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**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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In the Matter of the Application of PACIFICORP for Approval of an IRP Based Avoided Cost Methodology For QF Projects Larger than 1 Megawatt	<u>DOCKET NO. 03-035-14</u>  <b>UAE’S PETITION FOR REVIEW, REHEARING AND CLARIFICATION</b>
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Pursuant to Utah Code Ann. §§ 54-7-15 and 63-46b-12 and Utah Administrative Code § R746-100-11, the UAE Intervention Group (UAE) hereby petitions for review, rehearing and clarification of the Commission’s Report and Order (“Order”) issued in this docket on October 31, 2005. UAE respectfully submits that the Order as written fails to ensure just and reasonable terms and conditions for QF contracts or avoided cost rates, fails to encourage development of cogeneration and small power production facilities as required by Utah law, fails to protect ratepayers, and will serve to create additional and unnecessary barriers that will discourage the development of achievable, cost-effective and efficient QF resources in this State, leading to over-development of and increased reliance on less-efficient, more costly generating resources.

UAE requests review, rehearing and clarification as to the following issues and on the following grounds (discussed in the order in which they are addressed in the Order):

**1. *Out of System QFs.*** Page 5 of the Order includes the following statement, made in the context of a discussion of Schedule 37: “Other requirements may apply to ... out-of-system QFs seeking to wheel power to Utah for sale to the Company.” UAE fears that this sentence may create ambiguity or potentially unlawful results. In UAE’s view, federal and state laws require that a utility must treat any QF power delivered into Utah in the same manner, regardless of the location of the QF facility. UAE requests confirmation or clarification that the pricing and other provisions of the Order, as well as the requirements of Schedule 37, apply equally to any QF able to deliver power into Utah, regardless of where the QF facility is located.

**2. *The Next Deferrable IRP Resource.*** Page 8 of the Order and ordering paragraph 1 on page 32 approve a methodology for determining avoided capacity payments based on the “next deferrable IRP resource.” The Order is not clear, however, as to how that resource is to be identified at any particular point in time. Several important questions remain, including: Is the “next deferrable IRP resource” based upon the next resource proposed in the most recent IRP and action plan that were both acknowledged, the most recent IRP and action plan that were filed (even if not acknowledged), the most recent IRP update, or something else? What if the resource proposed in an earlier acknowledged action plan cannot now practically be completed in the remaining time? What if the utility has filed an update that proposes a new resource? What if the utility proposes to defer a resource because of changed QF assumptions? Does the deferrable resource always remain constant for at least two years between IRP acknowledgment cycles?

What if the next proposed resource changes after a request for indicative pricing has been submitted, or before a contract has been signed, or before a contract has been approved by the Commission? What if this Commission has acknowledged an action plan but the Commission in another state has specifically rejected the next proposed resource, making it unlikely that it will ultimately be constructed? UAE requests clarification as to these issues.

One of the most important components in encouraging QF development is pricing certainty; this has been clearly demonstrated by the level of interest shown following approval of the QF stipulation which established set pricing (and a meaningful tolling arrangement) for the first time in this State. UAE submits that, if critical pricing terms can be changed periodically by the utility without clear Commission guidance, QF development will continue to be thwarted.

For QFs who submitted pricing requests prior to the utility's formal 2005 IRP update, or who submit requests in the near future up to the QF level assumed in deferring the 2009 gas plant, UAE submits that pricing should be based on the 2009 gas plant proposed in the utility's 2004 IRP. That was the resource on which all GRID model runs and all analyses were performed in the recent case. Any fundamental change in the approach to pricing for pending QF requests would result in unfair and prejudicial delay and discouragement of these projects. Moreover, these and other QF projects provided, at least in part, a basis for the utility's decision to cancel the proposed 2009 gas plant. It would be particularly unfair and inappropriate to deny these entities pricing based upon the very plant that their QF projects helped defer.

In the future, UAE proposes that the "next deferrable IRP resource" used in responding to pricing requests should be a specific resource identified by the Commission in an appropriate

order as the next deferrable resource. Such a designation should be made by the Commission in any order responding to a request for acknowledgement of an IRP and in response to any update. The Commission's designation should continue to apply for all pricing requests received by the Company before a new Commission order is issued that changes the avoidable resource on a prospective basis. The Company should be directed to file an IRP update anytime it makes an internal decision that the next deferrable resource should be changed, along with a request for a Commission order designating the resource to be used in responding to QF pricing requests received after the date of the Commission's approval order. Ambiguity and disputes over resources and pricing should be minimized with such an approach.

**3. *Non-Firm Transmission.*** On page 14 of the Order, and in ordering paragraph 4 on page 33, the Commission directs the Company to include non-firm transmission in the GRID model based upon a 48-month history. UAE asks the Commission to direct PacifiCorp promptly to submit a compliance filing to demonstrate compliance with this requirement (and other requirements of the Order). Among other things, the filing should specify the level of non-firm transmission included, provide support for the selected level, explain all changes made to the model and its inputs to incorporate non-firm transmission and explain any resulting impacts on the output of the model.

**4. *Dispatchability.*** Pages 14-16 of the Order and ordering paragraph 3 deal with a tolling option "for dispatchable QF energy output" (Order at 33, ¶ 3). Elsewhere, the Order specifies that a tolling arrangement applies in hours in which energy is dispatched by the utility (e.g., pages 10, 14). It is UAE's reading and understanding of the Order that tolling pricing is paid in all hours dispatched by the utility on a day-ahead basis and that the QF remains free to

deliver energy in non-dispatch hours at a price determined by an appropriate GRID run (or to sell non-dispatch energy to others). However, some confusion has arisen around this point. For example, it has been suggested that variable pricing may be available only if a QF is willing to operate only during dispatch hours. It has also been suggested that the utility can make “day-of” dispatch changes that affect pricing or QF operations. UAE does not believe that any such reading is supported by the Commission’s Order. Moreover, such interpretations would make tolling arrangements unacceptable in virtually every circumstance. UAE requests clarification that variable pricing is to be paid under firm contracts electing this option in all hours designated by the utility on a day-ahead basis, with GRID-based pricing paid in all non-dispatch hours in which the QF elects to sell energy to the utility. Moreover, UAE requests clarification that the utility must provide to the QF, in advance, the pricing that will be paid in non-dispatch hours.

5. ***The Company’s Relevant Fuel Costs in Rates.*** Page 16 of the Order approves use of “the Company’s relevant fuel costs in rates” for variable energy pricing. Ordering paragraph 3 on page 33 similarly references the “Company’s relevant fuel costs.” UAE respectfully submits that this portion of the Order is ambiguous and not properly supported on the record, and that it is virtually useless to QFs as a variable pricing option.

The “Company’s relevant fuel costs in rates” is ambiguous. The Order does not identify which fuel is “relevant;” nor does it explain how relevant fuel costs are to be determined. A host of unanswered questions arise, including: If the deferrable resource on which the avoided capacity cost is determined for a specific QF project is a natural gas unit, are the relevant fuel costs natural gas costs only? If not, what fuel costs are included? Does the “relevant” fuel remain the same for the life of the QF contract or does it change if a future deferrable resource

uses a different fuel? How are fuel hedging mechanisms used by the utility factored into avoided cost rates? How are normalizing, annualizing and pro forma rate case adjustments factored in? Do the relevant fuel costs vary every hour, day and month based on a fuel price forecast from the rate case? Is the same fuel cost paid in all hours based on an average of the hours in the test year? Do fuel costs vary in future years based on the type of fuel price forecast used in the rate case? Do the same fuel costs continue in effect indefinitely unless and until a new rate case order is entered? How are relevant fuel costs in rates determined, particularly if the rate case was settled without adoption or approval of a specific fuel cost forecast? What is the impact on variable avoided costs if a fuel cost adjustment mechanism is adopted?

UAE respectfully submits that the proposal to use “fuel costs in rates” was made late in the proceeding and that there is insufficient critical analysis or review on the record to make it a just, reasonable or supported means of setting rates under a tolling arrangement. Avoided costs are predicated on costs that a utility may avoid, not on rates paid by ratepayers. Moreover, the approach adopted in the Order is not necessary to maintain ratepayer neutrality.

Avoided capacity costs are calculated based upon a reasonable set of assumptions – e.g., that, at appropriate avoided cost rates, sufficient QF capacity will be available to defer the need for a specified resource. Avoided capacity costs are not adjusted after-the-fact based on an analysis of whether QF projects actually contributed to a plant deferral. Avoided fuel costs should also be determined based upon reasonable assumptions, not based on an attempt to determine fuel costs used in a prior proceeding to set retail rates.

Absent QF contracts that presumptively permit the deferral of a resource, the utility would build the resource and pay actual fuel costs as they are incurred, for which ratepayers would ultimately be responsible (if prudently incurred, and subject to prudent hedging strategies and ratemaking adjustments). These actual avoided fuel costs should establish variable fuel costs paid to a QF that elects a variable priced option. Ratepayer neutrality is maintained, as with avoided capacity costs, through the use of reasonable assumptions as to the deferability of a resource.

Currently, we do not need to even speculate about the reasonableness of the deferral assumption; the utility has now cancelled plans for the 2009 natural gas plant proposed in its last IRP action plan based, in part, on assumptions as to QF deliveries. QFs that contribute to that deferral should be paid avoided variable fuel costs based on actual market prices that the utility would have incurred but for the deferral.

UAE appreciates the Commission's efforts to promote cogeneration and its recognition that a tolling option is essential for most QF projects to be feasible. Many potential developers and their financial backers simply cannot tolerate the significant fuel volatility risks of today's natural gas market. A tolling arrangement allows the developer and its bankers to avoid that volatility. Some argue, incorrectly, that facilitating the QF developer's need to avoid fuel risk is inappropriate. To the contrary, it is both essential and mandated by Utah laws that encourage the development of cogeneration. Absent deferral of a project, due at least in part to QF resources, the utility and its ratepayers would face the identical fuel volatility risks that they face with a QF tolling arrangement based on a market index (subject to prudent hedging activities, which are still available). With a QF tolling agreement the utility and its ratepayers face the very same risks

they would have faced but for the deferral, but the QF is able to avoid market risks that, in many cases, would make financing of the QF project impossible. Ratepayer neutrality is thus maintained and QF development is encouraged, as required by Utah law. Indeed, this is precisely the type of win-win scenario that must be encouraged under Utah law.

In attempting to approve the continued availability of a tolling option, the Commission's Order adopts a "variable" fuel cost that will not be reflective of actual market conditions. With such an approach, a QF developer cannot avoid fuel risk volatility; nor can the developer effectively hedge against fuel price risk. The Commission's laudable effort to encourage QF development through continued availability of tolling arrangements will thus be for naught; a tolling arrangement that does not permit a QF to be paid based on actual market prices is simply another prediction of future pricing which, like a fixed pricing option, will be incorrect. Either one will leave the owner subject to the significant risk that fuel prices will vary from the forecasts. To be meaningful, a variable priced tolling option must mirror actual market prices. UAE asks the Commission to approve a tolling arrangement based upon actual market prices as reflected in an available index such as the Opal gas index, plus actual transportation costs. To protect ratepayers, the utility should be required to engage in prudent hedging activities for the tolling gas as well as its purchased gas.

**6. Availability.** Page 17 of the Order acknowledges that "PDDRR results will reflect QF dispatchability, reliability and availability" and the Order thus accepted pricing "adjustments" based on the same. UAE fears, however, that potential ambiguity may have been created in the following accompanying sentence: "For the QF to be paid for avoiding capacity, it must meet the



availability of the avoidable resource.” UAE submits that the Order’s focus on price adjustments based upon differences in dispatchability, reliability and availability is clearly defensible, and that the accompanying sentence should be interpreted in a consistent manner to require the same availability to receive the same capacity payment. Any variations in dispatchability, reliability and availability, either less or greater than the avoided resource, should be dealt with in pricing adjustments, liquidated damage provisions or other contractual remedies. UAE requests clarification that this is the Commission’s intent.

7. ***Avoided Transmission Costs.*** Pages 17-18 of the Order, and ordering paragraph 5 on page 33, direct the formation of a work group to submit a report on avoided transmission capacity costs and line losses. Pending the Commission’s ruling on these issues, UAE includes avoided transmission capacity costs and line losses in this Petition in order to preserve its rights with respect to the same.

UAE submits that, consistent with the approved methodology for determining avoided generation capacity costs, a QF developer should be paid a pro rata portion of associated transmission costs as identified in the relevant IRP for the deferrable resource if the QF point of delivery will contribute to deferral of the resource and its associated transmission. For avoided transmission capacity costs, the QF’s point of delivery should be the only thing determined on a case-by-case basis. Avoided line losses should be paid for deliveries in all hours. The level of line losses to be applied should be determined on a case-by-case basis based on the QF’s location as compared to the avoidable resource, generally comparable to the manner used in the contracts, stipulations and orders approving QF contracts for U.S. Magnesium and Desert Power.

8. ***Short Term Capacity Payments.*** Page 29 of the Order acknowledges UAE's request for levelization of capacity payments in long-term firm contracts and for capacity payments for shorter term firm contract. The Order approves levelization for longer-term contracts (Order, page 34, ¶ 12), but is silent on UAE's companion request for capacity payments for shorter-term contracts. UAE respectfully requests that the Commission recognize that firm contracts avoid capacity costs in excess of the value reflected in short-term market prices, and that payments based on a SCCT should be included for years prior to the year in which the deferrable resource was to be built.

9. ***Access to GRID model.*** The Order directs the utility to notify the Commission and Division of updates to the GRID model, to provide reasonable training on the model and to consider internet access (Order, page 35, ¶ 15). Prompt and continual access to an updated GRID model is essential to any QF owner or potential developer. However, at least until internet access is provided, the Order does not specify how QF owners and potential developers and their consultants are to secure access to the GRID model and any updates. UAE submits that the utility should be directed to: (i) provide reasonable training on the GRID model promptly upon request to anyone who provides a reasonable basis for needing the same; (ii) allow regulators and consultants who have clients that own or operate a QF facility or who are actively considering developing a QF facility to have and retain a GRID computer and model; (iii) provide the model and all instructions promptly upon request to anyone who has received training and who provides a reasonable basis for needing the same; (iv) notify all who have received training of any changes or updates to the model at the same time that the Commission and Division are notified of the same, and offer updated training, if appropriate; and (v) promptly provide updates and updated

instructions to anyone with a GRID computer at the time a change or update is completed.

UAE requests review, rehearing and clarification on the issues discussed herein. UAE respectfully submits that these clarifications and changes are minimally necessary to establish just and reasonable avoided cost rates that are in the interest of Utah ratepayers. Frankly, even with these changes and clarifications, UAE fears that available, efficient and cost-effective QF developments are unlikely to be pursued in this State, leading to excessive reliance on more expensive, less efficient and less socially-desirable generation projects.

DATED this 30<sup>th</sup> day of November, 2005.

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## CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served by U.S. mail, postage prepaid, this 30<sup>th</sup> of November, 2005, to the following:

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