

DECISION MEMORANDUM

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

FROM: SCOTT WOODBURY

DATE: JUNE 2, 2003

**RE: CASE NO. PAC-E-03-2 (PacifiCorp)
2003 ELECTRIC INTEGRATED RESOURCE PLAN (IRP)**

On January 27, 2003, PacifiCorp dba Utah Power & Light Company (PacifiCorp; Company) filed its 2003 Integrated Resource Plan (IRP) with the Idaho Public Utilities Commission (Commission). The Company's filing is pursuant to a biennial requirement established in Commission Order No. 22299, Case No. U-1500-165. PacifiCorp states that its IRP provides a framework and plan for the prudent future actions required to ensure PacifiCorp continues to provide reliable and least-cost electric service to its customers. The final IRP, it states, culminates a year-long collaboration with considerable public involvement from customer interest groups, regulatory staff, regulators and other stakeholders.

PacifiCorp serves approximately 1.5 million retail customers in service territories comprising about 135,000 square miles in portions of six western states: Utah, Oregon, Wyoming, Washington, Idaho and California. This service territory has diverse regional economies ranging from rural, agricultural and mining areas to urban, manufacturing and government service centers.

PacifiCorp forecasts average annual load on its system to grow by 2.2% in the east and 2.0% in the west. Given uncertainties of economic growth and other factors, this growth in PacifiCorp's load, the Company states, could vary by 1.4% and 3.4%. At the same time, PacifiCorp notes, the resources available to the Company to serve this demand will diminish over time as supply contracts expire, hydroelectric generation facilities are subjected to relicensing conditions and thermal plants comply with more stringent emissions requirements.

The Company's IRP was developed against the backdrop of continuing market, regulatory and structural changes in the electric industry. These changes, the Company states, highlight the importance of understanding the risks and uncertainties inherent in resource planning. The IRP reveals that PacifiCorp has substantial new resource needs and will require an additional 4,000 MW of new resources (DSM, generation, and supply contracts) through 2013. Load growth, load shape growth, asset retirement and contract expirations cause the gap between demand and supply to grow over time.

Other key findings in the IRP include:

- The strongest resource strategy relies on a diverse portfolio of options, including strong components of renewables and demand-side management, but also natural gas- and coal-fired generating resources. A resource procurement process to pursue this diversified approach is described in the Action Plan.
- Possible paradigm shifts in the electric industry driven by federal regulatory requirements are significant uncertainties for PacifiCorp and its customers to manage in the next several years. These issues include (potentially favorable) changes in transmission operations, as well as the potential increased cost associated with PacifiCorp's existing resource assets, including complying with air emission standards and relicensing hydro electric facilities.
- Renewable resources are a good fit for PacifiCorp within the context of a diversified portfolio. The IRP proposes procuring renewable resources (primarily wind, and possibly geothermal) at a level shown to be cost effective, given the assumptions used to evaluate the resource. The amount of renewables is also a level that would meet or exceed renewable portfolio standards that have been proposed in federal and state legislation.
- Demand-side management (DSM) will continue to be an important and cost-effective program for PacifiCorp. A significant increase in programmatic measures is proposed, including a load control program to help mitigate growing capacity requirements.
- In addition to renewable resources and DSM, the study concludes that additional resources from thermal generation will also be required. The least-cost option is a combination of three natural gas-fired units and one coal unit to meet both growing energy and capacity requirements.

- The least-cost portfolio includes a coal base-load thermal unit in the east. Coal-fired generation may be particularly advantageous when procuring resources in the Rocky Mountains, the Company states, because coal is an abundant indigenous resource there. However, the long-term impact of atmospheric emissions is casting doubt on the viability of coal-fired generation. The IRP least-cost portfolio is dependent upon the impact of a number of these paradigm risks, including air emission standards and possible global warming measures. PacifiCorp believes it has adequately addressed these risks, based on its current understanding of them, and coal plants remain a low-cost option. The IRP action plan includes further work to develop and test the viability of a coal baseload thermal unit, including an ongoing assessment of the risks.

The Company's IRP proposes a significant procurement of new resources. The strategy outlined in the IRP includes the addition of about 4,000 MW of new capacity over the first 10 years of the 20-year IRP. The least-cost, risk-adjusted approach proposed is a diverse portfolio of resources, including renewables, DSM and thermal baseload and peaking units. These additions include the following portfolio additions during the planning period:

- 1400 MW of renewable resources
- 450 MWa of DSM and 90 MW of direct load control
- 2100 MW of baseload capacity
- 1200 MW of peaking capacity
- 700 MW shaped resource contracts

The Action Plan details findings of resource need and specific implementation actions. The plan also outlines step-by-step decision processes by which proposed resources will be continually evaluated and procured. Going forward, PacifiCorp will implement the Action Plan, while also maintaining the flexibility to adjust to future changes and opportunities. The Action Plan will be revisited and refreshed no less frequently than annually.

For analytic purposes, the IRP assumes new resources are developed and owned by PacifiCorp. However, no decision has been made to invest in specific resources. The decision to own, build and invest in a new resource versus contracting with a third party would be made as part of the procurement process for each new resource addition, and on a case-by-case basis. A multi-state process (MSP) (Case No. PAC-E-02-3) is expected to provide clarity on the regulatory treatment on investment decisions and the degree of cost recovery risk held by

PacifiCorp. The Company anticipates that the MSP will issue findings in the spring of 2003. The MSP outcome will influence the activities and operations of PacifiCorp and may impact action plan implementation. The Company states that a significant procurement program and potential investment is required to maintain reliable electric service. It is critically important, the Company contends, that state regulators support this IRP and issue their acknowledgement of the Action Plan. This support coupled with a useful and durable MSP outcome, the Company states, is vital to PacifiCorp being able to resolve issues around recovery lag and achieve allowed rates of return, and is critical in ensuring PacifiCorp can continue to provide least-cost, reliable electric service to its customers.

On February 13, 2003, the Commission issued a Notice of Filing in Case No. PAC-E-03-02 and established a comment deadline of March 26, 2003. Comments were filed by the J.R. Simplot Company, Monsanto Company, The Renewable Northwest Project, The Northwest Energy Coalition and Advocates for the West, and the Commission Staff. The comments can be summarized as follows:

J.R. Simplot Company

Simplot in its comments raises the following points and makes the following recommendations:

- The lack of a legitimate discussion of PURPA/avoided cost projects is distressing and leaves the report incomplete. PacifiCorp has not been a supporter of QFs and continues to develop regulated projects at costs exceeding its posted avoided cost rates.

- Natural gas is a just-in-time commodity. Supply/demand and infrastructure constraints will keep gas prices high significantly into the future. Northwest industrial end-users (including Simplot) are telling electric utilities and state regulators that the next generation of large power plants should be coal.

- A greater degree of public involvement from industrial end-users and customer interest groups is needed in the IRP.

- PacifiCorp's acquisition of renewable resources, especially wind, seems to be designed to curry the favor of specific individuals and agencies rather than meet the test of economic reality and the best interests of all ratepayers.

- Historically, PacifiCorp has added generation with high cost (at the time) fuel contracts (e.g., Hermiston) in the rate base while shepherding low cost projects (e.g., Klamath Falls; West Valley Project) into its unregulated merchant side.

- It remains unclear whether the underlying demand forecast assumes the effects of PacifiCorp's projected costs for hydro relicensing (and the attendant loss of hydro capability) and emission improvements on PacifiCorp's existing coal facilities.

- The IRP fails to identify key load forecasting assumptions such as price of electricity, price and availability of competing fuels and changes in the composition of economic activity.

- The IRP should include a thorough discussion of appropriate generating resources for peaking capacity including an Idaho Power Company-type risk advisory program for market access and relevant specific rate designs.

Monsanto Company

Monsanto in its comments raises the following points and makes the following recommendations:

- The Commission should not follow PacifiCorp's request for endorsement of the IRP conclusions and specific action plan. Monsanto recommends that the Commission "acknowledge", not "approve" or "disapprove" the PacifiCorp IRP filing.

- Frequent review.

PacifiCorp is commended for its commitment to revisit and refresh the Action Plan no less frequently than annually and file new IRP plans at two year intervals. This recognizes the need to remain flexible to adjust for future changes, uncertainties and opportunities. Greater regulatory scrutiny is required as PacifiCorp in its Action Plan proposes to add 4,000 MW over the next ten years at a cost projected to exceed \$2 billion.

- Demand Side Management (DSM)

The IRP does not succeed in adequately placing DSM resources or customer generation resources on a consistent and comparable basis with supply side resources for purposes of evaluation or pricing to ensure that all efficient and effective alternatives to traditional utility-built resources will be pursued.

- Conservative Assumptions

The IRP makes a number of conservative assumptions that dramatically increase the projection of required new resources, e.g., 15% planning reserve margin, a 5% limit on expected short-term market exposure, modeling of firm transmission rights only, assumed carbon taxes, renewable assumptions and restrictions on market products and purchases. Collectively, these assumptions lead to extreme projections for necessary resource additions.

- Base Case

An IRP “base case” should represent the utilities best reasonable projections of future conditions, rather than assuming speculative changes or charges or incorporating risk mitigation measures (such as increased planning margin requirements, carbon taxes, unavailability of non-firm transmission, etc.) PacifiCorp should be instructed in future IRPs to utilize a “base case” for analysis purposes that includes PacifiCorp’s best reasonable predictions as to reasonably known and measurable conditions and expectations. A base case run should not assume speculative or unknown events such as possible new taxes or reserve requirements.

- Open Bidding

A fair, open and competitive bidding process should be mandatory for any significant future resource additions. The process should include independent analysis and oversight in the formulation and evaluation of RFPs and in awarding contracts. It should also include a process for Commission resolution of disputes that may arise in the RFP, bidding and contracting processes.

As a regulated utility, PacifiCorp is permitted to earn a return for its shareholders only on rate-based assets. This reality creates an inherent bias in favor of utility construction of resources over acquisition of resources from others.

- Ratepayer Impact

The IRP does not attempt to identify impacts on different classes of ratepayers. Additionally, this and future IRPs should consider elasticity of demand by various rate classes in response to projected rate increases resulting from anticipated resource acquisitions and rate design options.

Renewable Northwest Project (RNP), a non-profit organization promoting solar, wind and geothermal resources.

RNP in its comments raises the following points and makes the following recommendations:

- The Commission should acknowledge PacifiCorp's 2003 IRP.
- The IRP results demonstrate that renewables are a least cost resource.
- The Company's analysis of renewable resources still contain some flaws, the most notable of which is the lack of capacity value assigned to new wind resources.

□ PacifiCorp is the single-largest coal-power producer in the western energy market. The Company is correct to anticipate future regulatory constraints on CO₂ emissions. The only way to limit green house gas emissions is to be actually reducing those emissions. It is short-sighted and risky for PacifiCorp to add another coal plant to its resource mix.

Northwest Energy Coalition and Advocates for the West

The Coalition and the Advocates raise the following points and make the following recommendations:

- The Commission should acknowledge PacifiCorp's 2003 IRP.
- PacifiCorp made several errors which undervalued renewables:
 1. The IRP underestimates the value of green tags.
 2. PacifiCorp gives no capacity value to wind resources.
 3. PacifiCorp undervalues the ability of renewables to mitigate fuel volatility.
 4. PacifiCorp assumes no emissions for purchased power.

The total effect of these errors is conservatively estimated at \$700 million. Correction of the errors should make the Renewables' portfolio the least cost option.

- Demand-Side Management Resources

PacifiCorp should consider the economic value of avoided or deferred transmission and distribution upgrades flowing from DSM acquisition.

DSM resources provide additional value as a hedge against fuel price volatility.

PacifiCorp does not have the regulatory tools in place to seek all cost-effective DSM investments—e.g., no DSM tariff rider or other DSM program funding mechanism. As with Idaho Power and Avista, the establishment of a continuously replenishing DSM fund ensures that program costs are recovered, and streamlines the creation of a portfolio of DSM resources.

Commission Staff

The Commission Staff in its Reply Comments raises the following points and makes the following recommendations:

- Staff believes the IRP analysis conducted by PacifiCorp is the most extensive ever by a utility regulated by the Commission.

- The preferred resource portfolio selected in the IRP consists of a blend of thermal plants, gas-fired plants, renewables, load control programs and DSM. This blend of resource types was the natural result of the analysis, not due to a preconceived belief by PacifiCorp that a diverse mix of resource types would be preferable.

- PacifiCorp has indicated to Staff its intent to release a series of four RFPs in the immediate future. The first, expected to be released in approximately 60 days (Staff comment file date March 26), will be seeking bids for east side capacity resources. The second RFP, to be issued in approximately 90 days, will be seeking wind or other renewable resources, both on the east and the west side. A third RFP will be issued in about 120 days for west side capacity resources. Finally, in early 2004, an RFP will be issued seeking a base load unit in the east.

Staff does not believe it is appropriate to seek new resources through RFPs any sooner than necessary. There is value in being able to defer decisions. The costs and viabilities of various resource alternatives are likely to change over time.

- PacifiCorp has stated its intent to revise and update its Action Plan at least annually; it should try to maintain as much flexibility in its resource acquisition efforts.

- Staff recommends that PacifiCorp enlist the aid of an independent third party to ensure that new resource evaluations are fair and complete, and that any Company self-build options are compared on a non-discriminatory basis.

- PacifiCorp intends to keep the Commission and Staff apprised of key resource activities, by providing procurement program status reports approximately every six months. Staff recommends that PacifiCorp also keep the Commission and Staff informed as to its activities and programs on any Requests For Proposals (RFPs).

- Staff is satisfied with the preferred portfolio selected in the IRP, but has some concern as to whether the aggressive level of wind resource acquisitions spelled out in the IRP can be sustained.

□ The Company has designed its Action Plan based on a planning margin of 15%. Further study of an appropriate planning margin for PacifiCorp will continue and is an appropriate element of the Action Plan.

□ Staff is encouraged by PacifiCorp's commitment to more closely align its resource planning and its business planning. A resource planning function has been created and organized in the Company's Commercial and Trading Department to ensure integration with PacifiCorp's resource procurement, trading and risk management functions.

□ Staff advises that if any other party in this case objects to some portion of the Company's IRP, that party should participate in the IRP process and seek to express its concerns and influence the next IRP to be filed in 2005.

□ Staff has always viewed "acknowledgement" as being closely related to the process of integrated resource planning, rather than the result. By acknowledging a utility's IRP, Staff believes the Commission is endorsing the process the utility followed in developing the plan, but not necessarily any actions called for in the plan. The results will be scrutinized in due course when the utility seeks rate recovery. Presumably, if the utility has followed a fair and thorough planning process, it will lead to a prudent, least cost, least risk result that can be supported by the Commission.

Commission Decision

PacifiCorp has submitted its 2003 IRP pursuant to prior Commission direction. Commenting parties have offered a critique of the IRP and suggested changes and recommendations. The Commission's standard practice with IRP filings is to simply "acknowledge" the filing as complying with prior Commission Orders. How does the Commission wish to treat PacifiCorp's present filing? How does the Commission wish to treat the filed comments and recommendations?

Scott Woodbury

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