

## DECISION MEMORANDUM

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

**FROM: SCOTT WOODBURY**

**DATE: MARCH 17, 2004**

**RE: CASE NO. PAC-E-04-1 (PacifiCorp)  
DETERMINATION OF EWG "ELIGIBLE FACILITY" STATUS  
SKOOKUMCHUCK HYDROELECTRIC PLANT**

On February 12, 2004, PacifiCorp filed an Application with the Idaho Public Utilities Commission (Commission) regarding the proposed sale by PacifiCorp of its ownership interest in the Skookumchuck Hydroelectric Plant, a 1-megawatt (MW) generation facility located in the state of Washington. The facility is co-owned by PacifiCorp, Avista Corporation, Public Utility District No. 1 of Snohomish County, Puget Sound Energy, Inc., City of Tacoma, City of Seattle and Public Utility District No. 1 of Grace Harbor County (collectively the "Owners").

PacifiCorp has entered into a Purchase and Sale Agreement to sell the Skookumchuck Hydroelectric Plant to 2677588 Washington LLC, a Limited Liability Company formed by TransAlta USA, Inc. (TransAlta). The Skookumchuck Project is a small, 1 MW hydroelectric facility located in the vicinity of Centralia, Washington on property adjacent to the Centralia Power Plant, a large coal-fired generating facility. Washington LLC intends to operate the Skookumchuck Project as an exempt wholesale generator (EWG) within the meaning of Section 32 of the Public Utility Holding Company Act of 1935 (PUHCA).

PacifiCorp seeks a Commission Order making certain public interest findings required in order for this Skookumchuck Project to qualify as an exempt facility and for Washington LLC to qualify as an EWG under Section 32 of PUHCA.

Washington LLC is a Washington Limited Liability Company and a direct wholly-owned subsidiary of TransAlta. TransAlta is the indirect owner of the Centralia Power Plant and

the Centralia Coal Mine. In 2000, the Owners sold the Centralia Power Plant to a direct wholly-owned subsidiary of TransAlta, TECWA Power, Inc., and PacifiCorp sold the Centralia coal mine to another direct wholly-owned subsidiary of TransAlta, TECWA Fuel, Inc. TransAlta Centralia Generation LLC, a direct wholly-owned subsidiary of TECWA Power, Inc., owns and operates the Centralia Power Plant as an EWG.

The Skookumchuck Project is an earth-filled dam and hydroelectric generating plant located in the vicinity of Centralia, Washington on property adjacent to the Centralia Power Plant. The Skookumchuck Dam was constructed in 1973 as a water storage facility for the Centralia Power Plant. In 1991, a generating plant with a capacity of approximately 1 MW was constructed at the dam. The Project was granted an exemption from licensing as a hydropower facility by the Federal Energy Regulatory Commission (FERC) pursuant to 16 U.S.C. § 2705(d), which allows exemptions for facilities less than 5 MW. The Project is, however, subject to dam safety regulations by the FERC.

PacifiCorp proposes to sell and transfer to Washington LLC the dam, powerhouse, water rights, land, easements and other assets of the Project, including certain fixtures, contracts and other rights. The sale and transfer of the Project is governed by the Skookumchuck facility's Purchase and Sale Agreement between the Owners and Washington LLC, dated November 25, 2003, ("Sale Agreement"), which is attached to the pre-filed direct testimony of Company witness Randy A. Landolt.

The aggregate sale price of the transaction is approximately \$7.57 million, adjusted for changes in PacifiCorp's net book value of the facilities from September 30, 2003 to the closing date. *See* Section 2.3(a) of the Sale Agreement. PacifiCorp's share of this amount is 47.5%. The sale price is determined in such a manner that PacifiCorp will receive its net book value of the assets being transferred, with no appreciable gain or loss. Payment will be made by wire transfer at closing.

PacifiCorp is informed that Washington LLC will continue operation of the Project to provide cooling water supply to the Centralia Power Plant and that it will produce power from the Project either as an EWG or as a Qualifying Facility under the Public Utility Regulatory Policies Act of 1978 (PURPA). None of the electrical output of the Project will be used to serve PacifiCorp's retail customers, except perhaps indirectly through the wholesale power markets.

To qualify as an EWG, Washington LLC must be engaged exclusively in the business of owning or operating an “eligible facility” and selling electric energy at wholesale. If the costs of a generation facility were included in the rates of a regulated utility on October 24, 1992 (the date of enactment of Section 32 of PUHCA), then in order for the facility to be considered an “eligible facility,” every state Commission having jurisdiction over such rates must specifically determine that allowing the facility to become an eligible facility (1) will benefit consumers, (2) is in the public interest, and (3) does not violate state law. 15 U.S.C. § 79z-5a(c). Thus, the Commission and each of PacifiCorp’s other state regulatory commission’s must make these determinations regarding PacifiCorp’s transfer of the Skookumchuck Project.

***A. Compliance with State Law***

Because the Project assets are located in the state of Washington, PacifiCorp contends that Idaho’s property transfer statute, *Idaho Code* § 61-328, is not applicable to the contemplated sale. Accordingly, the Company contends that the sale of the Project to Washington LLC and allowing the generating facilities to become an eligible facility will not violate Idaho state law.

***B. Benefits to Customers***

PacifiCorp proposes to transfer the project to Washington LLC because the sale is a lower cost option than continuing to invest in and operate and maintain the Project.

The Skookumchuck Project has an electrical capacity of 1 MW, but because the Project is operated for purposes of supplying cooling water to the Centralia Power Plant, PacifiCorp states that it has relatively low energy output. Over the last eight years, the average annual production has been 3,000 MWh. The Project’s bus-bar cost in fiscal year 2003 (12 months ending March 31, 2003) was approximately \$255 per MWh. The facility is interconnected with the distribution system of Puget Sound Energy, Inc. (PSE) and historically all of the power from the Project has been sold to PSE.

As one of the owners of the Project, PacifiCorp must pay its proportionate share of the costs of the Project. The Company analysis and forecast predict that ratepayers will see lower costs if the Project is sold because the projected cost of power from the Project substantially exceeds the Projected cost of market power. Moreover, the expected impact of the sale is to lower the Company’s future revenue requirement by removing the Project from the Company’s rate base and revenue requirement. The expected present value of the future reduction in Idaho revenue requirement is approximately \$700,000.

The proposed transaction eliminates the risk that PacifiCorp will be required to fund its share of expenditures for ensuring the structural integrity of the Skookumchuck Dam. PacifiCorp's share of this investment is estimated to be \$4 million. PacifiCorp contends that the benefits from the proposed sale outweigh the risks of rising costs of continuing to own and operate the Project. Continued operation of the Project as a hydroelectric project, the Company contends, would be uneconomic, and such operation would not be in the public interest.

### ***C. Public Interest Standard***

PacifiCorp contends that the transfer of the Skookumchuck Project to Washington LLC is in the public interest because it will benefit PacifiCorp's customers by lowering the Company's cost of providing electrical service. In addition, the transfer will give TransAlta greater control of the water flows in the Skookumchuck River for providing cooling water to the Centralia Power Plant, thus increasing the electrical output of the Centralia Power Plant for the benefit of all electricity consumers.

Washington LLC, the Company contends, cannot process its EWG Application with the FERC until all of the Company's regulatory commissions have made the three determinations required by Section 32 of PUHCA. Accordingly, PacifiCorp requests that the Commission process the matter expeditiously and pursuant to Modified Procedure, i.e., by written submission rather than hearing. Reference Commission Rules of Procedure, IDAPA 31.01.01.201-204.

Exhibits to the Company's Application include the following: (1) Application Exhibit No. 1: Original Cost, Accumulated Depreciation and Net Book Value of Assets to be Transferred as well as the proposed journal entries to record the transfer.

(2) The prefiled direct testimony of Randy A. Landolt, PacifiCorp's managing director of hydro resources, which describes the proposed sale, including how the sale is in the public interest. The Sale Agreement, which is the instrument governing the contemplated sale, is included as Exhibit No. 1 to the pre-filed testimony of Mr. Landolt.

(3) The prefiled direct testimony of Craig P. Johnson, PacifiCorp's regulatory consultant, describing the ratemaking impacts of the proposed sale.

On February 20, 2004, the Commission issued Notices of Application and Modified Procedure in Case No. PAC-E-04-1. The deadline for filing written comments was March 11,

2004. Timely comments were filed by Commission Staff and one Norman E. Anderson of Kuna, Idaho. Mr. Anderson states that with regional electricity needs increasing it seems inappropriate that any public utility be permitted to sell off a power generating facility. The only way PacifiCorp ought to be allowed to remove the facility from its resource portfolio, Mr. Anderson contends, is that it commits to an equal generating capacity from another source. Commission Staff in its filed comments concludes that the proposed sale (1) will benefit consumers, (2) is in the public interest, and (3) does not violate Idaho state law. Staff recommends approval of the Company's Application. Staff also recommends that the Company be required to file final accounting entries with the Commission within 45 days of closing.

### **Staff Comments**

Commission Staff in its Comments states that it has reviewed the referenced U.S. Code language regarding exempt wholesale generators (*see* Staff Comments, Attachment A, 15 U.S.C.A. § 79z-5a). As to the applicability of Section 32 of PUHCA and the requirement of Commission eligible facility determinations, Staff represents that the ownership interest of PacifiCorp in the Skookumchuck facilities are a part of the utility's rate base in Idaho on which PacifiCorp receives a return on investment and is now and has been included in the rate base of PacifiCorp since or prior to October 24, 1992. Based on Staff's review of the Idaho Code, Staff represents that it has discovered no Idaho laws that address the issues raised by the Company's request, and none (including *Idaho* Code 61-328) prohibit or limit the authority of Washington LLC as an EWG to operate Skookumchuck as a wholesale facility.

Commenting on the benefit to customers, Staff notes that the aggregate sale price of the transaction is approximately \$7.57 million, adjusted for changes in PacifiCorp's net book value of the facilities from September 30, 2003, to the closing date. PacifiCorp's share of this amount is 47.5%. The sale price is determined in such a manner that PacifiCorp will receive its net book value of the assets being transferred. After taxes and closing costs, PacifiCorp estimates a net loss from the sale of \$68,613.

Despite the relatively small projected financial loss on the sale, Staff believes there are other factors that should also be considered by the Commission. The Company's analysis and market price forecast predicts that ratepayers will see lower costs if the project is sold because the projected cost of power from the project substantially exceeds the projected cost of market power. According to PacifiCorp, the expected impact of the sale is to lower the

Company's future revenue requirement by removing the project from the Company's rate base and revenue requirement. The Company calculates the expected present value of the future reduction in Idaho revenue requirement is approximately \$700,000 on a present value basis. Staff accepts these calculations for the sale analysis.

PacifiCorp notes that the proposed transaction eliminates the risk that the Company will be required to fund its share of expenditures for ensuring the structural integrity of the Skookumchuck Dam. The Company believes that it is likely the FERC will mandate dam modifications to meet stability criteria. PacifiCorp's share of this investment is estimated to be \$4 million.

The Skookumchuck project has an electrical capacity of only 1 MWh. Moreover, because the project is operated for purposes of supplying cooling water to the Centralia Power Plant, PacifiCorp states that it has relatively low energy output. Over the last eight years, the average annual production has been approximately 3,000 MWh per year, and over the last four years the output has been limited to about 1,000 MG hours per year. This represents a very low capacity factor for a hydroelectric plant.

Finally, Staff notes that the project no longer represents "core business" assets to any of the current Owners because they no longer have any ownership interest in the Centralia Steam Plant. Operation of such a small plant located so far from any other PacifiCorp facilities, Staff contends, is problematic.

In summary, PacifiCorp contends that the benefits from the proposed sale outweigh the risks of rising costs of continuing to own and operate the project. Continued operation of the project as a hydroelectric project, the Company contends, would be uneconomic, and such operation would not be in the public interest. Staff agrees. All things considered, Staff believes that selling the project is a lower cost long-term option than continuing to invest in and operate and maintain the project.

Staff believes that the appropriate measure of whether the public interest standard is met is the effect of the sale on PacifiCorp's ratepayers. PacifiCorp contends that the transfer of the Skookumchuck project to Washington LLC is in the public interest because it will benefit PacifiCorp's customers by lowering the Company's cost of providing electrical service. In addition, the transfer will give TransAlta greater control of the water flows in the Skookumchuck River for providing cooling water to the Centralia Power Plant. Staff agrees that the Company's

ratepayers will not be harmed by the sale, thus Staff believes that the sale does, in fact, meet the public interest standard.

PacifiCorp as co-owner of the Project with a 47.5% interest in the Project has been one of the primary parties in the sales negotiation. Negotiation costs and all other costs of the sale are being directly assigned to a work order associated with the sale. Labor costs for legal and technical services represent the largest component of the sales cost for PacifiCorp. Because the Project is being sold at PacifiCorp's book value, the gain or loss on the sale of the Project is determined by the sales cost and any reimbursement offsets. PacifiCorp does not propose to recover any of the costs of sale, i.e., loss on the sale, from customers. If a test year includes these costs, they will be normalized out of the results. PacifiCorp states that if a gain should occur on the sale, that it will be passed 100% to customers.

Staff recommends that PacifiCorp be directed to file the final accounting entries associated with the sale within 45 days of closing. PacifiCorp accepts this recommendation. Any revenue requirement reduction from not operating the project will be reflected in PacifiCorp's results of operation. As such, Staff represents that this change will be reflected in a future PacifiCorp rate proceeding.

### **Commission Decision**

PacifiCorp requests a Commission Order determining that the operation of Skookumchuck as an "eligible facility" upon sale (1) will benefit consumers, (2) is in the public interest, and (3) does not violate state law. The EWG determination requested is a requirement pursuant to Section 32 of the Public Utility Holding Company Act of 1935 (PUHCA) (codified at 15 U.S.C. § 79z-5a(c)). Staff recommends that the Company's Application be approved. Does the Commission find it reasonable to grant the Company's Application and to provide the required EWG determinations?

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Scott Woodbury

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