Redacted

Recommendation

To: Public Service Commission of Utah

From: Utah Division of Public Utilities

Chris Parker, Director
Brenda Salter, Assistant Director
Doug Wheelwright, Utility Technical Consultant Supervisor
David Williams, Utility Technical Consultant

Date: April 30, 2024

Re: **Docket No. 24-035-13,** Division's Audit of PacifiCorp's 2023 Fuel Inventory Policies and Practices

Recommendation (Approve)

The Utah Division of Public Utilities (Division) has reviewed the 2023 "Coal Inventory—Policies and Procedures" of PacifiCorp (Company) and finds that the Company is generally in compliance with the directive from the Public Service Commission of Utah (Commission) in Docket No. 09-035-23.[1] The Company faced some challenges in 2023 that resulted in some coal inventory practices that have not previously been utilized. Nonetheless, given the practices that the Company chose to use, the Fuel Resources department managed the inventories in an appropriate manner. The Division recommends the Commission approve the Company's 2023 Coal Inventory Policies and Procedures as complying with the 2010 Order.

Issue

This memorandum is in response to the Commission's 2010 Order, which directs the Division to "conduct an annual audit of the Company's fuel inventory management policies,

[1] *In the Matter of the Application of Rocky Mountain Power for Authority to Increase its Retail Electric Utility Service Rates in Utah and for Approval of its Proposed Electric Service Schedules and Electric Service Regulations*, Docket No. 09-035-23, Report and Order on Revenue Requirement, Cost of Service and Spread of Rates, issued February 18, 2010, p. 106 (2010 Order).

Redacted

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."[2]

This memorandum does not preclude the Division's analysis of the impact of coal inventory levels on associated net power cost issues in future Energy Balancing Account filings, in a general rate case, or in other regulatory proceedings.

Background and Discussion

In conducting its review, the Division met with the Company's Fuel Resources Department on March 11, 2024, via conference call. The Company and the Division discussed the inventories at each of the Company's owned and affiliated coal plants and discussed plant deliveries, coal supply, and coal consumption.

Before the call, the Company submitted the following confidential documents to the Division for review:

- Confidential PacifiCorp Fuel Stock Balance Review (Summary Inventory Data)
- PacifiCorp Coal Inventory – Confidential Review of 2023 Inventory Levels with the Division of Public Utilities – Dated March 11, 2024 (the "2023 Review")
- Confidential PacifiCorp Coal Inventory – Policies and Procedures – Updated March 11, 2024 ("2024 Policies and Procedure Manual," or "2024 Manual")
    - Redlined Confidential PacifiCorp Coal Inventory – Policies and Procedures – Updated March 11, 2024

At the March 11, 2024 meeting, the Company disclosed that its year-end 2023 coal inventories were [redacted]

[2] *Id.*

Redacted

[redacted]

For the review of the 2023 inventories, the Company provided monthly average tonnage levels and end-of-year inventories at each plant, as well as both the previous year's targets and any new adjusted targets. The Fuel Resources Department monitors inventory levels and conducts quarterly aerial surveys for the Company's operated coal plants to determine the stockpile amounts. The Division looked at both historical and average stockpile levels, compared those to the Company's targeted inventory levels, and determined whether the Company met its targeted tonnage levels and days' worth of inventory (days' burn) at each respective coal generating plant. For any plants that were outside the target ranges, the Company and the Division discussed reasons for those inventory levels. The targeted fuel inventory levels and days' burn are based on recommended target levels that were determined in the previous report by RPM and the Confidential 2021 Kaptur Study.

The Division submitted data requests to the Company regarding [redacted][4] On March 28, 2024, the Division requested a one-month extension to allow the Company to respond to the confidential data request, and the Commission granted the request on March 29, 2024.

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

---

[3] The [redacted] is described in the Section below titled [redacted] The [redacted]; the Division uses that term merely as shorthand.

[4] [redacted] touches on aspects of the Energy Balancing Account and other regulatory areas; in this memo the Division only examines the strategy as it relates to the Company's fuel inventory policies and practices.

Redacted

> policy, the Division should, during the course of its annual auditing, review inventory levels and compliance with inventory policies.[5]

As part of its 2023 audit, the Division reviewed the documents listed at the beginning of this section, discussed the documents and the 2023 coal inventory year with the Company, and submitted data requests on the issue.

Findings

The Division has reviewed the Company's updated Coal Inventory Policies and Procedures and has reviewed the target levels versus actual inventory levels of coal at the relevant generation plants. The Company's Coal Inventory Policies and Procedures manual is updated each year. The current manual is dated March 11, 2024 (2024 Manual). The 2024 Manual states that the Company strives to "optimize delivered fuel costs and ensure supply reliability while providing appropriate fuel supplies and qualities based upon thermal generating station requirements."[6]

In its review, the Division considered issues that affected the Company's fuel inventory levels and its procurement practices in 2023. In 2022, natural gas prices were volatile due to the war in Ukraine and other factors. Increased gas prices led to a tight coal supply in general. In 2023, the volatility of natural gas prices decreased, but the Company was faced with Utah-specific supply problems that affected certain plants more than others.

2023 Year-End Inventory Levels

Each PacifiCorp-operated plant has customized target levels, consisting of a target range (low and high).[7] The Summary Inventory Data document sums the high and low ranges for

[5] 2010 Order, p. 106.

[6] Confidential 2023 Manual, p. 4.

[7] These ranges were established by the consultant Casey Kaptur in a March 2021 study "Coal Inventory Study for Coal-Fired Power Plants in Wyoming and Utah".

Redacted

each covered plant to arrive at a system-wide target level.[8] Overall, for the plants summarized in the Summary Inventory Data document, the inventory at year's end was [redacted].

One of the main drivers of inventory in 2023 was the [redacted].[9] Much of this decrease was due to the fire at Lila Canyon, which started in September of 2022 and [redacted][10]

Drivers of the Deviations from Target Levels

Hunter and Huntington receive all coal shipments by truck from local Utah mines. In 2023, the Company had agreements for Hunter with [redacted]

[redacted]

[8] The overall target range represents the sum of recommended ranges for the following coal plants: Hunter, Huntington, Jim Bridger, Naughton, Dave Johnston, Wyodak,* Colstrip, Craig and Hayden.
*[redacted].

[9] 2023 Review, p. 3-4.

[10] ACNR Holdings, Inc. operates the Lila Canyon mine.

Redacted

[redacted].

The Jim Bridger coal plant also had supply issues. Historically, the Jim Bridger plant has received coal from its captive Bridger Coal Company mine, and the local Black Butte mine. In 2023, the Company also used coal from the North Antelope Rochelle Mine, although this [redacted].

2023 Management of Coal Inventories

When faced with force majeure claims and contracted coal amounts fall short, the Company has several options, including the following: (i) it can try to obtain coal from mines other than the originally contracted mines; (ii) it can sue for specific performance or other contractual remedies, and (iii) it can attempt to renegotiate the current contracts. The second option (suing for specific performance or other contractual remedies) will often not solve the issue of how to get the necessary coal for the year; for example, if the suit causes the mining company to file for bankruptcy, the coal from the mine in question is no closer to delivery than it was pre-suit.

In the Company's case, [redacted]. The Division discussed the [redacted] with the Company, and in response to a Division data request, the Company provided a cost/benefit analysis of a scenario in which [redacted].

Redacted

[redacted]

The shortage of Utah coal for the Hunter and Huntington plants caused the Company to enact a coal management strategy [redacted]. The Company described the process as follows:[11]

[redacted]

[redacted]

[redacted] partially explain the lower capacity factors at Utah-supplied coal plants in 2023 (for example, S&P Capital IQ gave the capacity factors at Hunter in 2022 as 61.8%, and 2023 as 32.9%).

Given that Hunter and Huntington are supplied by nearby Utah coal, and that there are a limited number of mines that are local, supply issues can arise if there are unexpected closures of even a single mine, such as the [redacted] or the closure caused by

[11] Company's Response to the Division's *1st Set of Data Requests to Rocky Mountain Power*, March 18, 2024 (Undocketed): *Confidential Response to DPU Data Request 1.1* (dated April 1, 2024). [redacted], and determine whether the resource is [redacted] for the time period in question.

Redacted

the Lila Canyon fire. Given this situation, the Division asked in a data request to see if the Company had performed a cost/benefit analysis of other options, such [redacted]. The Company provided its recent analysis of this issue.[12] There were six scenarios evaluated; the scenarios included a baseline scenario where a [redacted]. The scenarios were evaluated using PLEXOS, which is the cost software used in the 2023 IRP.

Relative to the baseline scenario [redacted] the alternate scenarios had PVRRs that were [redacted] higher. For example, Scenario 5, which involved an [redacted] over the baseline scenario, with over [redacted] of capital costs. Based on these results, the Company's decision to [redacted] was understandable.

In addition to storage at Hunter and Huntington themselves, the Company has the [redacted].[13] At the end of December 2022 [redacted] The [redacted]. The usage of the [redacted] the inventory shortage caused by the Lila Canyon fire and other issues demonstrates the wisdom of [redacted] The Company intends to [redacted] when the opportunity arises.

The Division recommends that the Company continue to evaluate options for supplying fuel to the Utah plants. One option could be to look into possible [redacted]

[12] Attach DPU 1.6 HIGHLY CONF (the Company's highly confidential response to the Division's 1st Set of Data Requests to Rocky Mountain Power, In the Matter of Undocketed, March 18, 2024).

[13] See 2024 Inventory Policies and Procedures at p. 9.

Redacted

[redacted]. The Division also requests that the Company [redacted] (in both tons and market price). Additionally, the management of coal supplies during the supply crunch raises the question of when and how it is appropriate to deviate significantly from inventory policies. The policies help provide operationally secure and economically sound principles for fuel supply. In a case where market prices are high, there may be circumstances where allowing stockpiles to dip lower and taking advantage of lower priced generation is more prudent than firm adherence to inventory policies. Of course, it is also important that the Company remain able to use the coal plants in key times to maintain system stability, so [redacted] as the Company did in 2023 remains a reasonable strategy under most scenarios. Nevertheless, if part of the reason for maintaining inventories is to minimize costs, downward deviation from supply guidelines during times of high market prices may be necessary in certain conditions. In other words, keeping costs low is one rationale behind the inventory guidelines, and in some circumstances, deviating from the inventory policies may take precedence due to cost considerations.

The Company's fuel procurement policies and practices provide some flexibility for the Company to react to changing market conditions and to maximize contract opportunities where possible; this enables the Company to manage fuel supply risk at the least cost to customers. Therefore, an inventory outside the target range does not necessarily result from a flawed Company policy. In the case of 2023, the fact that the inventory was outside the recommended range was due to factors beyond the Company's control.

The determination of inventory levels involves an evaluation of the trade-offs between the costs of coal inventory against the costs associated with coal shortages—lost electricity sales and generation replacement costs.

2023 Coal Inventories

The Division's audit of coal inventories identified the following:

Redacted

- The Company has formal Coal Inventory Policies and Procedures in place that it adheres to. The inventory targets for the relevant plants in the 2024 Manual were the same as the targets in the previous manual.
- Taking all plants as a whole, and accounting for the Company's share of inventory at each of its jointly-owned plants, the Company's actual coal inventory started off 2023 lower than its target. At the end of 2023, the [redacted] than its total target range level [redacted]. The Company has near-term goals to bring the target levels within range in 2024, subject to coal availability.
- During 2023, coal production in Utah was down, due to the Lila Canyon fire and other force majeure events. These two factors in combination resulted in lower coal supplies region-wide.
- At the Company's managed southwest Wyoming plants, the [redacted] for the reasons discussed above.
- At the Company's Utah plants, [redacted]. The utilization of Utah coal plants was down from the previous year, and the [redacted] were a factor in this.
- With respect to the Company's joint-owned plants, in total, the 2023 monthly average coal inventories were within the target ranges. Where the inventories of specific plants were outside the target ranges, inventory levels may not be fully under the Company's control, especially where the Company is not the operator of the joint-owned plant.
- The Division concludes that given the strategy of [redacted], the Fuel Resources department acted appropriately with regard to the plant inventories that are outside the target range.
- The Lila Canyon mine fire has impacted Utah's coal production. The Lila Canyon mine produced a drastically reduced amount of coal in 2023 as compared to past years. This and force majeure events at other mines reduced Utah's coal production

Redacted

in the past year, thus lowering supply, increasing prices, and limiting the ability to cost-effectively restore inventory.

Summary and Conclusion

The Company provided and discussed its most recent Policies and Procedures manual, which was updated in March of 2024. The Division reviewed the 2024 Manual and finds that the Company is complying with the Commission's directive in its 2010 Order with respect to the Company's fuel inventory policies and procurement practices.

Although the total inventories for the relevant plants were lower than the target range at the end of 2023, the low inventory was due to circumstances beyond the Company's control. The Division determined that the Company is in compliance with its policies and procedures and has reasonable plans for plants that are outside the fuel inventory target ranges. The Division believes the Company is adequately managing its coal inventories.

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 generally followed its current policies and procedures in 2023; (3) the [redacted] was understandable from a coal inventory standpoint under the circumstances,[14] and (4) the Company's policies provide flexibility for the Company to react to changing market conditions. The Division recommends the Commission find the Company is compliant with the Commission's 2010 Order and with the Company's Coal Inventory Policies and Procedures.

cc: Jana Saba, Rocky Mountain Power
Michele Beck, Office of Consumer Services

[14] This memo takes no stance on the impact of the strategy on EBA accounts or other related issues.