

MEMORANDUM

Dominion Shareholder Proposal

**Request to include sustainability
as one of the performance measures
under the Company's incentive plans
for senior executive compensation.**

Dominion Resources, Inc

Symbol: D

Vote "FOR"

Shareholder Proposal for Executive Performance linked to ESG* Issues

The shareholders of Dominion Resources request the Compensation, Governance, and Nominating Committee, when setting senior executive compensation, include sustainability as one of the performance measures under the Company's annual and/or long-term incentive plans. Sustainability is defined as how environmental, social, and financial considerations are integrated into corporate strategy over the long term.

Why a "FOR" vote on the Shareholder Proposal:

Dominion faces risks to its reputation that need to be addressed:

1. Dominion faces increasingly angry customers, a skeptical public, and critical media. Dominion has had severe problems with their public image in recent years. Some examples of recent issues:
 - Dominion made more profit than legally allowed in at least two out of three recent years and was forced to return some of that excess to customers¹ – but by Virginia law, they have to return only a fraction of that excess to the rate holders, which led to many very angry customers².
 - Dominion received over \$76 million in bonuses for use of renewable energy as a part of the Virginia voluntary RPS, although they added no renewable energy generation to Virginia but instead bought Renewable Energy Credits (RECs) from older, out-of-state systems. There was a public outcry when it became widely known that

* Environmental, Sustainability and Governance

¹ <http://hamptonroads.com/2011/12/dominion-ordered-refund-783-million-customers>

² <http://hamptonroads.com/2011/12/dominions-excess-profits>

Dominion had spent \$2M on old RECs from other states, and received in return \$76M out of the pockets of Virginia rate-payers, and developed no renewable energy generation^{3,4}. The Virginia AG report⁵ found that:

The Renewable Portfolio Standard (RPS) adder has not served to advance the environmental concerns [that led to its inclusion in the legislation] because the utilities have not built any new renewable energy facilities to comply with the RPS goals, but instead, have primarily relied on buying Renewable Energy Certificates (RECs) from existing renewable facilities, including hydroelectric plants that have been in service for more than 80 years.

The RPS adder has contributed to increases in customer bills and will likely have a significant future impact by allowing utilities to keep profits that exceed their SCC-approved fair ROE and reducing the chance that customers will be entitled to future rate decreases.

Overall, Dominion's use of the RPS is leading to a deal that could be very expensive to its ratepayers.

- Dominion is seen by the public as making no investment in renewables, and yet when others take steps toward increasing Virginia’s production of renewable energy, Dominion actively steps in to oppose it – as demonstrated when the Washington and Lee University attempted to install a large solar array as part of a power purchase agreement, and received a cease-and-desist letter from Dominion⁶.
- Another recent action that angered the public was Dominion’s action to put a high standby fee on solar systems over 10 kW. At that time, this regulation applied to only a single customer with a solar array over 10 kW. Application of this fee directly inhibits adoption of solar power and feasibility of negotiating financing since it roughly doubles the payback period. Numerous public comments were received by the Virginia SCC in opposition to this fee. This fee was a very different approach than other utilities such as Tennessee Valley Authority and Austin Energy have taken towards solar, where they offer healthy feed-in tariffs to encourage solar generation and thus lessen the companies’ need for expensive peaker plants at peak electricity use times.
- In case PUE-2012-00064 to the Virginia SCC, Dominion proposed an extremely low purchase price for customer-generated solar. Dozens of angry Dominion customers

³ http://articles.washingtonpost.com/2011-12-30/opinions/35288335_1_renewable-energy-renewable-portfolio-dominion-power

⁴ http://www.chesapeakeclimate.org/file-uploads/kelly-trout/Virginia_RPS_Backgrounder_10-2012.pdf

⁵ http://www.ag.virginia.gov/Media%20and%20News%20Releases/News_Releases/Cuccinelli/AG%20Report%20on%20Statutory%20ROE%20Adders.pdf

⁶ http://articles.washingtonpost.com/2011-12-30/opinions/35288335_1_renewable-energy-renewable-portfolio-dominion-power

- from all over the state attended the hearing, many public witnesses spoke in opposition to the low rates and short term of the program, and over 1200 public comments were submitted in opposition to the program. Several professional solar installation companies testified to say that there would be no customers for this program, since they would not be able to tell their customers that this was a financially sound option.
- Dominion has been pressured a great deal in the press recently because they seem to be opposed to altering their behavior, regardless of reputational or financial consequences. The Virginian Pilot did a scathing editorial on Dominion’s “no comment” policy⁷ which has been strictly enforced on every story for the last year: Dominion will not give the Virginian Pilot information on any story the newspaper is going to run. This is hardly the mark of an open and transparent company.

Numerous media sources reported Dominion’s legislative agenda as hostile to renewable energy and sustainability. Meanwhile, polling indicates an increasing amount of support for renewable energy.

A selection of major news articles and editorials mentioning Dominion and exposing its anti-renewable legislative agenda:

- [Dominion Power’s wind and solar façade \(The Washington Post\)](#)
- [Virginia needs a better energy policy \(The Washington Post\)](#)
- [Dominion's bait and switch \(Virginian-Pilot\)](#)
- [Dominion’s excess profits \(Virginian-Pilot\)](#)
- [Dominion must invest in clean energy \(Virginian-Pilot\)](#)
- [Utility's overcharging shows need for true regulation \(Virginian-Pilot\)](#)
- [Keep renewables, or repeal the law \(Richmond Times-Dispatch\)](#)
- [Don't extend monopoly to the sun \(Virginian-Pilot\)](#)
- [On Dominion's money and energy stance \(Daily Press\)](#)
- [Dominion’s dual solar proposals \(Virginian-Pilot\)](#)
- [Dominion’s sunshine tax \(Virginian-Pilot\)](#)
- [State law hurting Virginia’s green future? Lawmakers eye changes \(WSLS News 10\)](#)
- [Staunton solar firm faced utility challenge \(News Leader\)](#)
- [Solar project caught in legal shadows \(News Leader\)](#)
- [Here we go again – another power play \(Virginian-Pilot\)](#)
- [Renewable energy laws are exploited \(Richmond Times Dispatch\)](#)
- [Dominion’s ineffective gift \(Virginian-Pilot\)](#)
- [Where’s Virginia’s Renewable Energy? \(Richmond Times-Dispatch\)](#)
- [Squelching sun power \(Virginian-Pilot\)](#)
- [From coal-burning to carbon-free \(The Washington Post\)](#)

⁷ <http://hamptonroads.com/2012/10/utility-policy-no-comment-hardly-useful-customers-0>

- Hundreds protest at Dominion VA Power (NBC News Channel 12)
- Environmental protesters target Dominion Va. Power (Richmond Times-Dispatch)
- Dominion makes play for offshore wind dominance (Virginian-Pilot)
- Virginia Environmentalists Urge Wind Power Speedup (WRIC ABC News Channel 8)
- Nuclear power protestors outside Dominion (NBC News Channel 12)
- Is Dominion serious about offshore wind? (Offshore Wind Wire)
- Dominion to Feds: delay Google's wind line (Daily Press)

Contrarily, major polls indicated public support for renewable energy:

- 59% of Americans prefer clean energy production over oil, gas and coal (Gallup)
- By a 3-to-1 margin, Americans prefer clean energy subsidies (Civil Society Institute)
- 82% of Americans believe government should support domestic solar manufacturing (SEIA)
- 70% of Americans support local wind projects; a new twist on NIMBYism (Saint Consulting)
- 76% of Americans worry about lack of clean energy progress (UT at Austin)

2. Dominion faces an increased number of shareholder resolutions regarding sustainability policy.

For this 2013 proxy season, there were nine shareholder proposals submitted to Dominion. Dominion opened dialog on none of them, but immediately protested seven of them to the SEC. Substantially more shareholder resolutions are submitted to Dominion than to most other companies. The number has been growing each year as more shareholders take this route to express their displeasure with Dominion’s policies. One reason there are so many shareholder resolutions filed at Dominion is that many people feel that the utility’s management is only looking at short term profit, and working to satisfy certain related companies (such as coal companies), but are not acting so as to assure future financial stability and success. The number of proposed resolutions is one indication of the shareholder view of the inadequacy of Dominion’s current policies. Inclusion of a direct link from Dominion’s executive compensation to sustainability performance would go a long way toward convincing shareholders that there was a meaningful policy toward including sustainability as a factor in Dominion top-level decisions.

3. Dominion is not keeping pace with peers in the arena of sustainability.

Many companies have added sustainability criteria to the mix of metrics used to determine executive compensation. According to a 2012 Glass Lewis report on executive compensation and sustainability⁸, 42% of companies in the S&P 100 disclose a link between sustainability and executive compensation.

⁸ <http://www.glasslewis.com/blog/glass-lewis-publishes-greening-the-green-2012-linking-executive-compensation-to-sustainability/>

Alcoa, cited as a notable case in a recent Conference Board publication, “Linking Executive Compensation to Sustainability Performance⁹,” linked 20 percent of executive bonuses in 2010 to non-financial metrics including carbon dioxide reduction, safety and diversity. According to this report, Intel, Xcel Energy, Alcoa, ING, National Grid, Shell, and Suncor Energy are among the US companies tying executive compensation to sustainability performance. The report also finds that shareholders are placing more value on corporate sustainability initiatives, and are becoming increasingly interested in linking such performance to executives’ compensation.

British utility company National Grid announced last year it would partly base executive compensation on meeting targets for reducing carbon emissions. In addition, Xcel Energy in its 2009 proxy statement discloses that certain annual incentive payments are dependent on green house gas emission reductions alongside the weight given to meeting earnings per share targets.

Intel, which has been providing a link between ESG metrics and compensation since 2005, includes a category entitled “People, Customers, Stockholders, Planet” as part of the operational goals approved by its Compensation Committee for 2011. Intel is often lauded for embedding ESG issues into its operational practices by including nearly 300 specific measurable issues upon which executives can be evaluated, including the company’s carbon footprint, cost savings through recycling, and employee morale. Aluminum manufacturer Alcoa is noted for its compensation incentives that increase representation of women and minorities in professional and managerial ranks, improve safety statistics, reduce carbon emissions and for its clear disclosure of its ESG metrics and executives’ associated performance against them in its annual proxy filings. Campbell’s Soup has some of the most comprehensive criteria, including diversity, safety, employee engagement, community impacts such as reducing hunger and childhood obesity in its communities of operation and broader environmental goals in areas of energy, water and recycling.

There are many examples of electric utilities succeeding financially by incorporating sustainability in their long-term plans. In 2007, the Texas energy company TXU agreed to scrap plans for 8 of 11 new coal plants, reduce their emissions to 1990 levels by 2020, and double investment in renewable energy. Duke Energy has commercial-scale solar projects, nine US wind farms with over 1,000 MW total generation, a senior vice-president for wind generation, and a distributed rooftop solar generation program. Florida Power and Light has commercial scale solar and wind plants, including 14 MW of wind and over 110 MW of solar generation. MidAmerican, after construction is complete, will generate 26% of its total electricity generation from wind. National Grid has two commercial scale solar plants complete, and four more under construction.

⁹ <https://www.conference-board.org/publications/publicationdetail.cfm?publicationid=2221>

Dominion is neglecting a path that could lead to improved long-term performance:**1. Linking executive compensation to ESG metrics improves company financial performance.**

An excellent and well-researched resource is the report Integrating ESG issues into executive pay¹⁰ from the Principles for Responsible Investment Association. In this report, many of the advantages of linking executive pay to ESG are enumerated, case studies are used to show benefits that have accrued, and methods of accomplishing these links are discussed. The report describes the financial benefit due to linking of executive pay to sustainability, and that show that these links are effective motivators. From the report: (emphasis added)

*Beginning in 2005, Intel started linking its bonuses to Environmental, Social and Governance (ESG) metrics. ... While there was initial skepticism for its ESG initiatives due to the uncertainty about the link between financial and ESG performance, **the company found that positive ESG practices have been beneficial to the company’s overall performance.***

*Research suggests that **companies which strongly link ESG metrics to executive pay are more likely to have board oversight of sustainability issues.***

*Eccles et al (2011) analyzed a harmonized sample of 180 US firms over the period from 1993 to 2010. Companies were divided in two groups: 90 companies were classified as High Sustainability firms, as they had already adopted sustainability policies on 1993; and 90 companies that had not adopted such policies were classified as Low Sustainability firms. Research found that **sustainable firms generated considerably higher profits and stock returns**, suggesting that in the long term developing a corporate culture of sustainability may be a competitive advantage for a company. In her study based on 157 German chemical firms, Delmas et al (2011) found that **proactive environmental strategies positively impact firm performance.***

*In a series of meta-analyses, various authors have agreed that **the majority of studies confirm the positive relationship between ESG and financial performance of companies** (Gompers et al., 2003; Orlitzky et al., 2003; Allouche & Laroche, 2005; De Bakker et al., 2005; Van Beurden & Gossling, 2008). In 2011, the World Economic Forum also published a white paper listing research (conducted in the 2000s by Mercer, McKinsey, Innovest Strategic Value Advisors and the UK Environment Agency) showing the positive correlation between ESG factors and shareholder value creation.*

*Several scholars seem to agree that monetary incentives linked to ESG factors have a positive impact on overall performance. Moreover, Russo and Harrison (2005) have studied the effect of tying environmental performance and remuneration on a sample of 169 U.S firms. The results reveal that **monetary incentives for environmental performance appear to be efficient in motivating managers concerning ESG performance.***

¹⁰ www.unpri.org/wp-content/uploads/IntegratingESGIssues.pdf

Dominion faces legal and financial risks that should be disclosed and mitigated:

1. Energy production faces risks that can cause large financial loss from even a single event. The need for a greater emphasis on sustainability factors in incentive pay is illustrated by incidents such as BP’s 2010 Deepwater Horizon oil spill, where a single occurrence caused significant losses to shareholders, with financial loss to the company still occurring but will undoubtedly total in excess of \$20 billion. As illustrated by many recent payments and litigation, Dominion is not immune to environmental risks.
2. Awareness of risks and appropriate response can lessen long-term financial impact. A publically available report by CERES lays out some of the risks inherent in capital investment in electricity generation, and gives examples of Dominion’s peers who are succeeding in risk-aware planning^{11, 12}:

It is estimated that the U.S. electricity industry could invest as much as \$100 billion each year for 20 years. This level of investment will double the net invested capital in the U.S. electricity system by 2030. Moreover, these infrastructure investments are long lived: generation, transmission and distribution assets can have expected useful lives of 30 or 40 years or longer. This means that many of these assets will likely still be operating in 2050, when electric power producers may be required to reduce greenhouse gas emissions by 80 percent or more to avoid potentially catastrophic impacts from climate change.

The very large amount of capital investment that’s being contemplated and the resulting upward pressure on electricity rates will make it very unappealing (or simply untenable) for regulators to burden ratepayers with the full cost of utility mistakes. As a result, it is likely that utility investors (specifically shareholders) will be more exposed to losses resulting from poor utility investment decisions than in years past.

A recently completed IRP by the Tennessee Valley Authority (TVA) illustrates how robust planning enables risk-aware resource choices and avoids higher-cost, higher-risk supply portfolios. TVA considered five resource strategies and subjected each to extensive scenario analysis. The lowest-cost, lowest-risk strategies were the ones that diversified TVA’s resource portfolio by increasing TVA’s investment in energy efficiency and renewable energy. The TVA analysis is careful and deliberate; analyses by other utilities that reach significantly different thematic conclusions must be scrutinized carefully to examine whether the costs and risks of all resources have been properly evaluated.

¹¹ <https://www.ceres.org/files/press-files/risk-aware-planning-and-a-new-model-for-the-utility-regulator-relationship>

¹² <https://www.ceres.org/resources/reports/practicing-risk-aware-electricity-regulation/>

3. Dominion faces financial risk due to investment based on poor planning of demand.
The U.S. Energy Information Administration projects electricity use will increase at the anemic rate of 0.7 percent per year through 2035, but Dominion has over 2% annual increase in their Integrated Resource Plan (IRP), which means their investments are not being made based on a realistic scenario.

Conclusion:

Dominion faces serious challenges with regard to environmental and sustainability goals that are not being addressed. Financial and reputational risks to Dominion’s shareholders are numerous and severe. Dominion management is not being compensated based on their performance with regard to sustainability. Adding this focus to the determination of executive compensation will change the weight and importance that Dominion gives sustainability issues, and should change their future stability for the better. Other utilities like National Grid, Xcel Energy, and Suncor Energy have developed specific targets for executive compensation. Other companies such as Intel have greatly benefited financially and reputationally from incorporation of links of executive pay to sustainability. Dominion should be required to include sustainability factors in their executive compensation decisions by a FOR vote on this shareholder resolution.