{55/}

The franchising statute for second class cities requires that grants be limited to "railroad or other public service purposes."^{56/} No other municipal franchising statutes contain similar wording.

A certificate of public convenience and necessity is not a prerequisite to obtaining a franchise. There is no statutory requirement that the award of a franchise be competitive or go to the highest bidder. There also appears to be no case law on the subject of competitive bidding. The services provided by the franchisee need not meet any specified standards. No other pertinent criteria or franchise qualifi-

cations are delineated in the Washington statutes or case reports.

IV. CHARACTERISTICS OF A FRANCHISE

A. Duration and Termination

It is doubtful that a perpetual franchise may be granted in the state of Washington. The state constitution provides that, "No law granting irrevocably any privilege, franchise or immunity, shall be passed by the legislature."^{57/} Citing this constitutional provision and pertinent franchising statutes, the state attorney general concluded that there was no authority for a third class city to grant a perpetual franchise to a railroad company for tracks and spur lines across city streets and rights-of-way.^{58/} The only express statutory limitations on the period of time for which a franchise may be granted are those pertaining to county and Commission franchises. Such grants may not exceed a term of fifty years.^{59/} There are no judicial decisions on the maximum duration of a franchise.

The statutes enumerate no conditions that will result in the automatic surrender of a franchise. A franchise may be forfeited by a failure of the grantee to perform the terms stipulated in a bond it executed in accepting the grant. In one case a town granted an electric franchise requiring the grantees to contract to furnish lights to the city at not over certain maximum rates.^{60/} The assignees of

the original grantee executed a bond to perform within a one-year period the obligations of the franchise ordinance, but wholly failed to construct the electric lines called for or to furnish any lighting as required.^{61/} In holding the defendants liable under the bond, the court explained:

Furth and Brown had not only failed to perform their obligations under the franchise ordinance within the time therein specified, but it is also manifested that they were not in a position at that time to do so, and had no intention of doing so. In other words, they had abandoned all their rights and repudiated all their obligations thereunder. Clearly the town had the right to treat the franchise contract as abandoned....^{62/}

In another case the court struck down two municipal ordinances that reduced by 85 to 90 percent the franchised area of an established utility.^{63/} In 1916 the town of Tukwila granted a privately owned electric utility a 50-year franchise^{64/} for sale of electricity within the town's geographic limits. In 1958 Tukwila awarded Seattle City Light, owned by the City of Seattle, a similar franchise, neither being exclusive of the other.^{65/} Apparently the prospect of competition arose when Tukwila annexed an area contemplated for industrial and commercial use.^{66/} For reasons not made entirely clear in the trial record, but ostensibly to assure greater safety to its residents, Tukwila enacted ordinances that exclusively allotted 10 to 15 percent of Tukwila's area to Seattle City

Light and 85 to 90 percent to the private utility.^{67/} The court rejected Tukwila's contention that legitimate police power was an adequate basis for impairing Seattle City Light's franchise where there was "no rational connection between the end to be achieved and the regulations by which it is sought to be accomplished."^{68/} Invoking contract principles, the court declared:

...[T]he enactment and enforcement of Tukwila's ordinances Nos. 353 and 364 limiting Seattle in the exercise of its electrical franchises to a part of the city's area constituted an unwarranted and unconstitutional impairment of Seattle's franchise and one not to be countenanced as an exercise of the police power to protect the citizenry from the dangers of electrical transmission and distribution.^{69/}

There seem to be no cases on the issue of whether a franchise may be forced to remove its facilities and to cease providing service if its franchise expires or is terminated. However, a statute does grant authority to the highway commissioner to require removal of facilities constructed under grants of franchise if "necessary for the construction, alteration, repair or improvement of the highway."^{70/}

B. Exclusivity

Grants of exclusive franchise privileges for the use of public streets and highways are expressly prohibited in the statutes applying to second class cities, counties, and the Commission.^{71/} The other franchising statutes are silent on the question whether there may be an exclusive franchise.

There is one judicial decision indicating that franchises will be strictly construed as not granting exclusive franchises in the absence of clear language to the contrary. Where the mayor of a town refused to sign an ordinance granting a franchise to erect and maintain an electric light and power plant therein on the ground that a franchise had been previously granted to another person, the mayor was found to be unjustified in his refusal, it not appearing that the previous franchise was exclusive. ^{72/}

C. Other Characteristics

The particular utility services that may be franchised are described with varying degrees of specificity in each franchising statute cited above. There is no mandatory franchise tax that must be paid to the municipality to comply with any statute. Abandonment of a franchise is not provided for by the statutes, though abandonment was an issue in a case mentioned above. ^{73/} There are no decisions on the question of whether a municipality can preclude the operation of a utility authorized by the Utilities and Transportation Commission to provide service if the utility does not obtain or have a franchise. In the absence of specific language in the franchise ordinance declaring the grant to be that of an exclusive franchise, there appears to be no bar to issuance of a second franchise for the same service in that community. ^{74/}

FOOTNOTES

1. Wash. Rev. Code Ann. §§36.55.010- .080, 47.44.040 (West 1964);
§§35.22.280(7), 35.23.440(39), 35.24.290(10),
35.27.370(12), 47.44.010, -.020, (West Supp. 1980).
2. Id. §47.44.010 (West Supp. 1980).
3. Id. §35.22.280(7).
4. Id. §35.24.290(10).
5. Id. §35.23.440(39).
6. Id. §36.55.050 (West 1964).
7. Id. §35.22.280(7) (West Supp. 1980).
8. Id. §35.22.200 (West 1965).
9. Id. §35.23.440(39) (West Supp. 1980).
10. Id. §35.23.390 (West 1965).
11. Id. §35.23.400.
12. Id. §35.24.290(10) (West Supp. 1980).
13. Id. §35.24.250 (West 1965).
14. Id. §35.01.040.
15. Id. §35.27.370(12) (West Supp. 1980).
16. Id. §35.27.330 (West 1965).
17. Id. §35.17.370.
18. Id. §35.17.220.
19. Id. §35.18.230.
20. Id. §35.18.030.
21. Id. §35A.01.010 (West Supp. 1980).
22. Id. §35A.47.040.
23. Ibid.
24. Id. §36.55.010 (West 1964).

25. Id. §36.55.030.
26. Id. §36.55.040.
27. Id. §36.55.050.
28. State ex rel. York v. Board of Comm'rs, 28 Wash.2d 891, 184 P.2d 577 (1947).
29. Id. 184 P.2d at 580-81.
30. Id. 184 P.2d at 583.
31. Ibid.
32. Wash. Rev. Code Ann. §47.44.010 (West Supp. 1980).
34. Id. §47.44.020.
35. Id. §§47.44.040, 47.56.256 (West 1970).
36. Id. §47.44.050.
37. Id. §80.32.010 (West 1962).
38. Washington Water Power Co. v. Rooney, 3 Wash.2d 642, 101 P.2d 580 (1940).
39. Id. 101 P.2d at 583.
40. Id. 101 P.2d at 582.
41. Id. 101 P.2d at 582-83.
42. Wash. Rev. Code Ann. §80.32.040 (West 1962).
43. Id. §35.22.200 (West 1965); §80.32.040 (West 1962).
44. Id. §35.17.220 (West 1965).
45. Id. §80.32.040 (West 1962).
46. Id. §80.32.010.
47. Washington Fruit & Produce Co. v. City of Yakima, 3 Wash.2d 152, 100 P.2d 8 (1940).
48. Id. 100 P.2d at 10-11.
49. Id. 100 P.2d at 11-12.
50. Ibid.

51. State ex rel. York v. Board of Commrs., 28 Wash.2d 891, 184 P.2d 577 (1947).
52. Id. 184 P.2d at 583.
53. Schwede v. Hemrich Bros. Brewing Co., 29 Wash. 21, 69 P. 362 (1902).
54. Id. 69 P. at 365.
55. Ibid.
56. Wash. Rev. Code Ann. §35.23.440(39) (West Supp. 1980) (emphasis added).
57. Wash. Const. art. 1, §8.
58. Op. Att'y Gen. No 32 (Wash 1968).
59. Wash. Rev. Code Ann. §§36.55.060(2) (1964), 47.44.020 (West Supp. 1980).
60. Town of Castle Rock v. Furth, 78 Wash. 47, 138 P. 317 (1914).
61. Id. 138 P. at 318.
62. Ibid.
63. City of Tukwila v. City of Seattle, 68 Wash.2d 611, 414 P.2d 597 (1966).
64. Id. 414 P.2d at 598.
65. Ibid.
66. Ibid.
67. Ibid.
68. Id. 414 P.2d at 600.
69. Id. 414 P.2d at 599.
70. Wash. Rev. Code Ann. §47.44.020 (West Supp. 1980).
71. Id. §§35.23.380 (West 1965), 36.55.060(3) (West 1964), 47.44.020 (West Supp. 1980).
72. State ex rel. Prosser Falls Land & Irrigation Co. v. Taylor, 36 Wash. 607, 79 P. 286, 287 (1905).

73. Town of Castle Rock v. Furth, 78 Wash. 47, 138 P. 317 (1914).
74. State ex rel. Prosser Falls Land & Irrigation Co. v. Taylor, 36 Wash. 607, 79 P. 286, 287 (1905).

CHAPTER 5

RATE REGULATION IN WASHINGTON

I. RATEMAKING AUTHORITY

The Washington Utilities and Transportation Commission (Commission) has statutory power to review and fix the rates and charges of utilities.^{1/} As explained in Chapter 2, the Commission has rate jurisdiction over investor-owned utilities, but not over cooperative or publicly-owned utilities. The statute requires that thirty days' notice be given to the Commission and to the public for a rate change to be approved.^{2/} The Commission may schedule hearings on the reasonableness of existing rates or proposed changes in rates,^{3/} and, pending a hearing may suspend the effective date of proposed rates for a period of up to ten months.^{4/}

While the Public Utilities Act sets forth the notice which must be given to the Commission and the public when a change or an increase in rates is proposed, the Act does not require the filing of supporting data.^{5/} However, administrative regulations describe in detail what data must be filed with the Commission.^{6/}

The statutes and administrative rules do not contain any provisions governing the disposition of significant issues that are likely to arise in a rate case, other than to provide that the Commission has the authority to determine the fair value of a utility property which is used and useful in the provision of public service.^{7/} In interpreting

this provision the Supreme Court of Washington has held that the Commission may use any lawful method or combination of methods to value utility property.^{8/} There is a provision that if a utility earns an excessive rate or return for five consecutive years immediately prior to a rate order, the Commission shall take official notice of whether the excess earnings have been invested in the company's plant or otherwise used for purposes beneficial to the companies customers and may consider such facts in fixing rates.^{9/}

The Commission has statutory authority to prescribe a uniform system of accounts and the manner in which such accounts shall be kept^{10/} and has prescribed the National Association of Regulatory Utility Commissioners (NARUC)^{11/} system of accounts for electric and gas utilities. The Commission has adopted a few minor changes to the NARUC^{12/} system that are outlined in administrative regulations. The Commission has been given authority, after hearings, to fix proper and adequate rates of depreciation for each utility, but there appear to be no reported judicial or administrative cases dealing with the Commission's authority^{13/} over depreciation accrual rates or accounting matters.

II. RATE BASE DETERMINATION

A. Test Period

The Commission has in the past, consistently adhered to the use of an historical test period, using the "average of monthly averages" to calculate rate base.^{14/}

Moreover, the Commission has indicated that it will continue

its practice of using an historical test period in future cases.

The Commission is of the opinion that an historical test year properly restated and proformed, using an average of monthly averages in calculating rate base continues to be a reliable and consistent basis for establishing rates in electric and other utility cases. 15/

Although the Commission denied Washington Power Company's request to measure rate base at year end, the Commission did permit inclusion of twenty items on a pro forma basis, which had been placed in service prior to the end of the test year, including transmission line rebuilds, fuse replacements, and installation of protective fencing. The staff had contended that the items should be permitted in the rate base only as of the date of service because their installation resulted in increased reliability which in turn would increase revenues. The Commission rejected the staff recommendation, holding that the items were of a "non-revenue" nature and should be proformed into the rate base. 16/

B. Rate Base Valuation

The Washington Code provides:

The Commission shall have the power upon complaint or upon its own motion to ascertain and determine the fair value for ratemaking purposes of any public service company used and useful for service in this state 17/

While the Commission is free to follow any lawful method or combination of methods of rate base valuation, 18/ in recently reported decisions, the Commission, "in determining the fair value to be ascribed to a utility's property and service

(rate base) . . . has measured rate base according to net average original cost established during an actual operating period"^{19/}

C. Rate Base Components and Adjustments

Utility property must be "used or useful" in the public service, to be included in the rate base.^{20/} Recently reported decisions have not dealt with the treatment of investment in facilities not devoted to utility service subject to agency jurisdiction. However, one Washington utility maintains joint operations which are provided from a single facility. The company's gas and electric operations are regulated, but its steam operations are not. The Commission excludes the company's investment in steam facilities from rate base.^{21/}

Traditionally, the Commission has excluded construction work in progress (CWIP) from the rate base, holding that only those items which are actually in operation are considered used or useful in the provision of service.^{22/} However, recent case law indicates a departure from the strict rule of exclusion of CWIP. In 1974 the Commission staff undertook a study to evaluate the impact of CWIP on various utilities over a ten year period. The results of that study indicated that while CWIP was a minor element in terms of percentage of net plant for gas and telephone utilities, the three largest electric companies operating in the state had experienced a dramatic rise in CWIP as a percentage of net plant. This "dramatic rise" was found

to be largely attributable to increases in electrical consumption which had forced electric utilities to undertake substantial investment in the development of thermal generating facilities.^{23/} In light of this study, the Commission has included CWIP in rate base for major long term projects related to power production facilities in several recent rate cases.^{24/}

There are two caveats to this departure from the general rule. First, the Commission maintains that its inclusion of CWIP in electric power cases cannot be advanced "as a persuasive precedent in cases other than those involving electric utilities and then only as to those wherein it is demonstrated that construction work in progress is shown to represent a dramatic, increasing percentage of net utility plant."^{25/} Thus, the Commission excluded CWIP from rate base in two recent telephone utility cases.^{26/} Second, the inclusion of CWIP is offset by adding to actual operating income the test year accrual of allowance for funds used during construction (AFUDC).^{27/} Therefore, where the Commission includes CWIP in rate base, the company will experience a cash flow benefit to the extent that its allowable rate of return is higher than the rate at which the company accrues AFUDC.

Recently, Pacific Power and Light sought to include in its rate base an electric generating facility which was under construction during the test year, but was transferred to another party after the end of the test year. Evidently, the property was transferred to a third party because of

the inability of the company to take advantage of the investment tax credit associated with the unit. The company had planned to lease back the unit, at a reduced rate to reflect the benefits obtained from the investment tax credit. The Commission commended the company's innovative financing arrangement, but excluded the item from rate base treatment. The Commission held, that its "intent in measuring the company's rate base is to determine the fair value of respondent's property, not to determine the fair value of property which may at some time produce the commodity respondent sells to its customers."^{28/}

D. Rate Base Allocation

There are no reported decisions wherein the Commission has discussed methods of allocation of rate base to different services provided by a single facility. Moreover, the Commission has not prescribed any particular method of rate base allocation.^{29/}

III. COST OF SERVICE

A. Allowed or Disallowed Expenses

The Commission has not stated a general test for what expenses may be included in the cost of service but does use, as a starting point, the revenue and expense recorded on a company's books. As far as charitable contributions and membership dues are concerned, the Commission has historically excluded such items as expenses which should be borne by the owners of a utility company rather than by its ratepayers.^{30/} However, the Commission recently

allowed Pacific Northwest Bell Telephone Company to include charitable contributions in its cost of service for the reason that: "[t]he time has come for the commission to recognize the validity of this socially appropriate, indeed mandatory company expense".^{31/} The Commission observed that all businesses are expected to support charitable organizations and that such expenses are necessarily reflected in prices charged for goods. Thus, it held that "charitable contributions are a necessary cost of doing business and are proper and reasonable in this case" ^{32/} In the future, such expenditures will be examined to determine their "propriety and reasonableness," as an expense item.^{33/}

The Commission has shown less receptiveness to advertising. For example, in one case the Commission held that an allowance for promotional advertising was improper, especially in light of its authorization of an energy conservation surcharge. Only those advertising expenses which were "directly related to the conservation of electric energy, or directing use thereof to off-peak periods" were allowed.^{34/}

In a 1975 case, the Commission, over staff objection, allowed an expenditure for first aid training. The Commission held that such expenses should be recognized as recurring in nature, due to a state ruling which required such training every three years, and concluded that one-third of the expense should be included in the test year cost of service.^{35/} In the same case, the staff had totally disallowed an expendi-

ture for waterproofing manholes and for repairing storm damage, as non-recurring and extraordinary. The Commission, rather than disallow the entire expenditure, elected to analyze its extraordinariness by a "parameter methodology." Essentially, extraordinary was defined as being "substantially in excess of any maintenance expense for a like period incurred over a 5-1/2 year period," with an adjustment to take into account the marked increase in inflationary costs during the test period.^{36/}

In addition to the above generally contested items of expense, it should be noted that the Commission has statutory authority to disallow payments to affiliated interests which are not reasonable.^{37/} In 1973 the Washington Supreme Court affirmed a Commission decision to use a "cost plus fair return" approach (i.e., the cost to the affiliate of providing services plus a fair return on investment, to the affiliate, as determined by reference to the earnings of comparable companies) in order to judge the reasonableness of affiliated transactions.^{38/}

B. Allocation of Expenses

The Commission has not specified any particular methods of expense allocation. Moreover, the issue of allocation is currently the subject of a generic hearing on electric rates the results of which will not be available before mid 1980.^{39/}

IV. FEDERAL INCOME TAX ISSUES

A. Liberalized Depreciation

The Commission has shown a definite preference for the flow-through method for treatment of depreciation expense for federal income tax purposes. It appears that the Commission will only permit normalization where it is barred from requiring flow-through under the federal tax laws. Thus, the Commission advised Pacific Northwest Bell that:

The company should be put on notice that any future use of liberalized depreciation on a normalized basis will be subject to immediate flow-through if permissible under the tax laws.
40/

The Commission has repeatedly denied company requests to switch from flow-through to normalization of liberalized depreciation. In a 1974 case a company which had previously not elected normalization under the 1969 Tax Reform Act, made a request to switch from flow-through to normalization. The Commission required the company to flow-through its deferred income taxes for rate making purposes.^{41/} In a subsequent case, the Commission again denied a company's request to switch from flow-through to normalization, observing that:

We adhere to our past policy statement and decisions accepting flow-through as the preferred method of treating deferred taxes and continue to recognize actual taxes paid. 42/

In sum, it appears that the Commission will permit normalization of liberalized depreciation where the company has made an election under the 1969 Tax Reform Act which

prohibits flow-through. According to an Argus Utility Scope report, dated March 1978, the state's largest telephone utilities follow normalization accounting, whereas, all major energy utilities flow-through liberalized depreciation. ^{43/}

B. Investment Tax Credits

The Commission's treatment of investment tax credits is similar to that of liberalized depreciation. Where a utility has previously elected to normalize its investment tax credits pursuant to federal tax law, the Commission has accepted normalization. However, where the company has previously elected to flow-through investment tax credits, the Commission has denied requests to switch to normalization, noting:

We recognize that we are not legally precluded from allowing normalization for rate-making purposes, but we remain firmly convinced, as we have previously stated, that Washington rate-payers are entitled to investment tax credit benefits on plant included in the Washington rate base. ^{44/}

In denying a request to switch to normalization, the Commission specifically rejected the argument that circumstances in 1978 were different than those in 1971, when the company made the election to flow-through. ^{45/}

There have been no recent decisions concerning the expansion of normalization beyond liberalized depreciation and investment tax credits. However, in view of the Commission's obvious preference for flow-through over normalization, it is doubtful that the Commission would permit full normalization of all tax timing differences.

V. METHODS USED FOR DETERMINING THE RETURN TO BE ALLOWED
A REGULATED UTILITY

A. Return on Equity

The Commission has been consistent in its use of the discounted cash flow method (DCF) of determining an allowable return on equity.

We again reaffirm our belief, based upon extensive regulatory experience and careful consideration of alternative approaches, that the discounted cash-flow analytical approach represents the most satisfactory and exact method of determining demands and expectations of a hypothetical investor in return for his investment in utility equity.
46/

In rejecting a company's use of the comparable earnings' approach to determine return on equity, the Commission noted that the "comparable earnings test is not wrong in principle," but in fact would be a useful tool if similarity of risk is established.
47/

The Commission has specifically rejected the setting of a spread between the cost of debt and the return on equity as determinative of the cost of equity.
48/

The table in Appendix A lists the overall return and return on equity allowed in recent rate cases.

B. Risk Factors

The Commission has not enunciated any risk factors which would justify awarding a higher than normal rate of return. However, in one case, where the staff's DCF analysis indicated that the return on equity required by investors was in the range of 11.5% - 11.75%, the staff recommended a 12.50% return on equity "to protect the investor against

short term market fluctuations and the combined effects of financing costs and 'pressure' associated with the sale of new equity capital."^{49/} The staff witness rejected any higher return than 12.5%, pointing to the "recent short-term strength in utility stocks."^{50/} The Commission held that the projection of recent strength into the entire period over which the rates were to be effective was sufficiently conjectured to warrant a 12.75% return on equity.

The Commission has not made allowances in rate of return to provide an incentive to utilities which do certain things. However, in one case where the Commission found that the appropriate rate of return should be within the range of 9.85-9.97%, it awarded a 9.85% return "in recognition of the serious service deficiencies of the company."^{51/}

VI. RATE DESIGN CRITERIA

The Commission has given little indication as to what criteria it uses to set rates to customers. It is clear, however, that the Commission has made moves to a more flattened rate structure in an effort to promote energy conservation. In a 1977 rate case the Commission commented that "[a]ll reasonable efforts must be exploited to achieve conservation of the national energy resource by reducing our demand for energy."^{52/} Thus, the Commission approved of a company's proposal to eliminate 17 rate schedules in a step toward leveling rates and suggested that the company's refileing should "be so structured that its charges for successive blocks of demand and energy reflect greater or at

least no lesser percentage increases than apply to the preceding block."^{53/} In addition to approving a more flattened rate structure, the Commission required the company to impose a 5% conservation surcharge on all electric power delivered pursuant to commercial and industrial tariffs for the winter peak demand period.^{54/}

The Commission's move to flattened rate structures is apparent in other cases as well. Thus, where a utility had proposed that the rate increase be allocated on a uniform percentage basis among all of its customers, the staff contended that a uniform cents per kilowatt charge coupled with an "appropriate" basic charge, minimum charge and demand charge was the more equitable way of spreading the burden of the increase. The Commission adopted the staff's recommendation stating that it was "consistent with the Commission's treatment of recent increases granted other Washington electric utilities and . . . places a smaller burden on the residential rate payer."^{55/}

On January 25, 1978 the Commission ordered an investigation which would culminate in a hearing on electric rates structures. The investigation is directed at considering the feasibility of "time-of-day rates, seasonal rates, cost-of-service pricing, including marginal cost pricing, interruptible rates and load management techniques, modification or elimination of declining block rates and such other modifications to rate design and rate structure, as would reasonably tend to encourage and accomplish more

efficient utilization and conservation of existing and potential resources and capital of electric companies and result in equitable rates to consumers."^{56/}

Lifeline rates are not presently mandated by statute. However, the Commission has indicated its receptiveness to such rates in its orders concerning Pacific Northwest Bell Telephone Company. In a 1975 case the Commission noted that in a previous order, it had directed the company to determine the feasibility of lifeline rates, which had resulted in an experimental exchange service, "providing for a relatively low flat rate 2-party service with ten free outgoing calls per month."^{57/} In the instant case, the Commission directed that this experiment be extended an additional year. In addition, no increase in basic flat rate local exchange service was provided in order to ease "the burden on our low income citizens and indeed all residential consumers."^{58/} The Commission noted that any additional provision for the low-income elderly or handicapped should come from the legislature.^{59/}

Only one recently reported Commission decision has dealt with value of service. The staff and telephone company disagreed on the amount of revenue that would be generated from the company's message toll service. The difference was accounted for by the company's assumption of the price elasticity effect of "reclassification, repression, and suppression." In short, the company argued that as prices for message toll service increased, customer usage

decreased or shifted to a lower price service (i.e., operator assisted to direct). The Commission acknowledged the presence of elasticity of demand, but maintained that there was no adequate way to measure its effect. The Commission held that the company's evidence of revenue erosion due to the elasticity of demand was inadequate. It found the message toll rates would generate revenue which would be more than adequate to meet the revenues deficiency from local service rates and denied the requested rate relief.^{60/}

Recently reported Commission decisions have not dealt with the pricing of excess power generated by a utility or other generator or the pricing of by-product services resulting from electrical or thermal generation. However, the Commission has never required a utility to purchase energy from another generator.^{61/}

VII. ISSUANCE OF SECURITIES

The Commission has authority to control the issuance of securities by utilities.^{62/} There appear to be no reported cases delineating standards applied by the Commission in determining whether to approve issuance of securities. In addition, pursuant to statute, an intrastate utility cannot pay dividend in its common stocks until: 1) its earnings and earned surplus, after provision for reasonable reserves, are sufficient; and, 2) the dividend can be paid without impuning the ability of the utility to render reasonable service at reasonable rates. A utility must first obtain approval of the Commission before any common stock dividend is paid.^{63/}

As for preferred capital structures, the Commission approved debt ratios of 56.6 percent and 62.56 percent in two recent electric utility ratemaking cases, but it gave no express reason for its conclusions.^{64/} The Washington Superior Court has held that the Commission has the authority to use a hypothetical capital structure, "when it finds from the evidence that the existing capital structure is so unreasonable as to impose an unfair burden on the consumer."^{65/} Thus, in one case, the Commission declined to use the company recommended debt ratio of 45%, holding that an equal ratio of 50% debt was the most "appropriate and reasonable structure for this ratemaking proceeding, a ratio . . . which based upon the evidence before us does not suffer the consumer to pay higher rates than necessary in order to provide the company the margin of safety necessary to prudent management."^{66/}

APPENDIX A

<u>CASE</u>	<u>ALLOWED % RATE OF RETURN</u>	
	<u>OVERALL</u>	<u>ON COMMON EQUITY</u>
<u>Washington Nat. Gas Co.</u>		
Cause No. U-78-38 (1979)	9.91	13.25
23 P.U.R.4th 184 (1977)	9.89	13.25
<u>Puget Sound Power & Light Co.</u>		
Cause No. U-78-21 (1979)	9.8	13.00
Cause No. U-76-1 (1976)	9.25	13.00
<u>Washington Water Power Co.</u>		
24 P.U.R.4th 427 (1978)	9.00	12.75
18 P.U.R.4th 154 (1976)	8.57	12.75
<u>Pacific Northwest Bell Tel. Co.</u>		
Cause No. U-77-87 (1978)	9.7	12.00
<u>Pacific Power & Light Co.</u>		
18 P.U.R.4th 316 (1976)	9.7	13.00
<u>Continental Telephone of the N.W., Inc.</u>		
14 P.U.R.4th 276 (1976)	9.85	13.3-13.6

FOOTNOTES

1. Wash. Rev. Code Ann. §80.28.020 (West 1962).
2. Id. §80.28.060.
3. Id. §80.28.020.
4. Id. §80.04.130.
5. Id. §§80.28.50, .060.
6. Wash. Admin. Code §480-80 (1969).
7. Wash. Rev. Code Ann. §80.04.250 (West 1962).
8. State ex rel Pacific Tel. & Tel. Co. v. Dept. of Pub. Serv., 19 Wash. 2d 200, 142 P.2d, 498 (1943).
9. Wash. Rev. Code Ann. §80.04.360 (West 1962).
10. Id. §80.04.080.
11. Wash. Admin. Code §§480-90-031, -100-031 (1976).
12. Ibid., Mr. D.C. McLean, Chief, Finance & Accounts Div., Commission, Telephone conversation, 9/26/78.
13. Wash. Rev. Code Ann. §80.04.350 (West 1962).
14. WUTC v. Washington Power Co., 18 P.U.R.4th 131,134 (1976).
15. Id. at 135.
16. Ibid.
17. Wash. Rev. Code Ann. §80.04.250 (West 1962).
18. State ex rel Pacific Tel. & Tel. v. Dept. of Pub. Serv., 19 Wash. 2d 200, 142 P.2d 498 (1943).
19. WUTC v. Pacific Power & Light Co., 18 P.U.R.4th 316, 318 (1976).
20. Wash. Rev. Code Ann. §80.04.250 (West 1962).
21. Mr. D.C. McLean, Chief, Finance & Accounts Div., Commission, Telephone conversation, 7/16/79.
22. WUTC v. Washington Power Co., 24 P.U.R.4th 427, 433 (1978).
23. WUTC v. Pacific Power & Light Co., 10 P.U.R.4th 449 (1975).

24. See e.g. WUTC v. Washington Water Power Co., 24 P.U.R. 4th 427 (1978); WUTC v. Pacific Power & Light Co., 10 P.U.R.4th 449 (1975).
25. WUTC v. Pacific Power & Light Co., 10 P.U.R.4th 449, 453 (1975).
26. WUTC v. Pacific N.W. Bell Tel. Co., 14 P.U.R.4th 422 (1976); WUTC v. Continental Tel. Co. of the N.W., Inc., 14 P.U.R.4th 276 (1976).
27. WUTC v. Pacific Power & Light Co., 10 P.U.R.4th 449, 453 (1975).
28. WUTC v. Pacific Power & Light Co., 18 P.U.R.4th 317 (1976).
29. Mr. D.C. McLean, Chief, Finance & Accounts Div., Commission, Telephone conversation, 7/16/79.
30. See, e.g., WUTC v. Pacific N.W. Bell Tel. Co., 93 P.U.R.3d 275, 291 (1971); WUTC v. Pacific N.W. Bell Tel. Co., 81 P.U.R.3d 371, 383 (1969).
31. WUTC v. Pacific N.W. Bell Tel. Co., 14 P.U.R.4th 422 (1976).
32. Id. at 428.
33. Id. at 429.
34. WUTC v. Pacific Power & Light Co., 7 P.U.R.4th 470, 488 (1974).
35. WUTC v. Pacific N.W. Bell Tel. Co., 9 P.U.R.4th 63 (1975).
36. Id. at 75.
37. Wash. Rev. Code Ann. §80.16.030 (West 1962).
38. Washington ex rel. General Tel. Co. of the N.W., Inc. v. WUTC, 100 P.U.R.3rd 453, 459 (1973).
39. Mr. D.C. McLean, Chief, Finance & Accounts Div., Commission, Telephone conversation, 7/16/79.
40. WUTC v. Pacific N.W. Bell Tel. Co., 81 P.U.R.3d 371, 387, (1969).
41. WUTC v. Pacific Power and Light Co., 7 P.U.R.4th 470 (1974).

42. WUTC v. Continental Tel. Co. of the N.W., 14 P.U.R.4th 276, 283 (1976).
43. Argus Utility Scope Regulatory Service, March 1978, p. 7.
44. WUTC v. Washington Water Power Co., 24 P.U.R.4th 427, 458 (1978).
45. Id. at 458.
46. Id. at 444.
47. WUTC v. Pacific N.W. Bell Tel. Co., 81 P.U.R.3d 371, 381 (1969).
48. WUTC v. Pacific Power & Light Co., 18 P.U.R.4th 316 324 (1976).
49. WUTC v. Washington Water Power Co., 24 P.U.R.4th 427, 445 (1978).
50. Id. at 445.
51. WUTC v. Continental Tel. of the N.W., Inc., 14 P.U.R.4th 276, 285 (1976).
52. WUTC v. Puget Sound Power & Light Co., 7 P.U.R.4th 44, 62 (1977).
53. Id. at 62-63.
54. Id. at 63.
55. WUTC v. Washington Water Power Co., 18 P.U.R.4th 131, 149 (1976).
56. Argus Utility Scope Regulatory Service, March 1978, pp. 8-9.
57. WUTC v. Pacific N.W. Bell Tel. Co., 9 P.U.R.4th 63, 80 (1975).
58. Ibid.
59. Id. at 81.
60. WUTC v. Pacific N.W. Bell Tel. Co., 9 P.U.R.4th 63 (1975).
61. Mr. D.C. McLean, Chief, Finance & Accounts Div., Commission, Telephone conversation, 7/16/79.
62. Wash. Rev. Code Ann. §80.08.040 (West 1962).

63. Id. §80.04.340.
64. WUTC v. Pacific Power & Light Co., 18 P.U.R.4th 316, 323 (1976); WUTC v. Washington Water Power Co., 18 P.U.R.4th 131, 139-40 (1976).
65. Pacific N.W. Bell Tel. Co. v. WUTC, 98 P.U.R.3d 16 (1972).
66. WUTC v. Pacific N.W. Bell Tel. Co., 14 P.U.R.422, 432-433 (1976).

CHAPTER 6

SUMMARY OF IMPEDIMENTS TO IMPLEMENTATION OF ICES

I. Types of Impediments

In order to analyze the extent to which the traditional public utility regulatory system may impede the implementation of ICES, one must first identify what is meant by the word "impediment." For the purposes of this analysis, four broad types of impediments can be identified. The first major category of impediment is the "no-subsidy impediment." This impediment consists of the failure of the government or the regulatory system to provide some desired degree of monetary or other encouragement of ICES. Such subsidies could take the form of grants or tax incentives. On the other hand, a subsidy could result from state public utility regulatory commission (PUC) departure from strictly cost-based rates for purchases and sales of electricity between an ICES and conventional electric utilities, thereby compelling the customers of the electric utility grid to subsidize ICES.

The second major category of impediment is the "uncertainty impediment." The absence of certainty with respect to the manner in which an ICES will be regulated will impose costs that must be borne by the ICES operator. Uncertainty impediments will appear in many forms. ICES will be faced with uncertainty because it represents a new concept which can be

expected to raise issues with which utility regulators are unfamiliar. Such uncertainties will be aggravated as a result of the fact that regulatory jurisdiction in the United States is decentralized. Thus, these uncertainties will have to be resolved largely on a jurisdiction-by-jurisdiction basis. In addition, ICES will necessarily be involved in the sale of excess electrical power to and the purchase of back-up electrical power from conventional electric utilities. These arrangements, however, can be altered by a PUC even though the ICES and utility initially agreed upon the terms. Therefore, ICES will face transactional uncertainties not normally encountered in doing business outside the utility field.

Another major category of impediment is the "discriminatory impediment." This type of impediment takes the form of rules or regulations which, for whatever reasons, affect ICES more harshly than competing energy technologies. These differences in impact may be the result of any number of factors including, but not limited to, ICES size, the type of customers it can be expected to serve and the manner in which it will do business.

The final general category of impediment is the "prohibition impediment." These impediments could be either regulations which impose so substantial a cost on the ICES that it cannot operate economically or regulations which would actually preclude operation of an ICES.

II. Regulatory Impediments to ICES Implementation

The degree and manner in which the existing regulatory system will impede the development of ICES will vary depending on the form of ownership, class of customer and method of doing business chosen by an ICES developer. The ICES type which can be expected to encounter the most serious impediments is the investor-owned ICES seeking to construct a new facility to serve customers in a community already being served by a conventional utility. Such an ICES will face impediments in the form of general PUC regulation, regulations relating to the siting of facilities and the granting of local franchise and regulations concerning rates charged for energy service.

A. General Regulatory Impediments

Public utility regulation probably is more pervasive and complex than any other form of government regulation of business. A businessman not engaged in the utility business may be reluctant to become involved in a business which will subject him to such pervasive governmental regulation. Some examples of areas of regulation which might discourage investors from becoming involved in ICES implementation are the requirement that a regulated utility maintain its books in conformity with a system of accounts prescribed by the PUC and PUC regulation and scrutiny of the financial affairs of the utility. When the ICES is operated in conjunction with a non-utility business, such regulation necessarily will extend beyond the operator's utility operations and involve PUC examination of

its non-utility business. Attempts at minimizing the effects of these types of impediments by setting up a subsidiary corporation to own and operate the ICES could subject the parent company to extensive Securities and Exchange Commission regulation pursuant to the Public Utility Holding Company Act of 1933.

Even if an ICES developer is willing to face the possibility of extensive PUC regulation, it will face a significant uncertainty in determining whether it will be deemed a public utility and therefore subject to PUC regulation. All states require that a utility provide service "to or for the public" before it becomes subject to the jurisdiction of the PUC. Few states, however, have provided any real guidance with respect to the meaning of the phrase "to or for the public." Thus, an ICES operator can expect very little guidance in determining whether its operations will be sufficient to bring it within the classification of "public utility."

Similarly, many states require that a utility "sell" utility service before it will be classified as a public utility. Again, statutes, administrative rules and caselaw provide very little guidance with respect to when a transaction will be classified as a "sale." Thus, the ICES operator must face another significant area of uncertainty with respect to PUC regulation of its operations.

Assuming that some aspects of the ICES operations will bring it within the classification of public utility, a

serious question remains with respect to whether sales of both of the ICES energy streams will be subject to PUC regulation and, if not, whether and by whom the non-PUC regulated energy stream will be regulated. This uncertainty arises because many state statutory schemes provide for the regulation of only certain enumerated utility services such as heat, electricity and gas. In such states, the provisions of refrigeration or motive power may not be within PUC jurisdiction. Regardless of whether these energy streams will be regulated by local governments, or left unregulated, such split regulation may raise significant problems with respect to the marketing of both energy streams at competitive rates.

State territorial assignment programs could present an impediment capable of precluding operation by ICES. Several states have enacted legislation which specifically provides that the PUC is to divide the state into a finite number of service areas and assign each of these service areas exclusively to a particular utility. Where such programs exist, service area assignments have been made and, generally, these programs make no provision for the assignment of service areas to new utilities unless there is some indication that customers are not being adequately served. Even where no specific statutory allocation scheme exists, PUCs generally have sought in granting certificates of public convenience and necessity to avoid what they viewed as wasteful duplication of facilities by granting the first utility serving a given area in effect an exclusive

right to serve that area so long as the utility provides adequate service. Thus, in many cases, an ICES may find that it is precluded from initiating operations as a result of these territorial assignment programs.

B. Siting Impediments

The siting of energy production facilities is regulated in some manner in all states. The types and degree of impediments presented will vary depending on the type of siting program in effect in a particular jurisdiction and the type of facility proposed to be constructed. In those states which have not adopted comprehensive one-stop siting programs, a utility desiring to construct an energy production facility generally must seek approval from a variety of state and local agencies. Because an ICES developer in such a state will be forced to obtain numerous approvals, the procedural requirements related to obtaining such multiple approvals could present significant impediments to the implementation of ICES. In those states which have attempted to minimize the procedural difficulties presented by the need to obtain multiple approvals by implementing one-stop comprehensive siting programs, an ICES operator may face significant impediments in the form of substantive requirements in obtaining the required approval.

C. Local Franchising Impediments

In addition to obtaining certificates of convenience and necessity from PUCs and siting approvals from one or more state agencies, ICES operators generally will be required to

obtain franchises from local governments to use public rights-of-way for transmission and distribution facilities. Because of the total lack of uniformity in the law and procedures governing local franchising, ICES operators will face many uncertainties in this area. One major uncertainty related to whether a franchise is needed or available and, if a franchise is not available, whether this will preclude the use of public rights-of-way in conjunction with the operation of the ICES. Many franchise enabling statutes list specific services which local governments are authorized to franchise. In addition, most statutes require that the franchisee be serving a public purpose in order to be eligible for a franchise. These types of restrictions raise the question of whether, if an ICES is providing a service which is not deemed to be serving a public purpose, a franchise may be granted. If a franchise cannot be granted, significant uncertainty exists with respect to whether the ICES may operate along public rights-of-way without a franchise. If not, it may be precluded from operating unless all facilities are maintained on private property with the permission of the property owners.

Assuming a franchise is available to an ICES, additional uncertainty exists with respect to the procedure pursuant to which the franchise will be granted and the standards which will be applied in determining whether the franchise should be granted. These procedures and standards vary substantially from state to state and from municipality to municipality within each state.

Finally, an ICES which might otherwise be eligible for a franchise may be unable to obtain the necessary franchise as a result of a prior grant of an exclusive franchise to another utility serving the area. Nearly one-half of the states have not resolved the issue of whether exclusive franchises are permissible.

D. Rate Regulation Impediments

Assuming that an ICES operator can overcome or operate in spite of the impediments described above and begin its operations, it must be able to market both energy streams at competitive rates in order to stay in business. Several areas of PUC rate regulation may impede the ICES' ability to operate profitably. For example, an ICES may find that the rates for one energy stream are regulated on a statewide basis by the PUC while the remaining stream is regulated by one or more local governments. With such split jurisdiction, there can be little assurance that rates will be regulated consistently and in such a way as to enable competitive marketing of both energy streams.

Even if both energy streams are regulated by the PUC, resolution of various cost and rate-base allocation issues could present serious issues unique to ICES. Depending on the method chosen to allocate costs and rate base between the two services being marketed, the ICES operator may find that it will be compelled to sell one energy stream at a rate too low for the whole ICES to be profitable while the second energy stream must be sold at a rate too high to be competitive.

In addition, PUCs traditionally have exercised rate-making authority only with respect to sales by conventional utilities operating in a monopoly market. Investment in these conventional utilities traditionally has been considered a low-risk investment and, therefore, the rates of return on equity permitted by PUCs have been commensurately low. Because ICES, as a new industry and as a utility operating in competition with other utilities, will be viewed as a more risky investment, PUC decisions with respect to allowable rates of return will have a significant impact on the ability of ICES to attract investors. Rates of return satisfactory to investors in conventional utilities are unlikely to attract investors to the more risky ICES operations.

Finally, ICES must be able to obtain reasonable rates for sales of excess electrical power to and purchases of back-up electrical power from conventional electric utilities. These rates also will be regulated by PUCs and the PUC determinations will substantially affect the ability of the ICES to operate profitably. The uncertainty surrounding the factors that will be considered by PUCs in establishing these rates is very likely to be perceived as an impediment by prospective ICES operators and investors.

CHAPTER 7

OVERCOMING IMPEDIMENTS TO ICES -- SUMMARY

The Chapter 6 analysis demonstrates that the traditional public utility regulatory system presents numerous impediments to the implementation of ICES. These impediments do not appear in the form of a list of individual statutory or rule provisions which can be easily modified to accommodate ICES. Rather, the impediments take the form of the existing regulatory system itself -- a system which is based largely on a set of assumptions and practices foreign to the ICES concept.

Because the existing regulatory system is, in effect, the major impediment to the implementation of ICES, there are only two available alternatives for dealing with this impediment. Advocates of ICES can attempt to change the system, or they can work within the system in order to demonstrate the value of the ICES concept. Because many of the regulatory provisions which appear to be impediments to the implementation of ICES are integral parts of the existing regulatory system, however, any effort to change the system sufficiently to encourage the widespread implementation of ICES will require changes so fundamental that traditional forces operating within the system would have little trouble blocking such changes. Thus, a widespread effort by the advocates of ICES to change the system may result in a substantial expenditure of resources while bringing about very little change.

There is no single configuration or form of ICES. While differences can result from employing different technologies to produce different energy streams, the most useful classifications for purposes of analyzing potential institutional impediments to the implementation of ICES are those based on type of owner/developer and the nature of the customer group served. The classification scheme used in the following analyses includes ICES-Utility -- an ICES owned and operated by a conventional electric utility, ICES-Complex -- an ICES designed to serve existing institutional complexes such as government, commercial, industrial, residential or medical centers, ICES-Heat Plant -- an ICES providing thermal service for its own use or the use of a limited class of customers and selling all electrical output to a conventional utility, ICES-Co-Op -- an ICES owned by its customers and serving only these member/customers and ICES-Entrepreneur -- an ICES owned and operated by any entity intending to sell or provide utility service at retail to all users within a particular service area. Obviously, additional types, of ICES can be developed by combining these various modes of ownership with the various available customer classes.

ICES may be established gradually in forms that will not encounter, or not be significantly affected by, many of the impediments discussed above. When the various types of ICES are compared against the existing regulatory framework, it is apparent that there is a wide range in the degree of compatibility

between that framework and the various ICES types. The degree to which the implementation of ICES will be impeded by the existing regulatory system varies greatly depending on the form of ownership of the ICES, the number and type of customers which it intends to serve and the manner in which it will conduct its utility operations. Therefore, if advocates of ICES seek implementation along the paths of least resistance, this gradual implementation will provide ICES technology with an opportunity to establish its viability and adapt to the existing regulatory system while permitting the existing system to become familiar with and adapt to the peculiar problems and benefits of ICES. The following may be the most appropriate sequence of implementation of ICES.

1. ICES-Utility

ICES-Utility would include any ICES owned by an existing electric utility and operated as a part of its existing utility business. The utility could either operate its own cogeneration equipment or operate equipment owned by another entity on behalf of the owner. The utility would carry on its electrical operations in the same manner as it had before becoming involved with the ICES, but the particular arrangements for the sale of thermal energy could vary. Thermal energy might be distributed by the ICES-Utility to individual customers or it could be sold in bulk to a single customer for use by that customer or for further distribution by it.

ICES-Utility, because it would be operated by an existing utility, would be least affected by the regulatory impediments discussed in Chapter 6. As an existing utility, the ICES operator would already be subject to PUC regulatory jurisdiction and would have the experience necessary to function within that system with a minimum of inconvenience. In addition, the ICES-Utility might be able to install and maintain its ICES equipment pursuant to existing franchises, certificates or other approvals or obtain minor modifications in these prior approvals so as to permit the ICES operations.

II. ICES-Complex, ICES-Heat Plant

A second approach would be to structure ICES so as to take advantage of traditional exemptions built into the existing regulatory scheme in most states. In all states, a utility must be providing service "to or for the public" before it will be subject to PUC regulatory jurisdiction. In about half of the states, a utility will be subject to PUC jurisdiction only if it is deemed to be making "sales" of energy service. If the ICES is structured so as to either not be deemed to be providing service "to or for the public" or not to be making "sales" of energy services, that ICES would not be subject to PUC regulatory jurisdiction. ICES-Complex and ICES-Heat Plant would be structured so that energy services would be provided only to a limited and clearly defined class of customers. In addition, in many cases, such ICES may be able to provide energy service

as a part of an over-all rental package rather than on an individual metered basis. Such ICES could, in many cases, avoid classification as public utilities. Examples of such ICES would be an ICES established to serve a residential, industrial, commercial, governmental or university complex.

A great deal of uncertainty exists with respect to what types of service can be provided and to how many customers before a utility will be deemed to be subject to PUC jurisdiction. These uncertainties, however, could be remedied by means of fairly simple legislative or administrative action.

By operating so as to avoid PUC regulatory jurisdiction, these ICES will also give up the protections afforded by the regulatory system. Thus, such ICES may be able to operate in competition with conventional utilities without having to obtain PUC approval, but they also must be capable of waging a competitive battle with the existing utilities in the area to be served because they would not enjoy the luxury of the traditional monopoly status of a public utility. Similarly, such ICES would not be subject to PUC rate regulation but would also possibly not receive adequate regulatory protection in their attempts to negotiate contracts to purchase back-up power from or sell surplus power to conventional utilities.

III. ICES-Co-Op

ICES-Co-Op, unlike the ICES discussed above, could lend itself to broad implementation of ICES. By operating as a

cooperative -- a utility which is owned by its customers and provides service only to these owner/customers -- the ICES-Co-Op could avoid many of the more troublesome aspects of the traditional regulatory system while still enjoying many of its benefits. For example, utility cooperatives are exempted from PUC rate regulation and regulation of financial affairs in many states. On the other hand, utility cooperatives often are subject to service area restrictions and, therefore, are afforded the protections of the various methods of territorial allocations utilized by PUCs.

This traditional utility concept could be utilized by, and modified to better serve, ICES projects intended to serve large numbers of customers. One area of possible modification would be to permit qualifying ICES-Co-Ops to commence operations in service areas of conventional utilities under certain circumstances. Qualifying ICES-Co-Ops could be allowed to serve only large concentrations of new customers or they could be allowed to serve existing concentrations of customers. The prejudicial effect of such an extension of the cooperative concept could be minimized by requiring ICES-Co-Ops to purchase those facilities of the conventional utility within the ICES service area which are necessary for serving the ICES customers and which would be rendered unnecessary to the utility.

IV. Exempt-ICES

By utilizing the ICES types discussed above, advocates of ICES can implement ICES in forms which will be least affected by regulatory impediments in order to establish showcase ICES designed to demonstrate the viability and special benefits of the ICES concept. After these showcase ICES have existed in peaceful coexistence with conventional utilities for a time, conventional utilities, utility regulators and legislators may be more amenable to the type of system modifications necessary to encourage widespread implementation of ICES in many forms. At this point, the advocates of an ICES might effectively petition PUCs and state legislatures to define certain categories of ICES which will be exempt from certain troublesome aspects of the traditional regulatory system while enjoying some of its benefits.

In order to qualify as an Exempt-ICES, the ICES must, of course, be required to establish that it would be a reliable, responsible supplier of energy. Once utility regulators are convinced that the ICES has the financial and technological ability to adequately serve its proposed customers, the ICES could be exempted from many traditional areas of regulation without jeopardizing the best interest of the customers.

The Exempt-ICES should be permitted to commence operations to appropriate groups of customers in the service areas of conventional utilities. However, like the ICES-Co-Op, it should be required to purchase any equipment owned by the conventional utility which is rendered useless as a result of

the ICES being permitted to serve customers within the conventional utility's service area. Once it has established its service area, the Exempt-ICES should receive the type of territorial protection traditionally afforded public utilities.

The Exempt-ICES could also be freed from traditional PUC rate regulation. Rather than establishing traditional cost-based rates, the Exempt-ICES could be permitted to market its energy package at any rate which does not exceed the rates for comparable service from conventional utilities. If the Exempt-ICES believed that it was, for some reason, entitled to higher rates, it should be compelled to submit to traditional rate-making procedures. This should assure that, if the ICES concept is in fact economically viable, investors will be able to achieve sufficient returns on their investment while ICES customers are guaranteed reliable energy service at reasonable rates.