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Attorney for the Commission Staff

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF)
IDAHO POWER COMPANY FOR AN ORDER) CASE NO. IPC-E-05-20
AUTHORIZING THE BLANKET SALE OF AIR)
EMISSION ALLOWANCES AND FOR AN)
ACCOUNTING ORDER.) COMMENTS OF THE
) COMMISSION STAFF
)

COMES NOW the Staff of the Idaho Public Utilities Commission, by and through its Attorney of record, Kira Dale Pfisterer, Deputy Attorney General, and submits the following comments in response to Order No. 29821.

BACKGROUND

On June 9, 2005, Idaho Power Company (Idaho Power) filed an Application with the Commission seeking (1) blanket authority to sell surplus sulfur dioxide (SO2) allowances obtained through provisions of the federal Clean Air Act (CAA) amendments of 1990, Title IV, and (2) an Accounting Order to record the proceeds from any such future sale. Each SO2 allowance represents permission from the Environmental Protection Agency (EPA) to emit one ton of SO2. Title IV aims to reduce SO2 emissions nationwide by putting a cap on electric utility emission levels and creating a system of SO2 allowances that can be traded or sold on the open market.

SO2 allowance trading is a regulatory approach to pollution control that emphasizes the use of market forces rather than forced technological compliance to reduce emissions. Under the CAA, if Idaho Power holds more SO2 allowances than it needs to cover its annual emissions, then it may trade or sell these allowances on the open market.

THE APPLICATION

Thermal plant owners like Idaho Power are issued allowances for the plant's sulfur dioxide emissions under Title IV of the Clean Air Act Amendments of 1990. Idaho Power has an ownership interest in five thermal power plants in the western United States. Three of these power plants are coal-fired and receive allocations of SO2 allowances from the EPA. These plants include: Jim Bridger Units 1 through 4 (1/3 interest); North Valmy Units 1 and 2 (1/2 interest); and Boardman (1/10 interest). The other two thermal power plants, Danskin and Bennett Mountain, are gas-fired but receive no allocation of SO2 allowances as they were constructed after Congress enacted the 1990 amendments to the CAA (Title IV).

Idaho Power believes that after retaining sufficient allowances to cover the emissions at these facilities and a reasonable cushion for unexpected changes and contingencies, it can make surplus SO2 allowances available for sale or trade. To avoid any potential "regulatory cloud" over the marketability of these surplus SO2 allowances, Idaho Power seeks blanket authority to sell SO2 allowances.

Idaho Power believes that the sale of such SO2 allowances does not fall under the provisions of *Idaho Code* § 61-328, which prohibits an electric utility from selling or exchanging property used in the generation, transmission, distribution or supply of electric power "except when authorized to do so by order of the public utilities commission." Idaho Power submits that *Idaho Code* § 61-328 does not apply because SO2 allowances are not property pursuant to the express provisions of the CAA, 42 U.S.C. § 7651b(f). Further, Idaho Power argues that the SO2 allowances are not used in the performance of Idaho Power's utility service obligations.

Idaho Power also requests an Accounting Order to provide for the recording of any proceeds received from future sales of surplus SO2 emission allowances. At this time, Idaho Power does not seek a Commission decision regarding how such revenue will be treated for ratemaking purposes.

Idaho Power recognizes that the Commission has jurisdiction over Idaho's allocable share of proceeds from the sale of surplus SO₂ allowances and acknowledges that receipt of blanket authority to sell SO₂ allowances and the Commission's initial accounting Order are not a determination of the appropriate ratemaking treatment for revenue requirement purposes. Idaho Power recommends that the determination of ratemaking treatment for SO₂ allowance proceeds be made at a later date.

STAFF ANALYSIS

A. SO₂ Emissions Trading Under the Clean Air Act

Allowance trading is the centerpiece of the EPA's Acid Rain Program. The purpose of this program is to allow utilities to adopt the most cost-effective strategies to manage available resources to comply with the acid rain requirements of the Clean Air Act.

An SO₂ allowance authorizes a utility generating unit to emit one ton of SO₂ during a given year or any year thereafter if the SO₂ allowance is not used in the year in which it is issued. At the end of each year, the utility generating unit must hold allowances at least equal to its annual SO₂ emissions as measured by its Continuous Emissions Monitoring System (CEMS) and reported to the EPA. If a utility holds a sufficient quantity of allowances over its annual requirement, then it is considered to have surplus SO₂ allowances.¹

Pursuant to the Clean Air Act, and underlying regulations, SO₂ allowances are fully marketable commodities. Utilities may sell or trade SO₂ allowances to other utilities or interested parties on the open market or through EPA-sponsored auctions held annually.

SO₂ allowances are allocated in two phases. Phase I allowances are allocated for each year beginning in 1995. The EPA allocated allowances at an emission rate of 2.05 pounds of SO₂/mmBtu (million British thermal units) of heat input, multiplied by the unit's baseline mmBtu output (the average fossil fuel consumed from 1985 through 1987). Additional allowance allocations were made based upon a pro rata share.

In Phase II, which began in the year 2000, the EPA expanded the group of affected sources to include virtually all units over 25 MW in generating capacity and tightened the allowance allocation. All of Idaho Power's SO₂ allowances fall under the provisions of

¹ Regardless of how many allowances a unit holds, it is never entitled to exceed the emissions limits set under Title 1 of the Clean Air Act to protect public health.

Phase II. These allowance allocation calculations were based upon coal- and gas-fired units with low and high emissions rates. The EPA allocated allowances to each unit at an emission rate of 1.2 pounds of SO₂/mmBtu of heat input, multiplied by the unit's baseline mmBtu output. In Phase II, the Clean Air Act places a cap of 8.95 million on the number of allowances issued to units each year. This effectively caps emissions at 8.95 million tons annually and ensures that mandated emissions reductions be maintained over time.

EPA records all trading and transfers of allowances that are used for compliance and ensures at the end of the year that a unit's emissions do not exceed the number of allowances it holds. To accomplish this task the EPA maintains an Allowance Tracking System (ATS). Each affected utility unit, corporation, group, or individual holding allowances has an account on the ATS. ATS accounts track issuance of allowances, how many allowances an account holds, allowance reserves, allowance deductions for compliance, and transfers of allowances between accounts.

Prices for SO₂ allowances are set on a system of supply and demand. These allowances are traded and sold just like commodity futures on the Chicago Board of Trade. The Air Daily Index tracks prices and volumes of SO₂ allowances available on the market. In addition, SO₂ allowances are also sold and traded through EPA sponsored auctions held once a year.²

Allowances provided for auction purposes extend from the EPA, which sets aside special allowance reserves of approximately 2.8 percent of the total annual allowances allocated to all units. These allowances are offered in the (1) Spot Auction (allowances dated for the year in which they are offered or previous years) or (2) Advance Auction (allowances 7 years in the future). For 2005, the spot auction and the advance auction were held in March with a total of 250,000 emission allowances for bid. Out of the 250,000 total allowances, 125,000 were sold on the spot auction for a weighted average price of \$702.51 per allowance, and 125,000 were sold on the advance auction for a weighted average price of \$297.49 per allowance. The gross proceeds of the 2005 emissions allowance auctions amounted to \$124,999,175.

² These auctions are sponsored by the EPA to ensure the availability of allowances, thus ensuring both the economic efficiency of the emissions limitation program and the addition of new electric-generating capacity. Auctions help ensure that new units have a public source of allowances beyond those allocated initially to existing units.

B. Authority to Sell SO2 Allowances

Pursuant to *Idaho Code* § 61-328, an electric utility, such as Idaho Power, may not sell or transfer any property located in the State of Idaho that it owns, controls, or operates and which is “used in the generation, transmission, distribution, or supply of electric power and energy” without Commission approval. *Idaho Code* § 61-328(1). Further, prior to approving each transaction, the Commission must find that: (1) the transaction is consistent with the public interest; (2) the cost of and rates for supplying service will not be increased due to the transaction; and (3) the applicant for such acquisition or transfer must have the bona fide intent and financial ability to operate and maintain the property in the public service.” § 61-328(3).

While SO2 allowances are necessary in order for Idaho Power to generate electricity from its thermal generating plants, the SO2 allowances are not directly used in the “generation, transmission, distribution, or supply of electric power and energy” and cannot be “operated and maintained in the public service.” *Idaho Code* §§ 61-328(1), (3). Therefore, this statutory provision does not apply to the sale of SO2 allowances.

Because *Idaho Code* § 61-328 does not apply to the sale of SO2 allowances, it is entirely appropriate for the Commission to issue an Order providing blanket authority to enter such transactions. Nonetheless, following each sale, the Commission shall retain the authority to evaluate the reasonableness of the transaction and appropriate treatment of the revenue for ratemaking purposes.

C. Accounting Treatment

In the Application, Idaho Power submits an initial proposed accounting pursuant to Code of Federal Regulations No. 18, in accordance with paragraph H of General Instructions 21. This regulation states that if there is uncertainty regarding the regulatory treatment, the gain should be deferred in Account 254, Other Regulatory Liabilities, pending resolution of uncertainty.

The following is Idaho Power’s proposed accounting to record the proceeds from the sale of surplus SO2 emission allowances net of income taxes for the initial transactions:

131 – Cash	\$XXX.XX
236 – Taxes Accrued	\$XXX.XX
254 – Other Regulatory Liabilities	\$XXX.XX

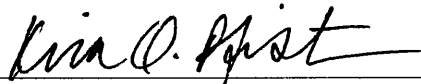
Idaho Power requested that the determination of ratemaking treatment for the proceeds be made at a later date. In determining the accounting treatment for SO2 allowances, Idaho Power stated that it would file a report with the Commission within sixty (60) days after receipt of any proceeds from the sale of SO2 emissions allowances, assuming blanket authority will be given. According to Idaho Power, this report would initiate the Commission's consideration of appropriate ratemaking treatment.

STAFF RECOMMENDATION

Staff supports Idaho Power's Application both for an Order providing blanket authority to sell excess SO2 allowances and for an Accounting Order. In addition, Staff would like the Commission to explicitly retain the regulatory authority to determine whether each sale or transaction was reasonable and in the public interest.

Staff recommends that a workshop setting be utilized to determine the appropriate treatment of all revenues obtained through the future sale of SO2 allowances. These workshops should involve Idaho Power, Staff and other interested parties. Staff further recommends that these workshops be conducted expeditiously to assure determination of ratemaking treatment in a timely fashion. It is Staff's position that customers are entitled to receive the benefits associated with the sale or trade of any SO2 allowances. Staff believes a workshop setting with the intent of reaching a settlement is an appropriate process to resolve any issues dealing with future accounting and ratemaking treatment. Any proposed resolution of remaining issues and/or negotiated settlement will be filed with the Commission.

Respectfully submitted this *2nd* day of August 2005.



Kira Dale Pfister
Deputy Attorney General

Technical Staff: Eric Johnson

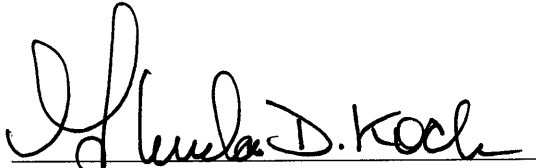
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 2ND DAY OF AUGUST 2005, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF**, IN CASE NO. IPC-E-05-20, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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