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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

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| IN THE MATTER OF THE APPLICATION OF IDAHO POWER COMPANY FOR AUTHORITY TO INCLUDE IN ITS POWER COST ADJUST­MENT COMPUTATIONS THE FIRM POWER PURCHASE FROM ARIZONA PUBLIC SERVICE. | )  )  )  )  )  )  ) | CASE NO. IPC-E-96-18  COMMENTS OF THE  COMMISSION STAFF |

On August 28,1996, Idaho Power Company (IPC) filed an application with the Idaho Public Utilities Commission (IPUC, Commission) requesting that it be allowed to include the cost of a firm power purchase from Arizona Public Service Company (APS) in its Power Cost Adjustment (PCA) mechanism.  The purchase contract is for 100 MW at a 100 % load factor during each of the months September through March.  The contract is to run for a five year period from September 1996 through March 2001.  The capacity rate remains constant over the five year period at $1.50 per kW-Mo. which, at a 100% load factor, is approximately 2 mills per kWh.  Energy rates increase gradually over the life of the contract starting at 18.69 mills per kWh and ending at 21.75 mills per kWh.  According to its application the Company entered into this agreement to satisfy firm energy and capacity needs identified in its June 1995 Integrated Resource Plan (IRP) which is on file with the Commission.

ANALYSIS

The Company’s 1995 Integrated Resource Plan, Figures 4 and 5, shows energy and/or capacity shortfalls in December and January of most of the five years included in the contract.  Those shortfalls do not exceed 100 MW during the life of the contract.  The APS purchase covers demonstrated need and allows the Company to meet or exceed a minimum reliability standard.  Meeting or exceeding a minimum reliability standard has substantial benefits to Idaho ratepayers. The previously referenced IRP figures are attached to these comments as Attachments A and B, respectively.

Commission Order No. 24806 from Case No. IPC-E-92-25 established Idaho Power’s PCA.  In that Order the Commission commented on including capacity purchases.  The Commission said:

We agree with FEA (Federal Executive Agencies) that any PCA that includes purchased power costs may motivate the Company to enter into long-term capacity purchases rather than invest in its own generation plant because the former would not require the Company to accept any risk and would bypass the least cost planning and prudency review process currently in place.

Although Idaho Power currently does not have any non-CSPP capacity contracts, we find that it is appropriate to exclude any future non-CSPP firm purchases from the PCA unless the Company has first obtained Commission approval to include them.

Commission Order No. 24806 at Page 23.

With regard to resource acquisition, the Company has been on record for several years saying that it does not intend to construct new resources but that it intends to purchase resources as the need arises.  In its most recent IRP the Company identified contract purchases as the method of meeting near-term capacity and energy shortfalls.  Staff believes that the IRP process  addresses the expressed Commission concerns about the choice of resource and the least cost review.  A full prudency review only takes place in a general rate case where all aspects of the Company’s business are reviewed.  In accordance with the rate stability commitment that Idaho Power has entered into it can not file a general rate case with rates to be effective prior to January 1, 2000.  In the interim, if PCA treatment of contract costs is allowed, the full risk of potentially poor purchase prices is not transferred to ratepayers.  The PCA shares costs and benefits on a 90 - 10 basis between ratepayers and shareholders.

In its application Idaho Power states:

At the time the Company decided to enter into the purchase from APS, market prices for capacity ranged from 3 - 6 mills and the historical spot-market price for non-firm energy was approximately 21 mills.  These prices were consistent with the Company’s market research at the time, which indicated that the long term price for five year base load contracts, delivered in this region, was in the 23 to 28 mill range.  The rate of 22.1 mills the Company was able to negotiate with APS, for both capacity and energy, fell within those parameters.  APS power would be available to cover the winter deficits forecasted by the IRP and could be marketed off-system when not needed to meet loads or maintain system reliability.  In addition, the relatively short five-year term provides desirable flexibility by not locking the Company into a long-term commitment during a time of uncertainty concerning supply requirements.

Application at pp.  2-3

Upon Staff request the Company provided the market research information that was available at the time prices were negotiated.  Based on this information the prices established in the contract were reasonable at the time the letter agreement was executed.  It is Staff’s understanding, however, that the price of energy and capacity has continued to fall since those negotiations.  Lower prices today indicate that at least the initial prices under the contract are too high.

As part of the review of this application Staff examined the feasibility of excluding this contract from PCA treatment.  A major concern is that from the day Idaho Power first began to receive power under this contract there have been associated changes in the three major accounts that make up the PCA.  First, addition of the new 100 MW resource in the Company’s resource pool immediately reduces the need to purchase on the non-firm market.  Second, it increases the Company’s ability to make non-firm sales.  Finally, it reduces the Company’s fuel costs.  Also, if all or part of the purchase goes to meet firm load growth, actual power supply costs captured within the PCA are reduced by 16.84 mills/kWh.  A combination of all of these things occur as the direct result of adding this resource to the Company’s resource pool whether or not PCA treatment of the contract cost is allowed.  Without including the contract cost, all of the aforementioned PCA effects benefit ratepayers.  It would be unfair to the Company, therefore, to allow these ratepayer benefits to accrue within the PCA without allowing the Company recovery of the reasonable costs that make the benefits possible.  It would be next to impossible to identify the PCA benefits and remove them.

On the other hand, if the Company is allowed to include the full cost of the power purchase in the PCA, the net effect will be an increase in customer rates.  Contract costs will exceed PCA benefits. The benefits of reduced non-firm purchases and increased non-firm sales in terms of mills/kWh average in the mid to upper teens.  The benefits of reduced fuel costs and increased firm load are expected to average 16.84 mills/kWh.  Contract costs, including both energy and capacity, start at 20.75 mills/kWh and increase to 23.81 mills/kWh over the life of the contract.  Since, under current market conditions, lower priced capacity and energy are likely to be available,  it seems unfair to ratepayers to allow full contract costs in the PCA.

Idaho Power Company and Arizona Public Service Company do not have a signed final contract for this purchase.  They have a letter agreement that both parties have signed that contains the essential elements of the unexecuted final contract.  A copy of the letter agreement is attached as Attachment C.  The unexecuted agreement is included in the Company’s filing and has been filed with FERC.  APS has signed the final contract; Idaho Power has not.  The two Companies are currently engaged in a dispute before FERC concerning non-firm transmission rights associated with FERC Order 888 that relate to this contract.  This dispute in no way affects the firm transmission rights that assure deliverability of the 100 MW to the Borah or Brady substations identified in the Company’s filing.

The letter agreement was executed July 12, 1995.  Thus, it has been over 15 months since the agreement was executed.  Since that time market prices for power have fallen significantly.  It is Staff’s opinion, therefore, that the acquisition of power from APS under the rates set forth in the contract would not be prudent from the perspective of Idaho Power’s ratepayers.

RECOMMENDATION

Staff believes APS contract power costs negotiated in mid 1995 and presented to the Commission for PCA treatment approval more than a year later to be stale and unacceptable.  In these comments Staff has identified PCA benefits and reliability benefits associated with Idaho Power’s APS purchase.  Staff’s position is not that the purchase is unnecessary, but that it is unreasonably priced in today’s market.  Staff has examined several options in an attempt to determine a reasonable price that it could support for PCA purposes.  Staff examined the possibility of tying contract rates to a market index but with limited access to this kind of information found no suitable index.  Finally, Staff considered allowing PCA costs of the APS contract to be included in the PCA at 16.84 mills/kWh.  If 16.84 mills/kWh is used as the cost of contract power, the costs and benefits reflected in the PCA of this sale should be approximately equal.  If the entire 100 MW is required to serve firm load growth, the Company receives the revenue from those firm sales and other customers are held harmless because the PCA load growth adjustment backs out the power cost at 16.84 mills/kWh.  If contract costs allowable for PCA purposes are set at 16.84 mills/kWh and the Company had to sell all of the APS contract power on the non-firm market, non-firm revenues, averaging somewhere in the mid-teens, would approximately offset contract costs and once again not impact other customers rates.  Therefore, it is Staff’s recommendation that the costs of the APS contract be allowed in the PCA at 16.84 mills/kWh.

DATED  at Boise, Idaho, this            day of October 1996.

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Brad Purdy

Deputy Attorney General

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