

**Commonwealth of Virginia**

**State Corporation Commission**

**Report to the Legislative Transition Task Force  
of the Virginia General Assembly**

**And the Governor of the Commonwealth of Virginia**



**Status Report: The Development of a Competitive Retail Market for  
Electric Generation within the Commonwealth of Virginia**

**Pursuant to Section 56-596 of the Code of Virginia**

**August 31, 2001**

# COMMONWEALTH OF VIRGINIA



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## STATE CORPORATION COMMISSION

August 31, 2001

TO: The Honorable James S. Gilmore, III  
Governor, Commonwealth of Virginia

The Honorable Thomas K. Norment, Jr.  
Member, Senate of Virginia  
Chairman, Legislative Transition Task Force  
and  
Members of the Legislative Transition Task Force

The State Corporation Commission is pleased to transmit its report regarding the advancement of competition in Virginia as required by Section 56-596 of the Virginia Electric Utility Restructuring Act.

This report, required annually on September 1, provides information on the status of competition in the Commonwealth, the status of the development of regional competitive markets, and the Commission's recommendations to facilitate effective competition as soon as practical.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Clinton Miller", written over a horizontal line.

Clinton Miller  
Commission Chairman

A handwritten signature in black ink, appearing to read "Theodore V. Morrison, Jr.", written over a horizontal line.

Theodore V. Morrison, Jr.  
Commissioner

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Hullihen Williams Moore  
Commissioner

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# **Report of the Virginia State Corporation Commission**

## **To the Legislative Transition Task Force of the Virginia General Assembly**

### **And the Governor of the Commonwealth of Virginia**

#### **Pursuant to Section 56-596 of the Code of Virginia**

**August 31, 2001**

### **Introduction**

Section 56-596 of the Code of Virginia directs the Virginia State Corporation Commission (“the Commission”) to prepare an annual report to the Virginia General Assembly’s Legislative Transition Task Force and the Governor of the Commonwealth of Virginia, concerning the development of a competitive market for retail electric generation within this Commonwealth. This reporting requirement was added to the Virginia Electric Utility Restructuring Act (“Restructuring Act”) by Senate Bill 1420, passed by the 2001 Session of the Virginia General Assembly, and signed into law by the Governor on March 26, 2001.

The purpose of this report, due September 1 of each year, is to examine three principal topics. First, the report is to examine the status of competition within the Commonwealth of Virginia. Second, the report is to report on the development of regional competitive markets. Additionally, the report is to address the development of “effective competition within the Commonwealth as soon as practicable.”<sup>1</sup> In that regard, the Commission is asked to provide recommendations of actions that may be taken by the General Assembly, the Commission, or others to facilitate competition in the Commonwealth.<sup>2</sup> The report that follows is thus broken into these three parts. For ease of use, the executive summaries of all three parts follow this introduction.

Part I, The Status of Competition Within the Commonwealth, provides a brief overview of critical activities currently underway to prepare Virginia for January 1, 2002—the Commonwealth’s “Day One” for retail choice. Specifically, this section of the report reviews the current status of retail choice pilot programs sponsored by the Virginia Electric and Power

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<sup>1</sup> Section 56-596 B of the Restructuring Act.

<sup>2</sup> Section 56-596 B of the Restructuring Act provides that such recommendations “shall include actions regarding the supply and demand balance of generation services, new and existing generation capacity, transmission constraints, market power, suppliers licensed and operating in the Commonwealth, and the shared or joint use of generation sites.”

Company (“Virginia Power”), AEP Virginia (“AEP-VA”), and the Rappahannock Electric Cooperative.<sup>3</sup>

Part I also discusses critical proceedings currently underway at the Commission concerning (i) the transfer of the management and control of Virginia utilities’ transmission facilities to regional grid managers, popularly referred to as regional transmission organizations, or RTOs,<sup>4</sup> and (ii) the functional separation of Virginia’s utilities into their transmission, distribution and generation functions.<sup>5</sup> Intimately related to functional separation, is the determination of “wires charges” to be paid by shopping customers to their incumbent utility. Such charges—designed to “provide the opportunity for competition,” and to compensate incumbents for potential “stranded costs” resulting from electric utility restructuring—are the positive differences between the incumbents’ unbundled generation rates (established through the utilities’ functional separation cases) and the market prices of generation, as determined by the Commission for each utility.<sup>6</sup> A proceeding concerning the development of market prices for calculating wires charges is currently underway at the Commission.<sup>7</sup>

Additionally, Part I discusses the important phase-in schedule for retail choice established earlier this year by Commission order in Case No. PUE000740. Consistent with that schedule, on January 1, 2002, more than one million Virginia electricity customers will be *eligible* to shop for retail generation services offered by competitive suppliers.<sup>8</sup> By January 1, 2003, that number will climb to three million. Of course, shopping eligibility does not guarantee shopping opportunities, and so the development of an effectively competitive market is essential to making “retail choice” a meaningful term.

Part II of the report entitled Performance Review of Electric Power Markets, examines the development of regional competitive markets for electric generation. It was prepared by Dr. Kenneth Rose, a Senior Institute Economist with the National Regulatory Research Institute (NRRI). Dr. Rose specializes in electricity market analysis and industry trends. As emphasized in this report, the development of regional competitive markets is critical to the implementation and success of Virginia’s Restructuring Act as well as retail choice in other states that have opened or are preparing to open their retail generation markets to customer choice.

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<sup>3</sup> As noted in the report, the pilot programs have helped these utilities prepare and implement (at least in part) important computer systems and other processes essential to the entry of competitive suppliers into Virginia’s electricity market. However, customer participation in these pilots has been nominal, and, at present, no licensed competitive suppliers are making any competitive offers in any of the pilot programs.

<sup>4</sup> Regional transmission organization, or “RTO”, is a term utilized by the Federal Energy Regulatory Commission in its Order 2000; Virginia’s restructuring legislation refers to these entities as regional transmission entities, or RTEs (§§ 56-577 and 56-579 of the Restructuring Act).

<sup>5</sup> Functional separation and RTO membership (for transmission-owning utilities) are required of all of Virginia’s incumbent electric utilities pursuant to §§ 56-579 and 56-590 of Restructuring Act.

<sup>6</sup> Section 56-583 A of the Restructuring Act.

<sup>7</sup> The methodologies for determining these market prices are currently the subject of a pending Commission proceeding in Case No. PUE010306.

<sup>8</sup> All customers of AEP-VA, Allegheny, and Delmarva, plus one-third of Virginia Power’s customers will be eligible to shop for retail generation supply on January 1, 2002. Virginia Power will complete the phase-in of its remaining customers by January 1, 2003, as per the Commission’s order.

Part II summarizes the current status of both retail and wholesale generation markets on a regional and national basis. In particular, the report discusses the state of retail generation competition in such key states as Pennsylvania, California, Massachusetts and New Jersey—states that have had the most experience with retail choice, thus far. Additionally, Dr. Rose has examined current developments in the wholesale market that are driving the availability of competitive offers in the retail electricity market. He concludes that higher prices and volatility in wholesale markets across the country have taken their toll on state retail markets. In the state of Pennsylvania, for example, during the twelve-month period of July 2000 to July 2001, the number of competitive suppliers offering prices below those Pennsylvania electric customers could obtain by simply staying with their incumbent utilities, dwindled from twenty-eight to two.

Finally, Part III of this report addresses Recommendations to Facilitate Effective Competition in the Commonwealth. Section 56-596 B of the Restructuring Act directs the Commission to address six separate issues in developing this part of the report: (1) supply and demand balance for generation services; (2) new and existing generation capacity; (3) transmission constraints; (4) market power; (5) suppliers licensed and operating in the Commonwealth; and (6) shared or joint use of generation sites.

As noted in Part III, the Commission Staff provided stakeholders and interested parties an opportunity to offer their views on this topic. The Commission Staff received responses from American Electric Power, Allegheny Power, Dominion Virginia Power, Old Dominion Power Company/LG&E Energy, Virginia's electric cooperatives, the Virginia Committee for Fair Utility Rates, AES New Energy and Exelon. All of the comments we received are summarized in Part III, and they are included, in their entirety, as Attachment II to Part III. The stakeholders' comments ranged from simply reiterating what the Restructuring Act currently requires (e.g., joining RTOs, etc.) to recommendations for dramatic departures from the Act, such as the immediate elimination of capped rates to create more competitive "headroom."

In conclusion, we note that before a competitive market for retail generation can develop in Virginia, it is necessary for a proper foundation to be laid. The strength of that foundation depends upon many critical details, whose development the Commission is overseeing during Virginia's transition to retail choice. Many of these details are discussed in Part I, The Status of Competition in the Commonwealth. They include the Commission's review of (i) utilities' proposed functional separation plans, (ii) utility rate unbundling and the corresponding development of wires charges for shopping customers, (iii) utilities' applications to transfer management and control of their transmission assets to RTOs, and (iv) the licensing of competitive electric suppliers.

The Commission provides this report to assist the General Assembly and the Governor of this Commonwealth, as we all endeavor to achieve the goals of Virginia's Restructuring Act: the development of an effectively competitive market for retail generation services provided to this Commonwealth's electricity consumers.