

DECISION MEMORANDUM

**TO: COMMISSIONER KJELLANDER
COMMISSIONER SMITH
COMMISSIONER HANSEN
COMMISSION SECRETARY
COMMISSION STAFF
LEGAL**

FROM: SCOTT WOODBURY

DATE: APRIL 14, 2003

**RE: CASE NO. IPC-E-03-1 (Idaho Power)
PURPA QF CONTRACT W/ TIBER MONTANA, LLC**

On February 20, 2003, Idaho Power Company (Idaho Power; Company) filed an Application with the Idaho Public Utilities Commission (Commission) requesting approval of a Firm Energy Sales Agreement (Agreement) between Idaho Power Company and Tiber Montana LLC (Tiber).

Tiber proposes to design, construct, install, own, operate and maintain a 7.5 MW hydroelectric generating facility (project) located on the outlet works of the existing Tiber Dam. The Tiber Dam is located 15 miles South of the City of Chester in Liberty County, Montana. Tiber warrants that the project is a "qualifying facility" (QF), as that term is used and defined in the Public Utilities Regulatory Policies Act of 1978 (PURPA). Tiber has elected an operation date of May 15, 2004.

Agreement

Idaho Power represents that the February 3, 2003, Agreement with Tiber is pursuant to rates, terms and conditions approved by the Commission. Reference Case No. GNR-E-02-1, Order Nos. 29069 and 29124. The Agreement is for a 20-year term and commits Tiber to deliver energy to the Company only during the months of May, June, July, August, September and October of each contract year. Tiber's project is located outside of Idaho Power's service territory. The entity transmitting the project's power to Idaho Power's transmission system (transmitting entity), Northwestern Energy, has purportedly agreed to "firm" all energy

deliveries from Tiber to Idaho Power. Reference Agreement Section 9. This arrangement will result in flat monthly firm energy being scheduled into the Idaho Power system.

Idaho Power states that certain terms and conditions of the submitted Agreement reflect updated and/or revised contract language in conformance with current IPUC Orders, current technologies and current utility energy standards. The included changes can be briefly described as follows:

1. Measurement of the 10 MW rating

In lieu of a reference to nameplate rating, Idaho Power and Tiber have agreed to include the concept of “optional energy.” Optional energy is defined as energy which is produced by the QF, scheduled by the transmitting entity and delivered to the point of delivery in an amount that exceeds 10,000 kWh in any single hour. The Agreement provides that Idaho Power is not obligated to purchase optional energy. Idaho Power contends that this arrangement allows Tiber to install generating capacity with a nameplate rating of 10 MW or more while still qualifying to be paid at the posted rates that the Commission has established for projects smaller than 10 MW.

2. Encouraging increased “firmness” of QF contracts.

Although contracts between Idaho Power and QFs have been denominated as “Firm Energy Sales Agreements”, Idaho Power contends that the energy purchased under these contracts is not firm energy as that term is commonly defined by the electric energy industry. Firm energy purchases Idaho Power makes from non-QF suppliers specify the amounts to be delivered during heavy load or light load hours for the term of the contract. If the energy is not delivered in the specified amounts, at the specified times, liquidated damage provisions in the purchase agreement allow Idaho Power to acquire the energy from other sources and receive reimbursement from the defaulting supplier for all the Company’s costs.

In Tiber’s case, Idaho Power contends that the arrangement with Northwestern Energy to firm Tiber’s generation makes the Agreement more like a true firm energy purchase. In an effort to bring QF performance more in line with actual firm energy production and to provide an opportunity for QFs using various generating technologies to receive the posted firm rates based on a QF’s actual performance, Idaho Power and Tiber have included in the Agreement provisions which encourage Tiber to provide energy with a greater degree of firmness while at the same time allowing a reasonable amount of flexibility to Tiber in operating

its facility. Reference Agreement Section 1.15—Surplus Energy and Section 7.1.2—Adjustment to Net Firm Energy Purchase Price.

Under Agreement Section 1.15, each month the actual net kW hours of Tiber's generation will be compared to the monthly kW hours of generation estimated by Tiber (Section 6.2). If Tiber's actual kW hours of generation exceeds 110% of a month's estimated kW hours of generation, the energy in excess of 110% is valued at the surplus energy price. Reference Agreement Section 7.2. The surplus energy price is a market-based price.

Under Agreement Section 7.1.2, Tiber's actual net monthly kW hours of generation is compared to the estimated monthly kW hours of generation as described in Section 6.2. If the amount of net firm energy is 90% or less of the month's estimated kilowatt hours of generation, all of that month's generation will be deemed to be surplus energy for which Idaho Power will pay Tiber the surplus energy price.

Under the Agreement, Tiber can reset the monthly estimated generation amounts to reflect its increased operating experience and to allow Tiber to respond to changes in water supplies, etc. The only limitation placed on Tiber by the Company is that the net firm energy estimated for each month cannot exceed the nameplate rating of the generation equipment.

3. Seasonality.

Idaho Power notes that previous Commission Orders and QF Agreements have recognized that the value of energy generated differs in accordance with the season in which it is actually delivered to Idaho Power. As an incentive for a QF to deliver energy to the Company during times when it is of greater value to the Company, the posted rates have historically "been seasonalized." To better align the seasons with the months in which Idaho Power has identified actual energy needs, the Agreement modifies the months within each historical "season" to account for those periods of higher demand. The months of August and September have been moved to season 3 and the months of November and December have been moved to season 2. The seasonal rates are identified in Section 7.1.1 of the Agreement. This adjustment, the Company contends, does not change the overall annual average payment—the average payment continues to be the posted rate.

Section 19 of the Agreement provides that the Agreement will not become effective until the Commission has approved all of the Agreement's terms and conditions and declared

that all payments Idaho Power makes for purchases of energy to Tiber will be allowed as prudently incurred expenses for ratemaking purposes.

On March 17, 2003, the Commission issued Notices of Application and Modified Procedure in Case No. IPC-E-03-01. The deadline for filing written comments was April 4, 2003. The Commission Staff was the only party to file comments.

Staff Comments

Staff finds that the rates contained in the Agreement comport with Order No. 29124, the most recent Commission Order establishing avoided cost rates. Staff additionally addresses the following terms and conditions of the submitted Agreement:

Measurement of the 10 MW rating

Staff believes that Idaho Power's proposal to use net generation measured on an hourly basis in determining whether the project is under the 10 MW threshold is reasonable. Staff believes that net generation of the QF project in a single hour, rather than gross average generation or nameplate capacity, is what should be used to define its capacity for eligibility of posted rates. In the present case, because the nameplate rating of the Tiber project is proposed to be 7.5 MW, Idaho Power believes optional energy is not likely to be an issue. Staff agrees. With a nameplate capacity of 7.5 MW and considering Northwestern Energy's agreement to firm the project's output on a monthly basis, Staff contends that unless Tiber expands its capacity at some point in the future, it would be impossible for net generation measured on an hourly basis to exceed 10,000 kWh in any hour .

Staff notes that Idaho Power's proposal would allow Tiber (or other QFs if this provision is included in future contracts) to install generating capacity with a nameplate rating greater than 10 MW while still qualifying to be paid the posted rates established for projects smaller 10 MW. In theory, Staff posits, a very large project could elect to sell only 10 MW of its output under a PURPA contract at the posted rates, leaving the remaining output to be sold in some other manner. Staff believes the principles outlined in Order No. 26772 (Case No. UPL-E-96-5, the "Earth Power Case") should continue to be followed with regard to whether multiple 10 MW contracts, perhaps with different utilities, would be permitted if the proposed Tiber contract terms are adopted. In Order No. 26772, the Commission ruled that the term "project" equates with "qualifying facility." Thus, each qualifying facility is only entitled to one PURPA contract. If this principle were followed with regard to the 10 MW project size threshold, it would

preclude a large project from breaking the generation into several 10 MW blocks for sale at posted rates under multiple contracts or to multiple utilities. However, it would not prevent a large project from selling 10 MW of its output under a single contract to one utility and marketing the remainder outside of PURPA.

Encouraging increased "Firmness" of QF contracts

Idaho Power and Tiber have included provisions in the Agreement to bring Tiber's project performance more in line with projects that actually provide firm energy production. Staff agrees with Idaho Power that the generation provided by many QF projects is not "firm" as defined by industry standards. Staff also agrees that the posted avoided cost rates adopted by the Commission are based on the costs of a combined cycle combustion turbine that would provide firm generation. However, while Staff believes it is reasonable in this case to include contract provisions regarding project standards of firmness given Tiber's concurrence, Staff notes that this is not a provision that has been required by the Commission in the past and should be further evaluated if opposed by developers in the future. Staff notes that there is a wide variation in the predictability and "firmness" of existing projects. Staff believes that Idaho Power's proposal in this contract to require the project to commit two years in advance to monthly generation amounts accomplishes the Company goal of attaining planning certainty, but stops short of penalizing the project for inability to predict generation hours, days or weeks in advance. As a result, this project can qualify for firm energy rates if the developer can reasonably predict monthly generation levels.

Whether the 90% minimum or the 110% cap are the appropriate bands of variance for projects other than Tiber or whether firmness standards should be required at all should be determined, Staff believes, at the time other projects seek contracts with Idaho Power.

Seasonality

Idaho Power has seasonalized the rates in this Agreement. The proposed seasonalization, however, differs from the way that posted rates have historically been seasonalized by the Company. Staff notes that neither the 2002 Garnet report nor the Company's 2002 RFP precisely support the proposed modifications to the months included in each season, although they do support it generally. The fact is, Staff contends, that Idaho Power's months of greatest need or surplus change over time as new resources are acquired. While the changes

proposed by the Company may be reasonable at this point in time, Staff contends that different months may be more appropriate for each season in future contracts.

Staff recommends that the Agreement be approved and that those non-standard terms unique to this contract (i.e., measurement of the 10 MW rating, encouraging increased firmness, and seasonality) not be viewed as establishing precedent.

Commission Decision

Idaho Power and Tiber have presented a negotiated PURPA contract for Commission approval. The contract rates are unlevelized and conform to Commission posted rates for QFs smaller than 10 MW. Staff recommends that the Agreement be approved and that the non-standard terms unique to the contract be clearly identified as not establishing precedent. Does the Commission find it reasonable to approve the contract with the qualified language as recommended by Staff? Does the Commission agree that payments made under the Agreement should be allowed as prudently incurred expenses for ratemaking purposes?

Scott Woodbury

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