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IDAHO PUBLIC
UTILITIES COMMISSION

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September 18, 2009

HAND DELIVERED

Jean D. Jewell, Secretary
Idaho Public Utilities Commission
472 West Washington Street
P. O. Box 83720
Boise, Idaho 83720-0074

Re: Case No. GNR-E-09-03
IN THE MATTER OF A REVIEW OF THE SURROGATE AVOIDABLE
RESOURCE (SAR) METHODOLOGY FOR CALCULATING PUBLISHED
AVOIDED COST RATES.

Dear Ms. Jewell:

Enclosed for filing please find an original and seven (7) copies of Idaho Power's and Avista's Initial Joint Comments in the above-referenced matter.

Please return a stamped copy of this transmittal letter for our files in the enclosed self-addressed stamped envelope.

Very truly yours,

Barton L. Kline

BLK:sh
Enclosures

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IDAHO PUBLIC UTILITIES COMMISSION

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF A REVIEW OF)
THE SURROGATE AVOIDABLE)
RESOURCE (SAR) METHODOLOGY) CASE NO. GNR-E-09-03
FOR CALCULATING PUBLISHED)
AVOIDED COST RATES) IDAHO POWER'S AND AVISTA'S
INITIAL JOINT COMMENTS
)
)

In Order No. 30873 issued in this case on August 6, 2009, the Commission directed Idaho Power Company ("Idaho Power"), Avista Corporation ("Avista"), and PacifiCorp to answer several questions, in "broad and general terms", concerning the current surrogate avoidable resource ("SAR") methodology. Avista and Idaho Power (sometimes referred to collectively herein as "the Companies") hereby submit this joint filing in which Avista and Idaho Power provide their answers to the questions posed by the Commission in Order No. 30873.

I. Historical Context

In Order No. 30873, the Commission described how the SAR methodology has evolved over time. In fact, it was approximately twenty-nine years ago, August 8, 1980, when the Commission issued its first order (Order No. 15746) establishing the principles applicable to purchases of power from Public Utility Regulatory Policy Act of 1978 (“PURPA”) qualifying cogenerators and small power producers (“QFs”). In Order No. 15746, the Commission directed Idaho Power Company, Utah Power & Light Company, and the Washington Water Power Company to provide drafts of tariffs and standard contracts which would be offered to QFs to facilitate purchases of energy and capacity by the three utilities. In Order 15746, the Commission determined that each of the three utilities would use a hypothetical baseload coal-fired generating plant as the generation facility that could be deferred or avoided. As such, the cost of this coal-fired facility would be used to set avoided cost rates. It was not until 1993, in Case No. IPC-E-93-28, that the Commission concluded that the avoidable resource or SAR should no longer be a coal-fired generating plant but instead should be a natural gas-fired combined cycle combustion turbine.

By initiating this proceeding, the Commission has acknowledged that another shift has occurred in the type of generating resource that utilities may avoid by purchasing energy from QFs. Idaho Power and Avista have each identified in their respective Integrated Resource Plans and other resource acquisition documents their intentions to acquire, outside of PURPA, substantial amounts of power generated by renewable resources—principally from generation using wind as its motive force. Idaho Power and Avista understand that PacifiCorp, dba Rocky Mountain Power, has similarly

identified in its resource acquisition document its intent to acquire power generated by renewable resources—principally from generation using wind as its motive force.

There has been at least one other major change that has occurred since the last time the Commission addressed the type of SAR to be used to set avoided costs. Specifically, several states, including Washington and Oregon have implemented state-mandated renewable portfolio standards (“RPS”). Also, a similar renewable energy standard (“RES”) is being considered at the federal level. Thus, it is important that the Commission address compliance with such standards when considering a change to the SAR methodology. For all of these reasons, the Commission’s decision to initiate this proceeding is both timely and appropriate.

II. Companies’ Responses to Commission Questions

The Commission’s questions and the Companies’ initial responses are as follows:

- 1. “Does the present SAR methodology for published avoided cost rates need to be modified or augmented? Yes or No.”**

Answer: Yes.

- 2. “If answer to Question 1 is yes,**
 - a. Please provide the basis for your answer.**

The present SAR methodology for setting published avoided cost rates (or PURPA rates) should be modified to ensure comparability with resources the Companies would build and own or otherwise acquire (“utility-build options”). The Companies believe that a wind-based SAR is more appropriate at this time for developing PURPA rates given that the Companies are currently acquiring or are planning on acquiring, and could avoid or defer, non-PURPA wind generation.

Using the present gas-fired SAR, the published levelized avoided cost rate is \$90.64 per MWh, or more than 9 cents per kWh.¹ The Companies include the addition of non-PURPA wind resources in their respective IRP's preferred resource portfolios. Northwest Power and Conservation Council ("NPCC") wind resource cost and generation assumptions result in a "busbar" price below 8 cents per kWh.² Avista's 2009 IRP estimates wind generation costs at approximately 9.5 cents per kWh and Idaho Power's 2009 IRP forecasts wind generation cost at 8.65 cents per kWh.

But simply comparing the cost of PURPA resources against utility-build resources does not tell the whole story. When a utility builds a resource, it obtains all capabilities of that resource, including any capacity, energy, and environmental attributes, including green tags or Renewable Energy Credits ("RECs").

Assuming that utilities will not get the environmental attributes when purchasing a QF's output at the published avoided cost rates, utility-build resource cost estimates used in an SAR should be reduced by the value of the environmental attributes in order to properly compare the costs of a utility-built resource with the costs of a similar PURPA resource. Utilities, and thus the utilities' customers, simply should not be required to pay substantially more for the capability from a PURPA resource than they would for the same capability from similar utility-build projects.

b. In broad and general terms, how should the methodology be modified or augmented?

The SAR methodology should be modified to use a wind farm as a surrogate avoidable resource instead of the current SAR, which is based on a gas-fired combined cycle combustion turbine. The current SAR cost-estimation model could be used to

¹ for a 20-year project beginning in 2010.

² NPCC cost assumptions input into the present SAR model.

calculate rates, or a new similar but simpler model might be developed. If the current model is used, input variables that would change from the existing gas-fired SAR include: installed capacity cost, transmission interconnection costs, fixed and variable operations and maintenance costs, capacity factor, project life, and escalation rates for SAR capital. The cost of gas and the cost of integrating wind would be zeroed out. In addition, and similar to the benefits the utility customers would obtain from a utility-build project, any environmental attributes associated with PURPA resources would be part of the output transferred to the utility purchasing the power.

To ensure that QFs continue to perform under their contracts, the existing Mechanical Availability Guarantee ("MAG") should be retained for wind and other intermittent QF resources. The 90/110 performance band should be retained for non-variable QFs. Retention of such provisions will provide some protection to help ensure that customers are not overpaying for the resource.

Wind and other intermittent generation resources cannot be relied upon to provide a significant contribution at the time of system peak. Other system resources must step in during times of system peak when the intermittent resource is not generating at or near its peak capability.

If the Commission adopts a wind-based SAR methodology to calculate PURPA rates, the Companies propose that a reasonable capacity adder to the PURPA rates be paid to non-intermittent (e.g., non-wind) QFs. Among other alternatives, a straight-forward option for calculating this adder would be to evaluate the all-in lifecycle costs of a simple-cycle gas turbine and subtract from those costs wholesale electricity revenues expected over the plant's life.

Wind and other renewable resources benefit from large federal tax subsidies that have been in existence since 1992. The present subsidy— 30% of installed cost— expires in 2012. These subsidies have been extended in nearly all years since 1992, and it is likely they will continue in some fashion after 2012. Subsidies have a very large impact on wind and other renewable resource costs. If a utility builds a renewable resource, its customers have the opportunity to benefit from the subsidy. To protect customers from paying too much for PURPA generation, tax subsidies must be accounted for in the PURPA rates. Accordingly, the Commission should reflect the benefits of these subsidies in the PURPA rate.

III. QF Contracts During Transition Period

In Order No. 30873 on page 3, the Commission noted: “As always the published rates remain presumptively reasonable and available to eligible QFs until changed.” While Order No. 30873 does not ask the parties to address how QF contracts executed during the period of time when the Commission is considering changes to SAR methodology are handled, prior history teaches that such a discussion is needed at an early stage of this proceeding.

As the Commission is well aware, it is unlawful for the Commission to order the Companies to pay avoided cost rates to QFs that are in excess of the utilities’ avoided costs. The Federal Energy Regulatory Commission (“FERC”) has unequivocally ruled that if utilities are required by state law or policy to sign contracts that include rates for QF sales that are in excess of avoided costs, those contracts will be considered to be void *ab initio*. *Connecticut Light and Power*, 70 FERC ¶ 61, 012, 61, 030 (1995);

Southern California Edison Company, San Diego Gas & Electric Company, 70 FERC ¶ 61,215 (1995).

The Companies do not know exactly how this proceeding will impact Idaho's avoided cost rates. However, in the past when avoided cost rate changes were being considered, it has been common practice for QF developers to greatly accelerate their efforts to require utilities to enter into long-term (20-year) contracts at then-current PURPA rates, thereby preserving their right to be paid higher prices if the Commission ultimately adopts a new SAR methodology that results in lower avoided cost rates. This "race for the door" creates a "heads the QF developer wins, tails the utility loses" situation. That is, the QF developer can sign a contract and lock in current PURPA rates and, if it eventually turns out those rates are higher than the rates ultimately determined by the Commission, the QF developer has locked in a higher price for up to 20 years. If, on the other hand, the Commission determines that the new rates should be higher than the ones in effect at the time the QF developer enters the contract, the QF developer may simply default on the contract, restructure its project with a new LLC, and then seek a new contract at the new higher PURPA rates.

For these reasons, the Companies believe that at the outset of this proceeding the Commission should establish criteria that QF developers must satisfy to enter into, or maintain, PURPA contracts at the existing PURPA rates. Those criteria should be simple and should require QF developers to have some "skin in the game" to prevent the developers from entering into PURPA contracts as a free "option," which they will allow to expire if new avoided cost rates turn out to be higher than the current PURPA rates. The Companies request that the Commission consider requiring QF developers

to, at a minimum, meet a two-pronged standard for entitlement to a contract at the existing PURPA rates.

Two-Pronged Standard

1. At the time the contract is signed, the QF developer would be required to post cash or an acceptable letter of credit in an amount equal to the greater of \$45 per kW multiplied by the nameplate capacity of the project or an amount equal to three months revenue under the contract. This amount would be a liquidated damages amount that would be retained by the utility if the QF failed to diligently pursue the interconnection application process, defaulted on the PPA or if the QF failed to achieve commercial operation on its scheduled operation date.

2. At the time the PPA is signed, the QF must have obtained, at a minimum, a feasibility study report from the interconnection provider. In addition, at all times, the QF developer must continue to diligently pursue the interconnection process and must maintain steady progress in the interconnection queue until it executes a generation interconnection agreement. If the developer fails to maintain steady progress, including a failure to enter into a generation interconnection agreement, the PPA would be terminated and the utility would retain the liquidated damages amount previously described.

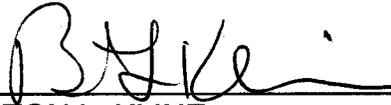
Compliance with the standards proposed by the Companies will not prevent viable QF projects from executing PPAs containing the current published avoided cost rates. Rather, adoption of standards, including the two standards proposed by the Companies, will merely discourage speculation by developers whose proposed projects are highly speculative.

The Companies recognize there may be other issues that need to be addressed with respect to QF contracts while the Commission considers the desirability of modifying the SAR methodology. For example, the Companies suggest that the Commission consider authorizing utilities to include in QF contracts signed during the pendency of this case a provision reserving to the Commission the right to prospectively reduce avoided cost rates paid under the contract to account for the value of the REC's associated with the power generated by such QF's if the Commission ultimately determines in this case that REC's should be retained by the QF.

III. Conclusion

The Companies urge the Commission to conclude that the current SAR, a gas-fired CCCT, no longer represents the type of generation resource that the Companies will defer or avoid by acquiring power from QFs. Accordingly, the Companies respectfully request that the Commission adopt a wind-based SAR methodology. The Companies further request that the Commission establish criteria, including at a minimum the standards discussed herein, that QF developers must satisfy in order to enter QF contracts during the pendency of this proceeding.

DATED this 18th day of September 2009.



BARTON L. KLINE
Attorney for Idaho Power Company



MICHAEL G. ANDREA
Attorney for Avista Corporation

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 15th day of September 2009 I served a true and correct copy of IDAHO POWER'S AND AVISTA'S INITIAL JOINT COMMENTS upon the following named parties by the method indicated below, and addressed to the following:

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