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State of Utah
Department of Commerce
Division of Public Utilities

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MEMORANDUM

To: Utah Public Service Commission
From: Utah Division of Public Utilities
Chris Parker, Director
Artie Powell, Energy Section Manager
Carolyn Roll, Utility Analyst
Joni Zenger, Technical Consultant

Date: March 28, 2013

Re: Recommendation—No Further Action

Docket No. 09-035-23, Division's Audit of PacifiCorp's 2012 Fuel Inventory Policies and Practices

RECOMMENDATION

The Division has reviewed PacifiCorp's (the Company) fuel inventory policies and procedures and finds that the Company has adhered to the Commission's directive in this docket. No further action is required.

ISSUE

This memorandum is in response to the Commission's directive in the 2009 general rate case (Docket No. 09-035-23) 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 This memorandum is in response to the Commission's directive and reports on the Division's third annual audit and associated findings of the Company's 2012 fuel management policies, procedures, and actual practices.

The Division has reviewed the Company's 2012 fuel management policies, procedures, and updates to its policies and provides this 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 or in future rate case proceedings.

DISCUSSION AND FINDINGS

In conducting its audit, the Division met with the Company's Fuel Resources Department on March 6, 2013. At the meeting, the Division discussed in detail the assumptions and inventories at each of the Company's owned and affiliate plants. The Division also reviewed confidential documents containing fuel inventory policies and 2012 inventory levels. The Division's review included detailed spreadsheets containing inventory data for each plant. Average stockpile levels were reviewed and compared to the Company's targeted inventory levels to determine if the Company met its targets.

The Company employs a diversified coal supply strategy, particularly for its short-term strategy. This is due to a decrease in coal suppliers, the need to blend lower-quality coal with higher-quality coal in order to get optimized fuel burn, plant outages, higher rail rates, higher spot coal prices, and third-party coal contract revisions, re-openers, or escalation clauses. In the longer term the Company is analyzing and planning for emerging environmental regulations, long-term basin depletion, coal quality, financial stability of Utah coal companies, and a market that is not liquid.

The Division's audit identified the following key findings:

¹ Docket No. 09-035-23, Report and Order on Revenue Requirement, Cost of Service and Spread of Rates, February 18, 2010, p. 106.

1. The Company has formal Coal Inventory Policies and Procedures in place that it adheres to. The Company's goal and commitment to provide low-cost power to its customers drives its fuel procurement practices.
2. Factors contributing the 2012 fuel inventory levels include: continuing hydro levels that are above forecast levels, lower natural gas prices, decreased burn requirements, coal quality degradation, geologically complex mines, and the changing dynamics of the coal industry.
3. Overall the 2012 inventory levels of PacifiCorp's Utah fleet are slightly above targeted levels due to the fact that the Company is currently in labor negotiations with the United Mine Workers of America (UMWA), which historically has resulted in labor stoppages. This has resulted in the Company managing its coal inventories in preparation for the expiration of the coal labor contract. The Company is tracking and monitoring all of these issues in its policies for procurement and for establishing stockpile target levels at each plant. Once the labor negotiations are completed, the Company will work to decrease the inventory level.
4. Power River Basin plants were over targeted levels due to changing fuel requirements. The Company is in the process of negotiating fuel supply and delivery contracts that better align with current generation needs. The Company's goal is to be within targeted levels by the end of 2013.
5. Inventory levels at the Company's joint-owned plants are above target levels. However, as a minority owner PacifiCorp has limited influence over the inventory levels at those plants. A planned outage at one of the joint-owned plants extended longer than expected, resulting in higher inventory levels. With other plants, low natural gas prices have affected the dispatch at Company plants. The joint-owners are using flexibility under terms of their contracts to bring inventory levels to targeted levels within the next two years.

With respect to the Division's overall audit, the Division recognizes that dynamic conditions require some of the Company's coal plants to be within or slightly above targeted inventory levels. Therefore, the Company made several updates to its 2012 Coal Inventory Policies and Procedures. At some plants the Company has now implemented both short and long-term inventory policies. At other plants, the Company has implemented changes to its policies based on changing mining conditions and aging plant conditions. The Division has reviewed the updated Policies and Procedures, dated January 2, 2013, and finds them reasonable.

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 adhered to its policies and procedures in 2012, and as amended on January 1, 2013; and (3) the Company's policies provide some flexibility to react to favorable market conditions. The Company's Manual states that the Company's strives to optimize delivered fuel costs and ensure supply reliability, while providing appropriate fuel supplies and qualities based on the particular needs at each generating plant. The objectives the Company's fuel management activities as presented in the Manual are to provide the lowest cost of fuels over the long run, maintain adequate inventory levels at each thermal generation station, and build a portfolio of fuels.

CONCLUSION

The Division finds that the Company is in compliance with the Commission's directive in its 2009 Report and Order with respect to its fuel inventory policies. The Division has reviewed the Company's Coal Inventory Policies and Procedures and has conducted its own analysis of target levels versus actual inventory of coal at the Company's generation plants.

The Company's Fuel Resources Department has adopted guidelines that state that the Company plans to review and revise its coal inventory Policies and Procedures when necessary and applicable or to otherwise meet its commitment to provide low-cost power to its customers

through its fuel procurement practices. The Company acted on this guideline and updated its policies on January 2, 2013.

The Division also reviewed the updated policies and finds them reasonable. The Company's formal policies and procedures are in place for its fuel procurement and coal inventory levels, and no further action by the Commission is required at this time.

CC Dave Taylor, Rocky Mountain Power
Michele Beck, Office of Consumer Services