

SHIFTING UTILITIES' INCENTIVES FOR EQUITY & AFFORDABILITY

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WHY IT MATTERS

Virginians pay some of the highest energy bills in the nation, disproportionately impacting low-income households and historically marginalized communities.^{1,2,3} High energy costs are tied to the regulatory system governing Virginia's investor-owned utility (IOU) monopolies that incentivize expensive investments rather than cost-saving measures – i.e., the more expensive an energy project is, the more profits the utility collects.⁴

Under the current “cost-of-service” (COS) model, utility monopolies in Virginia profit from (i) selling electricity and (ii) building infrastructure.⁵ Initiatives like reducing energy bills with energy efficiency improvements and expanding customer-owned distributed energy resources like rooftop solar conflict with utilities' profit sources.⁶ The current model also conflicts with buying clean energy from third-party developers through power purchase agreements (PPAs), even when it saves customers money.

This model does not align with solutions to minimize costs and harmful environmental and social impacts. Without rethinking alternatives to the current COS model, the transition toward a carbon-free energy system will likely be slower and more costly, and justice priorities could be relegated.

CURRENT LANDSCAPE

States nationwide have implemented several modifications to the COS model using a variety of performance-based regulation (PBR) tools. PBR is a group of reforms—including revenue decoupling, multiyear rate plans, and performance incentive mechanisms—that aim to make cost-saving measures—like energy efficiency, demand response, customer-owned resources, and PPAs—as financially attractive as capital investments.

For example, in 2013, New York utility Con-Edison needed to upgrade a portion of its grid due to increased demand. Instead of a \$1 billion substation upgrade, the regulator established the Brooklyn-Queens Demand Management program, implementing several incentives to ensure the utility would benefit from non-capital-intensive solutions. Costs were reduced by half with an alternative investment package that included energy efficiency, demand response, and storage.⁷ PBR frameworks require careful consideration, and justice needs to be at the forefront of implementation.⁸ In 2023 and 2024, the General Assembly passed two bipartisan legislative initiatives to advance PBR:

In 2023, the General Assembly enacted legislation to establish a State Corporation Commission (SCC) proceeding to implement “performance-based adjustments,” also known as performance incentive mechanisms (PIMs).⁹ PIMs reward or penalize utilities for specific target outcomes that the current system is not designed to incentivize. States have seen good results using PIMs to incentivize higher utilization of demand response—programs that reward customers for using less electricity during periods of high demand (peak hours). Demand response programs can decrease system costs and displace the need for new generation plants.¹⁰

In 2024, the General Assembly passed legislation establishing a study process in which the SCC, Virginia Energy, and stakeholders will further evaluate PBR tools. The study will examine how the current financial incentives of utility monopolies conflict with state policy goals, outline tools to better align utility incentives with the state's environmental and justice goals, assess risks, and identify implementation steps.¹¹

OPPORTUNITIES

The initiatives outlined above should generate a comprehensive evaluation of long-term solutions for the misalignment of IOUs' financial incentives with the state's energy policy goals. The General Assembly and the SCC will also need to generate short-term solutions to specific barriers stemming from utilities' incentives and other legal impediments.

For example, although the cost of PPAs for utility-scale solar has dramatically declined nationwide, the current statute caps PPAs at 35% of utilities' clean energy investments under the Virginia Clean Economy Act (VCEA).¹² Thus, utilities cannot consider PPAs to meet more than 35% of their clean energy goals under the VCEA, even when there are qualified PPAs that would be cheaper than utility-owned projects. Regulators should be allowed to consider all qualified and cost-competitive PPAs to reduce clean energy costs.

Furthermore, although it is the policy of the Commonwealth to “enable widespread integration of distributed energy resources,”¹³ distributed solar is facing unreasonable interconnection costs and timelines. Utilities in Virginia are requesting projects under 3 MW to pay \$1 to \$3 million for grid upgrades, making projects unfeasible.¹⁴ On average, it takes Dominion Energy 300 business days to get small facilities (less than 2 MW) interconnected; an SCC expert suggested 195 days as a more reasonable pro-

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cessing time benchmark.¹⁵ The SCC needs to accelerate fair interconnection rules and could use PBR tools like tracking metrics and PIMS to boost distributed generation.

Finally, Dominion reported it would not meet the net energy efficiency targets of the VCEA¹⁶ and in a recent SCC filing, Appalachian Power (APCo) and Dominion Energy proposed low energy efficiency targets for the 2026-2028 period.^{17,18} The proposed targets are lower than those of top energy efficiency-performing utilities.¹⁹ The SCC needs to refine existing incentives and ensure utilities leverage their maximum energy efficiency potential (see page 111).

TOP TAKEAWAYS

Current incentives for utilities are counterproductive to an equitable and affordable clean energy transition. These incentives are hindering the Commonwealth's distributed energy and energy efficiency goals. Decision-makers should establish short- and long-term systemic solutions.

The SCC and Virginia Energy should thoroughly explore all performance-based regulatory tools to shift utility incentives so that Virginia can successfully meet its clean energy policy goals.

Increasing the percentage of qualified third-party-owned solar and wind resources that the SCC can approve for our utilities' portfolios will ensure ratepayers receive lower prices for clean energy.

ENDNOTES

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