State of Utah

DEPARTMENT OF COMMERCE
Committee of Consumer Services

To: The Public Service Commission of Utah

From: The Committee of Consumer Services
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Date: May 2, 2007

Subject: Purchase Power Agreement between PacifiCorp, dba Rocky Mountain Power and Tesoro Refining and Marketing Company, Docket No. 07-035-06

Background

On April 12, 2007, the Division submitted a Memorandum to the Commission responding to the Commission's February 12, 2007 action request, which asked the Division to review and provide its recommendation(s) regarding the proposed Power Purchase Agreement (PPA) between RMP and Tesoro. Tesoro operates as a qualifying facility (QF) under PURPA and is expected to deliver to RMP, on a non-firm, hourly basis, 12 MW during peak periods and 7 MW during non-peak periods.

The Division recommends that the PPA be approved as proposed. However, the Division raised concerns with the inclusion of an avoided transmission line loss adjustment of 3.58% in the PPA because Tesoro is only required to deliver power to RMP on a non-firm basis. According to the Division, it is "unconvinced…that allowing an avoided transmission line loss adjustment to QFs providing non-firm power is necessarily appropriate." The Division takes a neutral position on the line loss issue in this docket for two reasons: (1) the PPA expires prior to RMP's next rate case; and (2) the Commission declined to provide guidance on the line loss issue in Docket No. 03-035-14.

The Committee is similarly concerned with non-firm QFs receiving avoided line loss payments and will limit its discussion and recommendation to this aspect of the Tesoro PPA.

Discussion

Avoided Line Losses

In Docket No. 03-035-14, RMP and PacifiCorp (Company) and the Division testified that QFs delivering non-firm power to the Company should not receive an adjustment for line losses. The Committee supported that position. In its April 19, 2006 Order, the Commission concluded that it lacked an adequate record to determine whether the Company's and Division's proposed methods for calculating the value of avoided line losses were reasonable and met the PURPA ratepayer indifference standard.[1] In its May 26, 2006 Order, the Commission clarified that it did not approve a generic method for calculating line losses due to insufficient evidence and would consider the reasonableness of avoided line loss payments to QFs on a case-by-case basis. However, in neither order did the Commission make findings as to whether avoided line loss payments were applicable to non-firm QFs.

Tesoro PPA

As part of its PPA, Tesoro receives an avoided line loss payment of 3.58%. The 3.58% represents 80% of the average line loss on the PacifiCorp system which is specified as 4.48% in PacifiCorp's OATT. The 80% figure is apparently based on the premise that Gadsby is expected to have a capacity factor of 20% and its output will normally be backed down when Tesoro is delivering power to the PacifiCorp grid. When Tesoro displaces Gadsby output line losses are assumed to be zero because of the close geographic proximity of the two resources.

The Division appears satisfied that the 3.58% avoided line loss adjustment negotiated between PacifiCorp and Tesoro has a reasonable empirical basis.[2] But as noted above, the Division raises the threshold question as to whether line loss payments should be included in non-firm QF PPAs.

Committee Perspective

The Committee views the avoided line loss issue as having policy and technical dimensions which are linked. The Committee has two primary concerns:

(1) There is no clear evidence on this record for supporting a line loss payment to QFs delivering non-firm power into PacifiCorp's system:

(a) In Docket No. 03-035-14, PacifiCorp, the Division and the Committee all testified that line loss adjustments should be limited to firm QFs. The Commission Avoided Cost Orders were silent on the firm/non-firm issue. At the heart of the issue is whether PacifiCorp, for reliability purposes, has to still "commit" units that are ostensibly displaced by non-firm QF energy.

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1 The Commission identifies various concerns with the proposed line loss methods that will not be recounted here. The concerns are laid out in considerable detail on pages 12-15 of the Commission's April 19, 2006 Order.

2 The avoided line loss issue is discussed on pages 3-5 of the Division's April 12, 2007 memo.

(b) The 2006 Kennecott non-firm QF PPA, which the Commission recently approved, does not include an avoided line loss payment; the proposed Tesoro contract includes such a payment. On what basis is PacifiCorp differentiating between these non-firm QF contracts of similar vintage and how does it impact the PURPA ratepayer neutrality test?

(2) There are a number of technical issues with respect to properly valuing a line loss adjustment. The Committee believes the issues set forth below should be addressed by the Commission and applied to future firm QF contracts.

(a) Is the average line loss on PacifiCorp's system as set forth in its OATT a reasonable proxy for establishing a line loss payment?

(b) Should this OATT average line loss figure be adjusted for aspects relating to the QF and the potentially avoidable resource(s) such as location, expected unit dispatch, unit forced outage rates, etc?

(c) Since PacifiCorp's net power costs are set on a normalized basis using the GRID production cost model and rates reflect those normalized costs, what role should GRID have in valuing avoided line losses to ensure ratepayer neutrality?

(d) How are avoided line losses determined in other PacifiCorp jurisdictions and are line loss payments included in QF contracts?

(e) Are avoided line loss adjustments typically included in PacifiCorp's firm and non-firm wholesale contracts and, if so, how are such adjustments determined?

While the proposed Tesoro PPA will not impact general rates due to the short duration of the contract (expires December 2007) and the current rate case stayout (next general rate change anticipated in August 2008), the Committee is nevertheless concerned about the precedent the proposed Tesoro PPA may establish for future non-firm QF PPAs, including a renewal of the Tesoro PPA. In addition, the Committee believes the various policy and technical issues identified in the Division and Committee memos merit further study.

<u>Recommendations</u>

The Committee recommends the following:

(1) The proposed Tesoro PPA should be approved without an adjustment for avoided line losses;

(2) A technical conference should be scheduled to discuss avoided line loss concerns raised in the Division and Committee memos;

(3) If the Commission approves the Tesoro PPA with the avoided line loss payment as proposed, the Commission should clearly specify that such approval sets no precedent for the inclusion of avoided line losses in non-firm QF PPAs.