DECISION MEMORANDUM

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

FROM: **SCOTT WOODBURY**

DATE: **MARCH 25, 2004**

RE: **CASE NO. IPC-E-04-1 (Idaho Power)**
AGREEMENT FOR SALE AND PURCHASE OF ELECTRIC ENERGY
IDAHO POWER/UNITED MATERIALS OF GREAT FALLS, INC.

On February 4, 2004, Idaho Power Company (Idaho Power; Company) filed an Application with the Idaho Public Utilities Commission (Commission; IPUC) requesting approval of an Energy Sales Agreement (Agreement) between Idaho Power and United Materials of Great Falls, Inc. (United Materials) dated January 6, 2004.

United Materials proposes to design, construct, install, own, operate and maintain a 9 MW wind generating facility (the Horseshoe Bend Wind Park or the Project) located at the United Materials industrial facility near Great Falls, Montana. The Project will be a qualified small power production facility (QF) under the Public Utilities Regulatory Policy Act of 1978 (PURPA).

As represented by Idaho Power, the Agreement includes purchase prices consistent with the "posted rates" approved by the Commission in Order No. 29391. United Materials has elected to contract with Idaho Power for a 20-year term and has agreed to arrange for delivery of energy to the Idaho Power electrical system across the system of another utility.

The submitted Agreement is the first wind energy sales agreement to be executed by Idaho Power. Idaho Power reports that it has developed a cogeneration small power producer (CSPP; QF) agreement concept that is consistent for all QF projects regardless of their energy resource (wind, hydro, geothermal, wood waste, etc.) that incorporates (1) current IPUC Orders, (2) current technologies, and (3) current utility industry standards. The submitted Agreement,

the Company states, contains many of these concepts as well as several unique provisions since the project is not directly connected to the Idaho Power system. The following is a brief description of some of these concepts and unique provisions:

A. **Opportunity for QFs to Participate in the Firm Energy Sales Agreement**: In order to eliminate the need to predetermine the firm or non-firm status of a Qualifying Facility (QF) resource (i.e., wind, hydro, biomass) and, instead, to provide an opportunity for QF resources to receive the Firm Published Avoided Cost Rate based upon the QF's actual performance, Idaho Power has included the concepts of "Shortfall Energy" and "Surplus Energy." Reference Agreement Sections 1.21 and 1.24.

Surplus Energy: Under the concept of "Surplus Energy," the QF is required to estimate its monthly kWh generation (Agreement Section 6.2). Each month, the actual net kWh of generation will be compared to the monthly kWh of generation estimated by the QF developer. If a project's actual kWh of generation exceeds 110% of a month's estimated kWh of generation, the energy in excess of 110% is valued at the Surplus Energy Price as described in Agreement Section 7.3. The Surplus Energy Price is a market-based price.

Shortfall Energy: Under this concept, a project's actual net monthly kWh of generation is compared to the estimated monthly kWh of generation. In accordance with Agreement Section 1.21, if the amount of Net Energy is less than ninety percent (90%) of the month's estimated kWh of generation, the difference between the actual net monthly kWh of generation and 90% of the estimated monthly kWh of generation is defined as "Shortfall Energy." If the market energy cost as defined in Agreement Section 1.13 is greater than the Agreement's price for energy in the month that shortfall energy occurs, then a "Shortfall Energy payment" is off-set against the project's energy payment. If the market

energy cost is less than the Agreement's price for energy for the month in which Shortfall Energy occurs, no Shortfall Energy payment is calculated.

Whether a QFs energy production is Surplus Energy, Shortfall Energy or qualifies for the firm published avoided cost, the Company states, is at the sole discretion of the developer since the developer sets the monthly estimated generation levels. The only limitation placed upon the developer by the Company is that the Net Energy estimated for each month cannot exceed the nameplate rating of the generation equipment and/or the capacity rating of the interconnection equipment. The Project has chosen to make use of non-firm transmission capacity to deliver the Project's energy to Idaho Power. United Materials must therefore consider the risk of energy delivery reductions due to transmission capacity interruptions in setting its estimated Monthly Net Energy amounts.

B. **Seasonality**: As an incentive for United Materials to deliver energy to the Company during times when it is of greater value to Idaho Power, the published avoided cost rate is "seasonalized." The seasons generally correspond to the months in which Idaho Power has identified actual energy needs and periods of higher demand. Reference Agreement Sections 6.2 and 7.1.

C. **Firm Energy Deliveries**: The United Materials Project is located outside of Idaho Power's service territory. Northwestern Energy, the Transmitting Entity for this project, has agreed, on an hourly basis, to firm all energy deliveries from United Materials to Idaho Power and to other scheduling requirements as specified in Agreement Section 10.

D. **Environmental Attributes**: As reflected in Agreement Article 8, Idaho Power notes its intention to file a Petition for Declaratory Order with the Commission in regards to the "Environmental Attributes." Reference Case No. IPC-E-04-2. Idaho Power is seeking a Commission ruling concerning whether the Environmental Attributes associated with a QF project are owned by the project or the utility at the time a utility purchases electricity from a QF project. The Commission's final Order will be included and become an integral part of the Agreement. United Materials reserves the right to cancel the Agreement within 30 days of the Commission's final Order regarding Idaho Power's Petition.

Agreement Section 22 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 United Materials will be allowed as prudently incurred expenses for ratemaking purposes. Should the Commission approve the Agreement, Idaho Power intends to consider the effective date of the Agreement to be January 6, 2004. United Materials has estimated an operation date of December 31, 2004. As reflected in the Company's Application, the Agreement contains non-levelized published avoided cost rates in conformity with applicable Commission Orders. Because the project is located outside the Idaho Power service territory, no interconnection charges or monthly operation and maintenance charges under Schedule 72 will be assessed.

As reflected in Agreement Section 21.3 United Materials may terminate the Agreement on 60 days prior written notice if (1) the Federal Production Tax Credit or other similar economic incentive is not renewed, modified or created in a manner that enables United Materials to participate in these economic incentives in the same manner as if the Project was commercially online as of the date of the Agreement, (2) and United Materials has not begun construction of the Project. Once construction of the Project has begun, United Materials may not terminate the Agreement as specified in Section 21.3.

Pursuant to Agreement Section 21.2, Idaho Power may terminate the Agreement on 60 days prior written notice if (1) existing Idaho law is modified to allow persons or entities other than Idaho Power to sell electric capacity or energy at retail in Idaho Power's exclusive

service territory, and (2) such change in law results in Idaho Power being unable to fully recover in its retail revenue requirement all costs attributed to this Agreement.

Idaho Power requests that the Commission issue an Order approving the Firm Energy Sales Agreement between Idaho Power and United Materials of Great Falls, Inc. The Company further requests a Commission finding that all payments for purchases of energy under the Agreement will be allowed as prudently incurred expenses for ratemaking purposes.

On February 20, 2004, the Commission issued Notices of Application and Modified Procedure in Case No. IPC-E-04-1. The deadline for filing written comments was March 12, 2004. Commission Staff and five interested parties filed timely comments.

Public Comments

Three of the five commenting parties support the renewable resource contract with one recommending that the Commission approve Idaho Power's Application before the Company changes its mind. A fourth commenter, Mr. Jay Contway, owns property adjacent to the proposed windfarm and voices opposition to the contract. The areas of concern that give Mr. Contway cause to make his protest are: (1) depreciation of land value for future development; (2) noise pollution of the surrounding area, particularly at his home; and (3) aesthetic depreciation of his land caused by the wind powers.

The fifth commenting party offers a critique of the Agreement and contract clauses which, he states, are punitive to the developer in which necessitate an expense of money by the developer to control something over which he really has no control, i.e., the wind. Wind, the commenter states is a viable resource but has some unique characteristics, one of which is that it is intermittent. This he states is far different though than being unreliable. The fact that wind varies on a minute-to-minute, hour-to-hour and day-to-day basis are characteristics that could be successfully integrated into the Company's supply system. Wind power, he states, can be used to upgrade the ability of the Company's existing hydropower facilities to supply peaking energy and can thereby increase the value of such facilities. Idaho Power, he states, needs energy, capacity and peaking capacity. The resource which supplies these needs best is hydropower. The integration of wind energy, a low cost energy, allows the Company to store water and use it when the Company needs to generate power. The problem with wind power, as with other base load energy resources, is that it does not adjust to handle variations in daily, monthly, weekly

and seasonal loads. This ability to follow load (in addition to just plain energy), the commenter states, is what Idaho Power needs.

The commenter suggests that it will be far better for all parties concerned, including customers of Idaho Power, that the money that United Materials is spending on daily, monthly, and annual energy production predictions, the daily redelivery of power by the transmission entity, the capital, operation and maintenance and fuel costs of the "insurance" generation system be paid instead to Idaho Power so that the Company can upgrade and improve facilities that can provide peaking power. The way to upgrade the Company's system, the commenter suggests, is to take in wind and upgrade the existing system to make use of that wind. This means energy storage. Having individual wind farms supply their own backup energy resources, the commenter suggests, is not as nearly as cost effective or as useful to Idaho Power as building what it needs to upgrade the entire system to not only take in wind but to provide far more robust system for every generating resource.

The commenter suggests that we are at a critical juncture. We can either start thinking in terms of upgrading our power system, or continue to simply rely on imported natural gas that can't be controlled by anyone in Idaho. Once we have a new frame of reference, a new leadership for upgrading the system, there are many possibilities, he suggests, that may emerge. The commenter suggests that payments from wind power generators go into a fund that would be used for the upgrading of Idaho Power's systems ability to store energy, to take it from base-load resources at times when the value of this resource is lower and return it when the energy is of higher value. There are considerable benefits to the combination of wind and hydropower, he states. These need to be explored and developed, not ignored.

Commission Staff

Staff has reviewed the rates contained in the Agreement and finds that they comport with the Commission established avoided cost rates in Order No. 29391. Staff notes that this is the first agreement for a wind energy generation project for Idaho Power and that it contains numerous terms and conditions significantly different than have been included in prior QF contracts. Many of the new and/or revised terms and conditions directly affect the amounts Idaho Power will pay to United Materials. Specifically addressed by Staff is (a) the Company's approach to tying contract rates to the degree of firmness of energy supplied and (b) the

Company's realignment of months used in the seasonalization or weighting of the annual prices paid to QFs.

Firm Energy

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

In the past, Staff notes that Commission rules have not established specific performance criteria for QF resources to determine their firm or non-firm status. Nearly all QFs were considered firm energy projects and eligible for the full published avoided cost rates. Now, however, Staff notes that particularly with the introduction of new generation technologies in Idaho, there is a wide disparity in the performance characteristics of new projects. In order to eliminate the need to predetermine the firm or non-firm status of a QF resource (i.e., wind, hydro, biomass), and instead, to provide an opportunity for QF resources to receive the firm published avoided cost rate based upon the QF actual performance, Idaho Power has included provisions for "base energy," "shortfall energy" and "surplus energy." The provisions require QFs using various generating technologies to actually perform on a firm basis to receive the posted firm rates. For non-firm energy delivered under the Agreement, and for firm energy not delivered, the provisions help ensure that Idaho Power pays no more than if it purchased equivalent energy from the market. Staff believes that it is reasonable in this case to approve the contract provisions regarding project standards of firmness, however, Staff notes that these are not provisions that have been required by the Commission in the past and may be appropriate for further evaluation in the future. Staff believes that the reasonableness of such provisions should not be determined in the context of a negotiated and mutually accepted contract.

Seasonality

As an incentive for a QF to deliver energy to the Company during times when it is of greater value to the Company, posted avoided cost rates have historically been "seasonalized." Generation in high demand months is paid at a rate of 120% of the avoided cost rate, generation in shoulder months at 100% and generation in low demand months at 73.5% of the avoided cost rate. The rates in the submitted Agreement are seasonalized. The weighting factors used for seasonalization remain the same as in prior QF contracts, but the months in which each factor applies have been re-arranged by the Company to better align the seasons with the months in which Idaho Power states it has identified actual energy needs. The months included in each season are the same as in the Company's most recent QF contract (Tiber Montana contract, *see* IPC-E-03-1, ON 29232). The seasons and their associated weighted factors are as follows:

Season	Weighting Factor	Months
1.	0.735	March-May
2.	1.20	June, July, November, December
3.	1.00	January, February, August, September, October

Staff believes that the seasons identified in the Agreement are reasonable. Staff recognizes that other months for future contracts may be demonstrated to be more appropriate.

Staff recommends that the United Materials Agreement be approved and that the non-standard terms unique to the contract (i.e., encouraging and increased firmness, and seasonality) not be viewed as precedential. Staff believes that because both parties find the terms of the Agreement acceptable and because the proposed rates and terms do not violate prior Commission Orders, that the Commission should not stand in the way of the Agreement.

Commission Decision

Does the Commission find it reasonable to approve the 9 MW wind power PURPA contract between Idaho Power Company and United Materials of Great Falls, Inc.? Does the Commission wish to include in its approval a caveat regarding the non-standard terms dealing with firmness and seasonality?

Scott Woodbury

Vld/M:IPCE0401_sw