

DECISION MEMORANDUM

**TO: COMMISSIONER KJELLANDER
 COMMISSIONER SMITH
 COMMISSIONER HANSEN
 COMMISSION SECRETARY
 COMMISSION STAFF
 LEGAL**

FROM: SCOTT WOODBURY

DATE: NOVEMBER 26, 2003

**RE: CASE NO. IPC-E-03-16 (Idaho Power)
 PROPOSED MODIFICATIONS TO PURPA CONTRACT SECURITY
 PROVISIONS**

On November 5, 2003, Idaho Power Company (Idaho Power; Company) filed a Petition with the Idaho Public Utilities Commission (Commission) for authority to accept modified insurance and lien rights as satisfactory risk mitigation measures in PURPA Power Purchase Agreements that contain levelized avoided cost rates. Without risk mitigation, PURPA QFs desiring levelized rates must post liquid funds as security for the overpayment that results from the front end loading that occurs with a levelized rate structure. Two of the mitigation methods authorized by the Commission in Case No. U-1006-292, Order No. 21692 are (1) the purchase of certain basic insurance policies and (2) the establishment of certain lien rights. Petition Exhibit 1 lists the type of insurance and levels of coverages and deductibles deemed acceptable in Order No. 21692, as amended by Order No. 25240, Case No. IPC-E-93-22. Petition Exhibit 2 describes the lien rights of Idaho Power on QF projects that receive levelized purchase rates.

Idaho Power reports that in its most recent audit of QF projects to assess whether those projects continue to conform with the risk mitigation requirements of their specific Power Purchase Agreements with the Company, the Company identified numerous projects that were in non-compliance. Some projects carried no insurance while numerous others had insurance that were products standard in the insurance industry but which, in many circumstances, did not conform with the insurance requirements of the projects' agreements. Idaho Power states that

notices were sent to the various projects which were non-compliant with respect to the insurance requirements and three common responses were received by Idaho Power from those projects: (1) the specific insurance required within the Power Purchase Agreement is not currently available from the insurance industry; (2) because the insurance is not available, as a matter of law (the Doctrine of Impossibility), Idaho Power cannot enforce these requirements or require alternative security; and (3) the financing structures of existing projects do not allow Idaho Power to place a second lien on the project as required in the -292 case.

Regarding insurance, Idaho Power states it has contacted various insurance providers and verified the unavailability of the specified insurance. Idaho Power states that it has also reviewed the potential application of the Doctrine of Impossibility and recognizes that it may be a legitimate claim that may be upheld in legal proceedings.

Regarding liens, the Company concedes that the financing arrangements of some projects preclude a subsequent lien position by Idaho Power or any other party without the consent of the primary lender. However, where those restrictions do not exist, the Company either places a second lien on the project at the time a levelized rate agreement is executed or at the time a project is amended to conform to the risk mitigation requirements of Order No. 21692, as amended. Realistically, however, the Company contends that the value of security obtained by placement of a second lien on a project is tenuous. Either the value of equipment, particularly on less sophisticated projects, is negligible since used or rebuilt equipment is utilized (often non-standard utility equipment, pump motors running in reverse, etc.) or the value of that equipment is highly financed and the financial institution has the first lien on those assets making the value of the second lien marginal. As the project ages and the financing is either paid or at least reduced, the value of the assets depreciate over the same time frame. Thus, the Company contends, were a project to default, the value of the assets remaining for the second lien would be minor due to removal and other costs. Furthermore, the Company states that the value of a project is generally not the actual value of the physical equipment; instead, the marketable and bankable value of a project is the value of the projected revenues of the energy delivered to Idaho Power under the levelized rate agreement.

In response to the requirements of the insurance industry and either the negligible value of second liens on QF projects or the Company's inability to obtain a second lien on a QF project, Idaho Power proposes to conform its QF contract requirements to contemporary

insurance industry standards and realistic lien rights. Due to what the Company contends is the marginal value of the secondary lien position and the inability of the Company, in some circumstances, to obtain security in the form of a second lien, Idaho Power proposes to delete the secondary lien rights as a risk mitigation measure in levelized rate arrangements with QFs.

The Company in Petition Exhibit 3 shows the proposed changes to the basic business insurance requirements that are now deemed by the insurance industry to be reasonably available to QFs.

INSURANCE

<u>TYPE</u>	<u>LIMITS</u>	<u>MAXIMUM DEDUCTIBLE</u>
Commercial General Liability	The greater of 15% of plant cost or \$1 Million/incident	0.5% of Plant Cost <u>Consistent with current Insurance Industry Utility practices for a similar property</u>
All Risk Property	Not less than 90% <u>80%</u> of Plant Cost	0.5% of Plant Cost or \$25,000, whichever is greater <u>Consistent with current insurance Industry Utility practices for a similar property.</u>
Catastrophic Perils (Earthquake and Flood)	Not less than 60% <u>80%</u> of equipment cost	5% of Plant Cost <u>Consistent with current Insurance Industry Utility practices for a similar property.</u>
Boiler/Machinery	Not less than 90% <u>80%</u> of equipment cost	5.0% of equipment cost or \$25,000, whichever is greater <u>Consistent with current Insurance Utility practices for a similar property.</u>
Loss of Income (Business Interruption)	Not less than 75% of estimated daily income; not less than 20% of estimated annual income	30 days of income <u>Consistent with current Insurance Industry Utility practices for a similar property.</u>

All of the above insurance coverages shall be placed with insurance companies with an A.M Best rating of A- or better.

Idaho Power contends that a QF can make changes to the required basic business insurance coverages without imposing substantial additional risk in the event of a default. In addition, the Company contends that by better aligning these requirements with current insurance industry standards and business practices, enforcement and compliance with these requirements will be reasonably attainable.

The Company proposes that the modified insurance requirements be accepted as basic business insurance coverages for purposes of risk mitigation as established in Order No. 21690, as amended, for future QF agreements and for pre-existing QF projects as their current insurance is renewed. The Company also proposes that the requirement for the establishment of secondary lien rights in favor of Idaho Power as established in Order No. 21690, as amended, for future QF agreements and for pre-existing QF projects as their agreements are amended be rescinded.

Idaho Power recommends that its Petition be processed pursuant to Modified Procedure, i.e., by written submission rather than by hearing. Reference IDAPA 31.01.01.201-204.

Commission Decision

Idaho Power in its Petition notes that the Commission's -292 Order had generic consequence for both Avista and PacifiCorp. Staff recommends that a Notice of Petition be issued and that the Idaho Power docket be expanded to include Avista and PacifiCorp (i.e., multiple case numbers). Staff recommends that the case be processed pursuant to Modified Procedure and that the standard comment deadline be extended to six weeks to allow sufficient time for Staff discovery.

Scott Woodbury

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