IDAHO POWER®
An IDACORP Company

RECEIVED
2009 OCT 16 AM 11:52
IDAHO PUBLIC UTILITIES COMMISSION

DONOVAN E. WALKER
Senior Counsel
dwalker@idahopower.com

October 16, 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, Avista's and Rocky Mountain Power's Joint Sur-Reply to Exergy's Reply 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,

Donovan E. Walker

DEW:sh
Enclosures

BARTON L. KLINE (ISB No. 1526)
DONOVAN E. WALKER (ISB No. 5921)
Idaho Power Company
P.O. Box 70
Boise, Idaho 83707
Telephone: 208-388-5825
Facsimile: 208-388-6936
bkline@idahopower.com
dwalker@idahopower.com

Attorneys for Idaho Power Company

Street Address for Express Mail:
1221 West Idaho Street
Boise, Idaho 83702

MICHAEL G. ANDREA (ISB No. 8308)
Avista Corporation
1411 East Mission Avenue—MSC-23
Spokane, Washington 99202
Telephone: 509-495-2564
Facsimile: 509-777-5468
michael.andrea@avistacorp.com

Attorney for Avista Corporation

Daniel E. Solander
Rocky Mountain Power
201 South Main
Salt Lake City, Utah 84111
Telephone: 801-220-4014
Facsimile: 801-220-3299
daniel.solander@pacificorp.com

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF A REVIEW OF THE SURROGATE AVOIDABLE RESOURCE (SAR) METHODOLOGY FOR CALCULATING PUBLISHED AVOIDED COST RATES	CASE NO. GNR-E-09-03 IDAHO POWER COMPANY's, AVISTA CORPORATION'S, AND ROCKY MOUNTAIN POWER'S JOINT SUR-REPLY TO EXERGY'S REPLY COMMENTS

I. Background

In Order No. 30922, issued in this case on October 6, 2009, the Commission authorized the parties that had filed comments on September 18, 2009, Idaho Power Company, Avista Corporation, and Rocky Mountain Power (collectively "Utilities"), Commission Staff ("Staff"), Idaho Wind Farms, and Sagebrush Energy to file sur-reply comments responding to the reply comments Exergy Development Group of Idaho, LLC ("Exergy") filed on September 29, 2009.

Exergy's reply comments were generally critical of the Staff's and Utilities' recommendations that the Commission adopt a new Surrogate Avoided Resource ("SAR") based on the cost of a generating facility using wind as its motive force ("Wind SAR"). Exergy focused most of its attention on two recommendations for adjustments to avoided costs included in the comments of the Utilities and Staff. The first recommendation called for the Commission to consider the value of renewable energy credits ("RECs") in setting avoided cost rates. Second, the Utilities suggested that the income tax subsidies wind generation projects receive should also be considered by the Commission in setting avoided cost rates. In its reply comments, Exergy objected to both of these recommendations on public policy grounds. In addition, Exergy argued that both PURPA and the United States Constitution would be violated if the Commission accepted either of these recommendations and considered the value of RECs and tax subsidies in setting avoided cost rates based on a Wind SAR.

In these Sur-Reply Comments, the Utilities will not address the general policy positions taken by Exergy. But the Utilities do need to correct some inaccuracies in Exergy's description of their recommendations to consider the value of RECs and tax subsidies in setting avoided cost rates and respond to the legal arguments raised by Exergy. It is important that the Commission understand that, contrary to Exergy's assertions, PURPA and the U.S. Constitution do *not* prevent the Commission from considering the value of RECs and tax subsidies in setting published avoided cost rates based on the cost of a Wind SAR.

II. **The Commission Must Set the Published QF Rates Equal to the Utilities Avoided Costs.**

There is no disagreement in any of the filed comments concerning the ratemaking standard the Commission must meet when it sets avoided cost rates. On the top of page 3 of its Reply Comments, Exergy states: "Under PURPA section 210(b), however, the rate to be paid for such power is not to exceed the "incremental cost to the utility of alternative electric energy." 16 U.S.C. §824a-3(b)(d)."

On page two of its comments, Staff states: "Under PURPA Section 210(b) the rate to be paid for such power is not to exceed "the incremental cost to the utility of alternate electric energy." Staff's comments also state: "There are two general caveats under PURPA: (1) electric utilities are not required to pay more than the utility's avoided costs for purchases of QF capacity and energy (PURPA Section 210(b); 18 C.F.R. § 292.304(a)(2)); and (2) co-generators and small power producers in their sales to utilities are not to be subjected to pervasive utility type regulations, i.e., regulation respecting (i) the rates of electric utilities; and (ii) the financial and organizational regulation of electric utilities. PURPA Section 210(e); 18 C.F.R.§ 292.602(c)(1)(i)(ii)."

In their joint comments, on pages 6 and 7, Idaho Power and Avista cited two FERC cases[1] in which the Federal Energy Regulatory Commission ("FERC") 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*.

---

[1] *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).

III. <u>The Wind SAR Methodology Would Not Violate PURPA</u>

Exergy argues that the Wind SAR Methodology proposed by the Utilities and Staff would violate PURPA by depriving wind energy developers of RECs. Exergy is incorrect.

FERC has clearly stated that the ownership of RECs is not controlled by PURPA and that states have the power to determine who owns RECs in the first instance. *American Ref-Fuel Co., et al.*, 105 FERC ¶ 61,004, P 23 (2003), *order on reh'g*, 107 FERC ¶ 61,016 (2004). Moreover, FERC made clear that states may decide that a sale of power at wholesale automatically transfers ownership of RECs. *Id.* Therefore, regardless of whether the Commission decides to indirectly compensate customers for the value of REC's by reducing avoided cost rates to reflect the value of RECs or assign RECs to the purchasing utility the Wind SAR methodology proposed by the Utilities and Staff would be consistent with FERC precedent and would not in any way violate PURPA.

IV. <u>RECs and Tax Subsidies Are Available to Non-QFs</u>.

As the Staff and the Utilities all noted in their comments, all three utilities are currently in the process of acquiring wind generation resources outside of the PURPA process. As a result, all three utilities will obtain the RECs associated with their acquisition of these wind resources. In addition, the three utilities will also benefit from, either directly or indirectly, the substantial tax subsidies that are currently available to developers of wind resources. This is why the Utilities have proposed that published avoided costs based on a wind SAR should be adjusted to reflect both the value of RECs and the value of tax subsidies. If avoided costs are not reduced to reflect these benefits, then utility customers will be paying more than the "incremental cost of alternative electric energy." (PURPA 210(b).)

V. <u>Exergy's Preemption Argument Is Not Applicable</u>.

On page 6 of its Reply Comments, Exergy asserts that the Commission is legally prohibited from considering the value of renewable resource tax subsidies, when setting published avoided cost rates based on a Wind SAR. Exergy claims that adjusting avoided cost rates to consider the tax subsidies available to wind resource developers would violate PURPA and the supremacy clause of the United States Constitution. The premise of Exergy's constitutional argument is the doctrine of preemption; that federal law occupying the same field preempts state law. Exergy characterizes Congress' amendments to the federal tax code providing subsidies for developers of wind resources, as "federal law" and this Commission's setting of avoided cost rates as "state law". On page 7 of its Reply Comments Exergy states: "The Commission, therefore, has no authority to adopt a Wind SAR methodology that decreases the avoided cost rate by the amount of the federal tax credits because federal law preempts such state action."

Exergy misunderstands both the preemption doctrine and the genesis of the PURPA law. PURPA *is* federal law. When this Commission sets avoided cost rates, it is enforcing federal law, not state law. Exergy's attempt to apply the preemption doctrine to this Commission's mandated actions under PURPA, misses this fundamental point.

A very brief summary of the intersecting federal laws that established the respective roles of this Commission and the FERC in setting QF rates is necessary at this point. For all investor-owned public utilities, jurisdiction over rates for sales at wholesale, in interstate commerce, is vested exclusively in the FERC. In 1927, in *Public Utilities Commission of Rhode Island v. Attleboro Steam & Electric Company*, 273 U.S. 83 (1927), the Supreme Court held that rates for sales of electric energy in interstate commerce are beyond the reach of a state authority. The Court added that regulation of such rates "can only be obtained by the exercise of the power vested in Congress." (*Id.* at pp. 86-90.)

Congress did not change this basic federal-state jurisdictional scheme when it passed PURPA in 1978. Sales between QFs and utilities are still sales at wholesale in interstate commerce. Therefore, ultimate jurisdiction over the rates QFs are paid for sales at wholesale is still vested in the FERC. However, in creating the PURPA rate-setting mechanism, Congress directed the FERC to allow the state regulatory commissions to set wholesale rates for QFs, *so long as* the state regulatory commissions complied with the rules established by FERC. As a result, setting avoided cost rates is not a function of state law. It is a function of federal law performed by state regulatory commissions.

The United States Supreme Court recognized this unique situation in the case of *Federal Energy Regulatory Com'n v. Mississippi*, 102 S. Ct. 2126 (1982). In its opinion in *Mississippi*, the Court stated, "Section 210(f), 16 U.S. Code § 824a-3(f) requires each state regulatory authority and non regulated utility to implement FERC's rules." (*Id.* at 2133.) The Court in the *Mississippi* case explained the role of state commissions under PURPA as follows:

> In essence, then, the statute and the implementing regulations simply require the Mississippi authorities to adjudicate disputes arising under the statute. Dispute resolution of this kind is the very type of activity customarily engaged in by the Mississippi Public Service Commission. (*FERC v. Mississippi* 102 S.Ct. 2126, 2137 (1982).)

The Court went on to say:

> So it is here. The Mississippi Commission has jurisdiction to entertain claims analogous to those granted by PURPA, and it can satisfy § 210's (of PURPA's) requirements simply by opening its doors to claimants. (*FERC v. Mississippi 102 S. Ct. 2126, 2138 (1982).)*

As can be seen from the *Mississippi* case, PURPA provided a federal preemption of QF rate setting long before wind resource tax subsidies were included in the federal tax code. When this Commission sets avoided cost rates there is no preemption of state law.

Later in its comments, Exergy states "the federal tax credits for renewable projects preempt adoption of the proposed Wind SAR because the proposed SAR would deprive QFs of the value of the tax credit." (Exergy Reply Comments, p. 7.) Not true. Regardless of how the Commission sets avoided cost rates, QFs will still get the full value of the tax credits from the IRS. But changing the tax code did not eliminate PURPA's requirement that the Commission set avoided cost rates to match the incremental cost the utility would incur if it constructed the Wind SAR and obtained the tax subsidies. There is no conflict between the statutes. PURPA and the tax code still work exactly, and separately, as directed by Congress. Congress changed the tax code, not PURPA. If Congress had wanted to amend PURPA to direct this Commission to ignore the effect of tax subsidies in setting PURPA avoided costs, it would have been simple for it to express that intent. But, if the Commission ignores the tax subsidies when it assesses avoided costs, then it is almost certainly setting published avoided cost rates that do not track with the costs the utility would incur if it constructed a Wind SAR itself or purchased energy from a wind project as a result of a competitive bidding process.

VI. <u>Considering the Utility's Cost of Alternative Resources Is Not Discriminatory</u>.

Finally, Exergy argues that considering tax subsidies when setting avoided cost rates violates PURPA because "by depriving wind QFs under 10 average MW of the renewable energy tax credit available to larger wind projects in the competitive bidding process, the Commission would discriminate against qualifying small producers in violation of PURPA." (Exergy Reply Comments, p. 1.) Again, no one is proposing that the tax credits should or can be taken from QFs. What Exergy is really proposing is that the Commission grant QFs a preference. If the utility would have received the benefits of the tax subsidies when it constructed a Wind SAR or acquired wind energy in a competitive bidding process, *failing* to recognize the effect of the tax credits in setting published avoided costs would actually provide a preference to QFs and result in higher customer rates. PURPA does not allow either of those results.

VII. <u>RECs Do Have Value for Utilities</u>.

On page 8 of its Reply Comments, Exergy asserts that RECs have no resale value to utilities that operate in jurisdictions that have adopted renewable portfolio standards ("RPS"). Exergy states that "the utility will not resell the RECs if it developed its own wind resource because those RECs would go toward meeting the utility's targeted RPS." (Exergy Reply Comments, p. 8.) Exergy paints with too broad a brush. Idaho Power, for example, operates in one state with no RPS standard, Idaho, and another, Oregon, in which it has a small RPS requirement. Currently, Idaho Power generates more RECs than it needs to satisfy the requirements of the Oregon RPS. As a result, Idaho Power has excess RECs that it can sell.

At a minimum, the inability to obtain the RECs associated with the purchase of PURPA resources imposes an opportunity cost on any utility with an RPS requirement. All utilities <u>must</u> purchase PURPA resources. If no RECs come with a PURPA resource purchase, then the utility with an RPS requirement must either build more resources or buy RECs on the market to satisfy its RPS requirements. This is a cost that would be mitigated by lower avoided cost rates. RECs have value for utilities, RPS or not.

VIII. <u>The Commission Can Require Liquidated Damages and Security as a Condition of Obtaining a QF Contract</u>.

In its Reply Comments, Exergy makes the sweeping statement, "The Commission has no authority to provide remedies for breach of a QF contract." (Exergy Reply Comments, p. 9.) In that same section of its brief, Exergy goes on to assert that the inclusion of security for liquidated damages would violate the QFs due process rights. (Exergy Reply Comments, p. 10.) Exergy claims that the only way that a utility can recover damages is through litigation in the courts. (Exergy Reply Comments, p. 10.)

Exergy's arguments are strawmen. The Commission's authority to assess damages or fashion remedies in a QF contract *after* a QF contract has been signed and approved by the Commission is irrelevant. Utilities are proposing that the Commission, as a condition of approving QF contracts entered into during the pendency of this proceeding, direct the utilities to include a liquidated damages provision in the contract and require the contracting QF to post cash or a cash equivalent to secure the liquidated damages. Liquidated damages are routinely included in contracts when the parties know at the outset of the contract that it will be difficult to precisely determine the amount of damages if there is subsequent breach of the contract. For this very reason, liquidated damages provisions have been a part of many QF contracts previously approved by this Commission. The inclusion of liquidated damages in a QF contract has nothing to do with whether a court or the Commission is the appropriate forum for subsequent resolution of utility contract disputes.

The Idaho Supreme Court has already determined in two separate cases that the Commission has the necessary jurisdiction under PURPA to approve QF contracts and determine when a QF is entitled to a contract which includes rates, terms, and conditions approved by the Commission. The first case was *Empire Lumber v. Washington Water Power*, 114 Idaho 191, 755 P.2d 1229 (1988). The other case was *A.W. Brown Company, Inc., v. Idaho Power Company*, 121 Idaho 812, 828 P.2d 841 (1992). In the *A.W. Brown* case, the Court held,

> Finally, Brown argues that the PUC had no jurisdiction 'to litigate the common law contract issues between Brown and Idaho Power that neither party had even pleaded.' We disagree. Regarding whether Brown either had or was entitled to a contract with Idaho Power, this court stated in *Empire Lumber, supra*, that the Commission 'has jurisdiction to hear complaints against utilities alleging violation of any provision of law . . . and is the appropriate forum to . . . determine whether a regulated utility has an obligation under PURPA to purchase power from an applicant.

114 Idaho at 192, 755 P.2d 1229. (*A. W. Brown* 121 Idaho 812, 819 (1992)

In this proceeding, the Utilities are asking the Commission to do exactly what the Idaho Supreme Court said the Commission could do in the *Brown* and *Empire* cases. They are asking that the Commission require QF developers, as a condition of obtaining a contract during the pendency of this proceeding, to agree to include a liquidated damages provision and to post security to fund those liquidated damages if there is a breach of the contract. Such a requirement falls clearly within the scope of the Commission's jurisdiction as demonstrated in *A.W. Brown* and *Empire.*

IX. Conclusion.

Exergy's assertions that the proposed Wind SAR violates PURPA and that the Commission is legally precluded from considering RECs or tax subsidies when setting avoided cost rates under a wind SAR methodology are not well founded. If the Commission decides that it is in the public interest to consider using a wind SAR to determine avoided cost rates, the Commission is free to consider any of the recommendations for rate adjustments made by Staff or the Utilities.

DATED at Boise, Idaho, this 16th day of October 2009.

for

BARTON L. KLINE
Attorney for Idaho Power Company

MICHAEL G. ANDREA
Attorney for Avista Corporation

DANIEL SOLANDER
Attorney for Rocky Mountain Power

a contract during the pendency of this proceeding, to agree to include a liquidated damages provision and to post security to fund those liquidated damages if there is a breach of the contract. Such a requirement falls clearly within the scope of the Commission's jurisdiction as demonstrated in *A.W. Brown* and *Empire*.

IX. Conclusion.

Exergy's assertions that the proposed Wind SAR violates PURPA and that the Commission is legally precluded from considering RECs or tax subsidies when setting avoided cost rates under a wind SAR methodology are not well founded. If the Commission decides that it is in the public interest to consider using a wind SAR to determine avoided cost rates, the Commission is free to consider any of the recommendations for rate adjustments made by Staff or the Utilities.

DATED at Boise, Idaho, this 16th day of October 2009.

BARTON L. KLINE
Attorney for Idaho Power Company

MICHAEL G. ANDREA
Attorney for Avista Corporation

DANIEL SOLANDER
Attorney for Rocky Mountain Power

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 16th day of October 2009 I served a true and correct copy of IDAHO POWER COMPANY'S, AVISTA CORPORATION'S, AND ROCKY MOUNTAIN POWER'S JOINT SUR-REPLY TO EXERGY'S REPLY COMMENTS upon the following named parties by the method indicated below, and addressed to the following:

Commission Staff Scott Woodbury Deputy Attorney General Idaho Public Utilities Commission 472 West Washington P.O. Box 83720 Boise, Idaho 83720-0074	X Hand Delivered ____ U.S. Mail ____ Overnight Mail ____ FAX X Email scott.woodbury@puc.idaho.gov
Avista Corporation Michael Andrea Avista Corporation 1411 East Mission Avenue P.O. Box 3727 Spokane, Washington 99220	____ Hand Delivered X U.S. Mail ____ Overnight Mail ____ FAX X Email micahel.andrea@avistacorp.com
Rocky Mountain Power Daniel E. Solander Rocky Mountain Power 201 South Main Salt Lake City, UT 84111	____ Hand Delivered X U.S. Mail ____ Overnight Mail ____ FAX X Email danel.solander@pacificorp.com bruce.griswold@PacifiCorp.com
J. Ted Weston Rocky Mountain Power 201 South Main Street, Suite 2300 Salt Lake City, Utah 84111	____ Hand Delivered X U.S. Mail ____ Overnight Mail ____ FAX X Email ted.weston@pacificorp.com
Exergy Development Group of Idaho, LLC Peter J. Richardson Greg Adams RICHARDSON & O'LEARY 515 N. 27th Street P.O. Box 7218 Boise, Idaho 83702	____ Hand Delivered X U.S. Mail ____ Overnight Mail ____ FAX X Email peter@richardsonandoleary.com greg@richardsonandoleary.com

Sagebrush Energy, LLC Dean J. Miller MCDEVITT & MILLER P.O. Box 2564 Boise, Idaho 83701	____ Hand Delivered _X_ U.S. Mail ____ Overnight Mail ____ FAX _X_ Email joe@mcdevittmiller.com
Idaho Forest Group, LLC Dean J. Miller MCDEVITT & MILLER P.O. Box 2564 Boise, Idaho 83701	____ Hand Delivered _X_ U.S. Mail ____ Overnight Mail ____ FAX _X_ Email joe@mcdevittmiller.com
Idaho Windfarms, LLC Glenn Ikemoto Idaho Windfarms, LLC 672 Blair Avenue Piedmont, California 94611	____ Hand Delivered _X_ U.S. Mail ____ Overnight Mail ____ FAX _X_ Email glenni@pacbell.net

Dean E. Miller for

Barton L. Kline