



State of Utah
Department of Commerce
Division of Public Utilities

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Memorandum

To: Public Service Commission of Utah
From: Utah Division of Public Utilities
Chris Parker, Director
Artie Powell, Manager
Joni Zenger, Technical Consultant
David Williams, Utility Analyst
Date: March 27, 2019
Re: Docket No. 19-035-07, Division's Audit of PacifiCorp's 2018 Fuel Inventory Policies and Practices

Recommendation (No Action)

The Division has reviewed the 2018 fuel inventory policies and procedures of PacifiCorp (the Company) and finds that the Company is generally in compliance with the Public Service Commission's (Commission) directive in Docket No. 09-035-23. No further action is required.

Issue

This memorandum is in response to the Commission's Report and Order in Docket No. 09-035-23 that directs the Division to conduct an annual audit of the Company's fuel inventory management policies, procedures, and actual practices and provide a summary of its audit and associated findings to the Commission by no later than March 31 of each year for the previous year's activity.¹

¹ Docket No. 09-035-23, Report and Order on Revenue Requirement, Cost of Service and Spread of Rates, February

This memorandum represents the Division's ninth annual audit and report to the Commission. This report does not preclude the Division's analysis of coal inventory levels or any associated net power costs issues in the current Energy Balancing Account filing (Docket No. 19-035-01) or in upcoming general rate case proceedings.

Discussion

In conducting its review, the Division met with the Company's Fuel Resources Department on March 14, 2019 and again on March 25, 2019. At the meetings, the Division discussed the assumptions and inventories at each of the Company's owned and affiliated plants. The Division also looked at plant deliveries, coal supply, and coal consumption at the Company's operating plants. The Division reviewed confidential documents, including the December 2018 coal inventory levels and PacifiCorp's Coal Inventory Policies and Procedures, dated March 14, 2019 (the 2019 Policies and Procedures Manual).

Per the Division's recommendation in its March 31, 2014 audit report,² the Company performed an updated analysis of its current coal inventory policies and updated the stockpile target levels at its Utah and Wyoming coal operating plants. The Company retained the consulting firm RPMGlobal, to update the coal inventory review in 2015 and in 2018 (the RPM Report). RPM performed the analysis and completed its most recent report on March 19, 2018. The Division has reviewed the 2018 RPM Report and confirmed that the Company has updated its target inventory levels at each of its owned coal plants using the recommendations from the RPM Report.

The Division looked at both historic and average stockpile levels, compared those to the Company's targeted inventory levels and determined whether the Company met its targeted tonnage levels and burn days at each respective coal generating plant. The targeted fuel inventory levels and burn days are based on recommended target levels that were determined in the analysis contained in the RPM Report. The Division verified that the Company has in place

18, 2010, p. 106.

² Docket No. 14-035-35, Division's Audit of PacifiCorp's 2013 Fuel Inventory Policies and Practices, March 31, 2014.

tracking and monitoring requirements associated with its policies and procedures. The Fuel Resources Department monitors inventory levels, and aerial surveys are performed quarterly for the Company's operated coal plants to determine the stockpile amounts.

The Commission's Report and Order in Docket No. 09-035-23 states the following goals of the Company's coal inventory policy:

The policy should provide an overall management strategy, flexibility to react to favorable market conditions, documentation requirements for deviations from the policy with an assessment of the costs and benefits associated with deviations, and tracking and monitoring requirements. In response to this policy, the Division should, during the course of its annual auditing, review inventory levels and compliance with inventory policies.³

The Division has reviewed the following documents:

- The 2019 Policies and Procedures Manual (confidential)
- The PacifiCorp Coal Inventory Confidential Review of 2018 Inventory Levels with the Division of Public Utilities, March 14, 2019 (the Review of 2018 Inventory Levels) (confidential)
- The Coal Inventory Study for Coal-Fired Power Plants in Wyoming and Utah, March 19, 2018 (the 2018 RPM Report) (confidential)
- Other materials provided by the Company (confidential)

Findings

The Company's Coal Inventory Policies and Procedures manual (Policies and Procedures Manual) is updated each year. This year's manual, the 2019 Policy and Procedures Manual, is dated March 14, 2019. The 2019 Policy and Procedures Manual states that a guiding strategy of coal inventory management is "to provide low cost power to its customers." More specifically, the objectives include: providing the lowest cost fuels over the long run, maintaining adequate inventory levels at each plant, and a managing a complex portfolio of fuels at each plant. The

³ Docket No. 09-035-23, Report and Order on Revenue Requirement, Cost of Service and Spread of Rates, February 18, 2010, p. 105.

Company must plan, adapt, and factor in the delivered cost of fuel, coal supply reliability, coal quality, environmental impacts, operational costs, transportation costs and reliability, flexibility in fuel supply, mine source operating risk, and mine source financial risk.⁴

In its review, the Division considered issues that currently affect the Company's fuel inventory levels and its procurement practices. These issues include the following:

- A decline in coal-fired generation and correspondingly lower average capacity factors,
- The risk profile of geologically complex mines and mine sources,
- The dynamics of the coal industry, including transportation issues, bankruptcies, and possible plant closures,
- Contract specifics (such as take-or-pay contracts, contracts which allow purchasing flexibility, etc.), and
- Environmental laws and regulations, including the uncertainty of current environmental policies and regulations.

The Company employs a diversified coal supply strategy, planning for and managing a multitude of factors, including a decrease in coal production, the shrinking number of coal suppliers, the need to blend lower-quality coal with higher-quality coal in order to get optimized fuel burn, temporary planned and unplanned plant outages, the possibility of permanent plant outages or closures, fluctuating rail rates, and complex third-party coal contracts.

The Division determined that the Company is managing inventories by considering appropriate factors in its longer-term analyses and planning. The Company's fuel procurement policies and practices provide some flexibility in order for the Company to react to changing market conditions and to take advantage of contract advantages when present.

Overall Coal Inventory

Taking all plants as a whole, and accounting for the Company's share of inventory at each plant, the Company's coal inventory was within its target at the end of 2018. If inventories for each

⁴ 2019 Policy and Procedures Manual, p. 4. Here and elsewhere in the Division's report, the Division paraphrases the Company's Policies and Procedures Manual and other documents to protect confidential information.

month are averaged for the whole year, the Company was slightly over the high end of its target for the year.

Inventory at Specific Plants

With respect to individual plants, most plants were within their target ranges at the end of year 2018. Overall, the fuel inventory of all plants combined decreased during the year leading up to December 2018. In general, the Division agrees that the decrease in overall inventory from mid-year to end-year was prudent, due to business and operational projections. For example, temporary planned and unplanned outages can affect coal inventories, causing inventories to rise in certain months or repairs.

At the Company's Jim Bridger plant, the Company has a sharing arrangement with Idaho Power that provides flexibility for each company to use the other company's coal supply. This allows the Company to control costs by maintaining a flexibility of monthly and year-end supply. The Company used this flexibility in 2018 by keeping Company-owned inventory levels below target range during and at the end of the year. However, the Company has shown that the overall inventory at Jim Bridger is close to the plant permit capacity. The Division determines that the Company is being prudent with respect to Jim Bridger inventory, as long as the combined Company/Idaho Power inventories remain near the site maximum. The Division will continue to monitor this in next year's audit.

One of the Company's owned and operated plants had inventory above the upper end of the target range at the end of 2018. The Company has determined that it can provide lower cost fuel at this plant to its customers by taking advantage of current contract prices that will not be available indefinitely.

With respect to the plants that the Company owns jointly, as a minority owner the Company has somewhat limited influence over the inventory levels at those plants, because inventory levels are determined collectively by the plant owners. The inventory levels at most joint-owned plants are within or near the target ranges at the end of 2018. However, at one joint-owned plant, the Company has increased inventory above the target range to take advantage of a contract

opportunity. The Company expect this inventory to fall throughout 2019 and be within target ranges by 2020. At another joint-owned plant, the Company is keeping inventory near the lower end of the range to take operational projections into account.

The Company updated its 2019 Policies and Procedures based on the analysis in the March 19, 2018 RPM report and based on operational and contract expectations at the various plants. The Division has reviewed the Policies and Procedures, dated March 14, 2019. The Division finds that the Company is in compliance with the Commission's directive in its 2009 Report and Order with respect to the Company's fuel inventory policies and procurement practices. Where end-of-2018 levels are outside of the targeted levels, the Company has plans in place to bring the inventory stock into targeted levels as soon as practicable. The Division will continue to monitor this in its next review.

The Company has agreed that going forward, it will provide the end-of-year inventories at each plant, as well as both the previous year's targets and the new adjusted targets. This information will help the Division audit any mid-year revisions to policies.

Conclusion

The Division concludes that: (1) the Company has formal policies and procedures in place for its fuel procurement and coal inventory levels; (2) the Company has generally adhered to its policies and procedures in 2018, and as amended with an effective date of March 20, 2018; and (3) the Company's policies provide flexibility for the Company to react to the changes in the market that the industry faced this past year.

The Division has reviewed the 2019 Policies and Procedures and has conducted its own analysis of target levels versus actual inventory of coal at the Company's generation plants. The Division notes that the Company is generally in compliance with its policies and procedures and has prudent business reasons for plants that are outside the fuel inventory target ranges. Where end-of-2018 levels are outside of the targeted levels, the Company has plans in place to bring the inventory stock into targeted levels as soon as practicable. The Division will continue to monitor inventory stock levels and recommends no action is required by the Commission.

Cc: Jana Saba, Rocky Mountain Power
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