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BEFORE  THE  IDAHO  PUBLIC  UTILITIES  COMMISSION

IN THE MATTER OF THE APPLICATION OF )

IDAHO POWER COMPANY REGARDING)CASE  NO.  IPC-E-98-10

ITS PROPOSED CANCELLATION OF FIRM)

ENERGY SALES AGREEMENTS.)

)COMMENTS OF THE

)COMMISSION STAFF

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COMES  NOW  the Staff of the Idaho Public Utilities Commission, by and through its Attorney of record, Scott Woodbury, Deputy Attorney General, and in response to the Notice of Application, Notice of Modified Procedure and Notice of Comment/Protest Deadline issued on October 9, submits the following comments.

On July 1, 1998, Idaho Power Company (Idaho Power; Company; IPCo) filed an Application with the Commission in Case No. IPC-E-98-10 requesting Commission approval of the Company’s proposed cancellation of two Firm Energy Sales Agreements (Sales Agreements) between Lynn E. Stevenson and Arrowhead Trust (hereinafter collectively referred to as “Stevenson”) and Idaho Power.  Reference Agreement to Cancel dated June 10, 1998.

In 1984, Lynn E. Stevenson and Idaho Power entered into two Firm Energy Sales Agreements for the purchase of electrical capacity and energy to be generated by two under-one-megawatt PURPA qualified small hydroelectric production facilities (QFs) in Gooding County, Idaho known as Stevenson Site No. 1 and Stevenson Site No. 2.  The contracts were for a term of 35 years.  Site No. 1 has a capacity of 75 kW, a projected contract annual net energy amount of 286,000 kWh, and a projected annual revenue stream of approximately $16,590.  Site No. 2 has a capacity of 65 kW, a projected contract net annual energy amount of 194,000 kWh, and a projected annual revenue stream of approximately $11,212.

As reflected in Idaho Power’s Application, the Stevenson QFs failed to generate electricity during most of 1992.  In July of 1993, a landslide occurred in the Snake River Canyon and the projects were inundated with water.  As reported, it is not known when, if ever, the Stevenson QF projects, as currently configured, will be capable of resuming operation.

In 1996 Idaho Power served Stevenson with notice of default under the contracts.  Specifically, Idaho Power contended that Stevenson failed to maintain Valued Loss of Income Insurance and the required amount of Liability Insurance, and that Stevenson was delinquent in payment for O&M services provided by Idaho Power.  The defaults alleged by Idaho Power were for lack of performance during the period after the landslide.  Stevenson has disputed the occurrence of any defaults and has responded that if any defaults have occurred, they are excused by the force majeure provision of the underlying Sales Agreements.

Idaho Power and Stevenson, to avoid litigation of the issue of defaults and disputed claims, have agreed to cancel the Sales Agreements.  On June 10, 1998, the parties entered into an Agreement to Cancel the Firm Energy Sales Agreements agreeing and acknowledging that cancellation is “a full and complete release and settlement of all of the claims for injury or damage, or underpayment or overpayment which any party may sustain as a result of the other party’s performance” of the Sales Agreements and the cancellation of same.  Idaho Power reserves the right to remove (at its expense) all interconnect facilities and Stevenson waives any claim for salvage value.  The effectiveness of the Cancellation Agreement is contingent on Commission approval.  The Cancellation Agreement recites an effective date of May 1, 1996.

Should Stevenson decide to rebuild the projects in the future, new sales agreements at the rates in effect at the time would be required.

STAFF ANALYSIS

Staff believes that the key issue in this case was Stevenson’s failure to perform according to the Sales Agreement prior to the occurrence of the landslide in 1993, and Idaho Power’s failure to enforce insurance provisions of the Agreement at that time.  Had both parties strictly abided by the terms of the Sales Agreement, there likely would be no dispute between the parties necessitating the Cancellation Agreement for which the parties now are seeking Commission approval.

Staff believes that the apparent dispute between the parties over default and force majeure subsequent to the landslide is a relevant issue, but only to the extent it gives reason for the Cancellation Agreement as a settlement of the disputes.  While it is admittedly a contractual legal issue for the courts, Staff contends that the first default under the Sales Agreements happened before the landslide occurred when Stevenson failed to maintain required insurance coverages.  The overpayment liability existed at the time of the first default, thus Staff believes force majeure occurring subsequent to the default cannot excuse the overpayment liability.  Based on information submitted by Idaho Power in response to Staff Production Requests, Idaho Power’s allegations of default appear to be for lack of performance in the 1995-1996 period, not during the period prior to the 1993 landslide.

The Sales Agreements contain a provision requiring Stevenson to maintain Valued Loss of Income Insurance.  The primary purpose of this provision is to insure that funds will be available to Stevenson to pay any debts owed to Idaho Power in the event the Sales Agreement is prematurely terminated.

Under the Sales Agreements, Stevenson was to be paid levelized rates.  This means that the same rate would be paid for energy from the projects for the entire duration of the 35-year contracts.  Non-levelized rates, by contrast, start out low and gradually escalate over the life of the contract, mirroring the actual value of the energy.  In effect, by paying levelized rates, Idaho Power pays more than the true value of the energy in the early years of the contract and less than the true value in later years.  This creates an overpayment liability on the part of Stevenson should the contract not go to its full term.  To protect both parties (e.g., Stevenson from not having funds to pay the overpayment liability, and Idaho Power by insuring there will be sufficient funds available to collect), the contracts require that Valued Loss of Income Insurance be maintained in an amount equal to the overpayment liability.

Stevenson failed to maintain Valued Loss of Income Insurance.  Records provided by Idaho Power in response to Staff Production Requests show that Stevenson frequently allowed his insurance coverages to lapse during periods when premiums went unpaid.  Staff believes that the failure to maintain insurance was not due to the insurance being unavailable, but rather due to failure to promptly pay the premiums.  While the primary responsibility for maintaining required insurance rests with Stevenson, Idaho Power provided no written documentation during the period noting Stevenson’s failure to maintain insurance, or warning Stevenson of contract default.

Despite Stevenson being primarily responsible for maintaining insurance, Staff believes Idaho Power also should shoulder some responsibility for seeing that project owners maintain adequate insurance coverage in order to protect ratepayers.  Without Valued Loss of Income Insurance, many project owners have little means, other than the revenue from their projects, of meeting possible liability.  When the project itself is destroyed or made inoperable, there is no means of meeting liability.

Idaho Power has pointed out in the past that Valued Loss of Income Insurance has become difficult, if not impossible, to obtain.  In fact, partly as a result of this difficulty, security requirements for QF projects were changed at Idaho Power’s request in Case No. IPC-E-93-22.  Revised security requirements are contained in Order No. 25240 issued on November 2, 1993. Idaho Power filed its application in that case on September 13, 1993.  (Note that Idaho Power’s application to revise required insurance coverages was made after the July 1993 landslide occurred).

Given that both parties, as Staff contends, failed to adequately protect themselves in the event of a catastrophic event as has occurred here, Staff believes the Commission’s only alternative is to attempt to protect ratepayers from shouldering the loss.  Staff contends, and

Idaho Power concurs, that Stevenson was not excused from the overpayment liability as a result of force majeure.  Stevenson disagrees.

Idaho Power has calculated the amount of the overpayment liability as $90,908 for Site No. 1 and $60,699 for Site No. 2, or a total of $151,607.  In addition, Idaho Power contends Stevenson owes $3,066 for unpaid operation and maintenance of interconnection facilities.  The total amount owed Idaho Power is $154,674.  Staff agrees with these figures.

Because the dispute between the parties is a contractual matter, Idaho Power would have to seek relief through District Court.  The time and expense required to pursue the matter, combined with Idaho Power’s belief that collection of any judgement rendered would be unlikely, have led Idaho Power to seek settlement through the Cancellation Agreement.

Idaho Power has suggested that the Cancellation Agreement be viewed similar to a contract buy out.  In exchange for forfeiting any claim to overpayment liability and unpaid O&M charges, Idaho Power would be relieved of any future obligations under the existing contract to purchase energy in the event the projects are rebuilt.  The existing contracts include levelized rates of 57.79 mills/kWh.(footnote: 1)  Today’s avoided cost rates for small projects like Stevenson’s are 31.06 mills/kWh.  Given the difference in rates today, and Idaho Power’s forecast of what those rates may be in the future, Idaho Power calculates that it could save $383,911 over the remaining life of the contract by acquiring an equivalent amount of energy from some source other than the Stevenson projects.  The present worth of these savings is $116,553 (computed at 9.199%, IPCo’s overall rate of return as determined in their last rate case).

Staff considers the contract buy out analogy to be somewhat deceptive.  Staff questions whether Stevenson has ever seriously intended to rebuild the projects and continue to generate under the existing contracts.  For a period of more than four years, Stevenson has made no apparent attempt to remedy the force majeure.  Furthermore, it is significant that neither project was generating for most of the year before the landslide occurred.  Staff contends that Idaho Power exercising proper oversight should have been able to terminate both contracts at no cost to Idaho Power and its ratepayers, whether the landslide had occurred or not.  Ratepayers would have benefitted from termination of the contracts, and Idaho Power should have been able to collect the overpayment liability owed.

Absent specific orders from the Commission, ratepayers absorb the loss associated with unrecovery of any overpayment liability.  Since no generation is occurring however, ratepayers are benefitting because payment is not being made to Stevenson under the contracts and the reduction in power supply cost is reflected in the Power Cost Adjustment (PCA).  Going forward, ratepayers will continue to realize the same benefits through the PCA

if cancellation of the contracts is approved.  Although the over-payment liability will be forfeited, cancellation of the uneconomic contracts will continue to be reflected in the PCA to the benefit of IPC customers.

STAFF RECOMMENDATIONS

Staff believes Stevenson owes Idaho Power $154,674 whether the Sales Agreements are canceled or not.  However, Staff also agrees with Idaho Power that the expense associated with pursuing the matter in court, and the small likelihood of being able to collect on any judgement, makes settlement a preferred alternative.  With one small but significant caveat, the settlement agreement negotiated by the parties is reasonable.

Staff recommends that as a result of the outstanding overpayment liability, approval of the Cancellation Agreement must be conditioned upon a requirement that Stevenson repay the overpayment liability from the salvage value of any generation equipment (if realized) and/or prior to the execution of any new contracts should Stevenson choose to sell his interest in the site(s) or to redevelop and sell the generation from either site.

DATED at Boise, Idaho, this            day of October 1998.

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Scott Woodbury

Deputy Attorney General

Technical Staff:Rick Sterling

Sydney Lansing

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**FOOTNOTES**

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The levelized average annual rate of 57.79 mills/kWh reflects the contract seasonal rates of 70.0 mills/kWh in seasons 1 and 3 and 46.7 mills/kWh in seasons 2 and 4.