

DECISION MEMORANDUM

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

FROM: SCOTT WOODBURY

DATE: SEPTEMBER 26, 2005

**SUBJECT: CASE NO. IPC-E-05-24 (Idaho Power)
FIRM ENERGY SALES AGREEMENT – ARROW ROCK WIND, INC.**

On July 28, 2005, 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 and Arrow Rock Wind, Inc. (Arrow Rock) dated July 28, 2005. Under the Agreement, Arrow Rock will sell and Idaho Power will purchase electric energy generated by the Arrow Rock Wind Generating Project, located near Billings, Montana, in an area more particularly described as located approximately 100 miles northwest of Billings, Montana in Wheatland County on the west side of Highway 191 in the NW 1/4 of Section 36, Township 10 N, Range 15 E. The nameplate rating of the wind facility is 19.5 MW. Under normal and/or average conditions, the project will not exceed 10 aMW on a monthly basis.

As represented, Arrow Rock will be a qualified small power production facility (QF) under the applicable provisions of the Public Utility Regulatory Policies Act of 1978 (PURPA). Idaho Power contends that the Agreement comports with the terms and conditions of Commission Order No. 29632 (*U.S. Geothermal et al v. Idaho Power*) and avoided cost Order No. 29646. The Agreement is for a 20-year term and contains the published non-levelized avoided cost rates set forth in Order No. 29646. Arrow Rock has selected December 1, 2005 as the scheduled Operation Date for this facility.

Arrow Rock has made arrangements with NorthWestern Energy to deliver the net energy from its Montana facility to the Idaho Power electrical system. The transmission arrangement with NorthWestern Energy means that the Company will receive firm energy from the facility rather than

the intermittent energy generally associated with a wind-generating project. Energy deliveries from the Arrow Rock project are for nine months out of the year and exclude deliveries during the spring months of March, April and May when the value of energy on the Company's system is the lowest.

Idaho Power acknowledges the Company's Petition in Case No. IPC-E-05-22 and represents that Arrow Rock was in the final stages of negotiations with Idaho Power immediately prior to the Petition filing and that prior to that date Arrow Rock had submitted an executed Agreement to the Company. It is Idaho Power's contention that Arrow Rock is appropriate for exempting from the temporary suspension requested by the Company in Case No. IPC-E-05-22.

Section 22 of the Agreement provides that the Agreement will not become effective until the Commission has approved all the Agreement's terms and conditions and declared that all payments that Idaho Power makes to Arrow Rock for purchases of energy will be allowed as prudently incurred expenses for ratemaking purposes.

On August 19, 2004, the Commission issued Notices of Application and Modified Procedure in Case No. IPC-E-05-24. The deadline for filing written comments or protests was September 9, 2005. The Commission Staff was the only party to file comments. Staff recommends that the Commission approve the Agreement.

Staff Comments

Staff sees nothing within the Arrow Rock Agreement that either violates PURPA or that is not in compliance with prior Commission Orders. Staff believes that the Arrow Rock project is unaffected by Commission Order No. 29839 concerning intermittent wind QF published rate eligibility. Under that Order, wind projects that are firm, as the Arrow Rock project is, are not subject to the change in published rate eligibility and grandfathering criteria.

Staff identifies aspects of the Arrow Rock project that cause concern, such as the disparity between Idaho Power's published avoided cost rates paid for 10 aMW of Arrow Rock output and the price that is paid for the remaining Judith Gap output, ownership status, and the disaggregation of large projects into 10 aMW pieces. Staff believes that those issues, however, can be best addressed and remedied in the context of Case No. IPC-E-05-22.

Staff in its comments expresses concern regarding the ownership, control, operation and maintenance of the Arrow Rock generation facility and notes that there are no Commission rules requiring or specifying ownership or lease arrangements.

Staff notes that Arrow Rock will comprise 13 wind turbines of a total 90 turbines that constitute a larger project termed the Judith Gap Project. The Judith Gap Project was the successful bidder in a recent Request for Proposals (RFP) issued by NorthWestern Energy. Under the Agreement between Judith Gap and Northwestern, NorthWestern will purchase 135-150 MW of generation from Judith Gap at a price of \$31.71 per MWh and will bear whatever costs must be incurred to integrate the Project's generation into its system. The generation produced by Arrow Rock, Staff contends, will be delivered to NorthWestern, who in turn will "firm" the energy and deliver a flat 10 MW product to Idaho Power. One view of the Agreement under consideration, Staff contends, could be that 13 turbines have been "carved off" from the Judith Gap Project so that 10 aMW of project output could be sold to Idaho Power at a higher price than what otherwise have been received. This arrangement, Staff believes, illustrates some of the problems of wind projects still being debated in Case No. IPC-E-05-22. However, even with the apparent price differential, Staff notes that the Agreement represents a better deal to Idaho Power and its ratepayers than other PURPA contracts. The rate being paid by Idaho Power is the same as the rate paid under any other PURPA contract, but Idaho Power is receiving a completely firmed, thus a more valuable product in return. Moreover, unlike other contracts, Idaho Power is not required to accept output from the project during March, April and May when it is not normally seeking to acquire power. When viewed from this perspective, Staff contends that the Agreement appears to be a good deal for Idaho Power and its ratepayers.

Arrow Rock Comments

On September 23, 2005, Arrow Rock submitted Reply Comments. The purpose of Arrow Rock's reply comments are to clarify the record and correct some factual errors in Staff's comments related to the development, cost and structure of the Arrow Rock project. Arrow Rock contends that the Judith Gap Power Purchase Agreement price is far from representative of the cost to develop a wind project today. In fact, Arrow Rock contends that the cost to develop a wind project today is in \$50 to \$60 range, as can be identified by the procurement of the Wolverine Project in Idaho by PacifiCorp and the wind resource bids in Idaho Power's latest RFP. To further explain the increasing costs of wind resources, Arrow Rock provides an article from Wind Energy Weekly identifying production costs and demand related factors that have contributed to an 18% (approximate) increase in wind generation equipment over the last year.

Arrow Rock contends that the site adjacent to the Judith Gap site was chosen because of (1) the benefit of the wind resource; (2) the mobilization cost of construction; and (3) the deliberate and beneficial studies with the USF&W in the area on avian (bird) impact. The Montana site area demonstrates a wind resource capacity factor of approximately 35 to 37 percent compared with 28 to 30 percent in Idaho and Oregon. The increase in wind energy production assists in lowering the fixed costs of the project. However, Arrow Rock contends that this benefit is substantially offset by transmission costs to deliver the energy from Montana to Idaho. The Arrow Rock Agreement with Idaho Power also incurs an additional cost of integrating, firming and shaping the wind energy into a fixed-rate schedule to Idaho Power. This structure is a value added component of the Arrow Rock resource and Arrow Rock must compensate the integration agent, NorthWestern, for such services.

Arrow Rock further clarifies that it is not intending to sell any electrical energy to NorthWestern Energy in March, April and May. The energy produced from the Arrow Rock project during those months will be integrated and stored by NorthWestern for later delivery to Idaho Power. The integration service contemplated with NorthWestern is intended to be an energy-neutral service at market-based rates.

Arrow Rock notes also that it is not providing a 10 MW flat product to Idaho Power. Pursuant to Agreement the base load firm energy deliveries to Idaho Power will be 7 MW in the months of June, July and August and 9 MW in the months of September through February.

COMMISSION DECISION

Idaho Power has submitted for Commission consideration and approval a Firm Energy Sales Agreement with Arrow Rock Wind, Inc. dated July 28, 2005. The energy product delivered is a firm product exempt from the change in published rate eligibility in recent Order No. 29839. The Agreement is for a 20-year term and contains the published non-levelized avoided cost rates set forth in Order No. 29646. Does the Commission find it reasonable to approve the Agreement and authorize payments made under the Agreement as prudently incurred expenses for ratemaking purposes?

Scott D. Woodbury