BEFORE THE

IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF IDAHO POWER COMPANY'S PETITION TO MODIFY TERMS AND CONDITIONS OF PURPA PURCHASE AGREEMENTS	CASE NO. IPC-E-15-01
IN THE MATTER OF AVISTA CORPORATION'S PETITION TO MODIFY TERMS AND CONDITIONS OF PURPA PURCHASE AGREEMENTS	CASE NO. AVU-E-15-01
IN THE MATTER OF ROCKY MOUNTAIN POWER COMPANY'S PETITION TO MODIFY TERMS AND CONDITIONS OF PURPA PURCHASE AGREEMENTS	CASE NO. PAC-E-15-03

REPLY TESTIMONY OF

DR. DON READING

ON BEHALF OF

J.R. SIMPLOT COMPANY AND CLEARWATER PAPER CORPORATION

MAY 14, 2015

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Don Reading and my business address is Ben Johnson Associates, 6070 Hill Road, Boise, Idaho. I am Vice President and Consulting Economist for Ben Johnson Associates.

Q. ARE YOU THE SAME DON READING WHO PREFILED DIRECT TESTIMONY IN THE CURRENT DOCKET ON APRIL 23RD, 2015?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REPLAY TESTIMONY?

A. The following Reply Testimony is to provide comments on the Intervenor testimonies of Rick Sterling and Yao Yin of the Commission Staff (Staff), Adam Wenner and R. Thomas Beach for Idaho Conservation League and the Sierra Club (ICL/Sierra), Anthony J. Yankel for the Idaho Irrigation Pumpers Association (IIPA), John R. Lowe of the Renewable Energy Coalition (Coalition), Ken Miller of the Snake River Alliance (SRA), and Mark Van Gulik of the Intermountain Energy Partners (IEP). Each of the above Intervenors filed Direct Testimony in response to the petitions filed by Idaho Power Company (Idaho Power), Avista Corporation (Avista), and Rocky Mountain Power (RMP) (collectively the "Utilities") asking the Idaho Public Utilities Commission (Commission, IPUC) to modify the terms and conditions of Public Utility Regulatory Policies Act of 1978 (PURPA) contracts.

Five of the seven non-utility parties – including Simplot/Clearwater - that filed direct testimony three weeks ago strongly urged the Commission not to shorten QF contract lengths from the current 20 years. The IIPA witness Tony Yankel proposed a temporary two year contract length as a "stopgap" in order to allow time to correct errors he identified in the Commission's avoided cost model. The Commission Staff recommends maintaining a 20 year contract length for PURPA projects that currently qualify for SAR-based rates and a maximum five years for QFs subject to the IRP based rates.

In our reply testimony, Simplot/Clearwater recommend a compromise proposal pertaining to PURPA contract length for QFs ineligible for standard rates. We propose that capacity and energy be treated slightly differently within the term of a 20-year contract. We recommend the Commission maintain a 20-year contract length with the capacity component of the rate fixed for the entire 20-year term. However, as a compromise, the energy portion of the rate would only be fixed for the first 10 years of the contract.   After the first 10 years, the energy component would be recalculated each year adhering to the Commission approved method for the remaining term of the contract. Simplot/Clearwater still believe the current 20-year term, for reasons stated in my direct testimony, should be maintained. However, as described below, this alternative proposal addresses some of the concerns of the other parties.

Q. YOU ARE RECOMMENDING THE ENERGY COMPONENT OF THE 20-YEAR CONTRACT BE UPDATED ANNUALLY OVER THE SECOND TEN YEARS. ARE THERE CURRENT PURPA CONTRACTS IN IDAHO THAT THE ENERGY PORTION IS UPDATED ANNUALLY?

A. Yes. There are approximately 25 PURPA contracts that are adjusted periodically based on coal costs. The commission uses the variable costs associated with the operation of Colstrip, a coal-fired generation facility located in southeast Montana, for an annual adjustment of the adjustable portion of avoided costs for those contracts. These projects had their rates set using an older coal SAR methodology. So there is ample precedent for adjusting PURPA contracts on an annual basis.

Q. ARE YOU AWARE OF OTHER PURPA CONTRACTS APPROVED BY THE IDAHO COMMISSION WHERE CAPACITY IS FIXED FOR THE TERM OF THE CONTRACT AND ENERGY IS ADJUSTED PERIODICALLY?

A. There are approximately 43 PURPA contracts tied to Idaho Power's Schedule 89 where the energy rate is adjusted when Net Power Supply Expenses (NPSE) are changed in the Company's base rates. For these projects the capacity component was fixed for the life of the contract, however the utility's variable costs, including fuel and variable operation and maintenance costs, are adjusted when these expenses change in the Company's base rates, most often in a general rate case filing. This approach was intended to minimize potential overpayments and underpayments. The Commission's rational for establishing these contracts was:

> *Idaho Power appears particularly sensitive to fluctuations in avoided energy costs. Allowing energy payments derived from annual estimation of avoided costs may obligate the Company to payments in excess of the actual avoided costs. Conversely, annual estimates of avoided energy costs may also allow the QF too little. Underpayments are likely to occur from this scheme during poor water years or during nearly every year for those facilities whose production coincides with the months of high avoided energy costs. In the long run, a policy based on Idaho Power's estimated avoided costs at delivery time reduces the financial risk to both the utility and the QF.*[1]

If the Companies were filing periodic rate cases or updates to base rates then the energy costs would be adjusted every few years.

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[1] Order No. 15746, Docket No. P-200-12.

Q. YOU STATED ABOVE YOUR ALTERNATIVE PROPOSAL ADDRESSES SOME OF THE CONCERNS OF THE OTHER PARTIES. COULD YOU PLEASE BE MORE SPECIFIC?

A. The majority of the intervenors focused on the inability of a PURPA project to receive financing with shortened contracts on the one hand, and on the other hand the Utilities and Staff focused on the risks ratepayers face from the utilities signing fixed-price long-term contracts. As I explained in my direct testimony, I do not agree with the latter contention of ratepayer risk, however the alternative proposal offered here addresses that issue by adjusting the energy component annually during the second ten years of the contract.

Q. YOU SAID MOST OF THE INTERVENORS ARE CONCERNED ABOUT THE INABILITY OF PURPA PROJECTS TO OBTAIN FINANCING USING SHORT-TERM CONTRACTS. COULD YOU CITE SOME EXAMPLES?

A. Without repeating the logic used by the intervenors, the crux of their positions was made clear in their direct testimony. The shorter the contract length the more difficult it is to obtain financing for a PURPA project. For example, *"The consequence of a Commission order limiting energy sales agreements to two or five years would be to bring any meaningful PURPA development in Idaho to a halt."*[2] The Renewable Energy Coalition witness John Lowe stated, *"In addition, imposing a policy change like a shortened contract term on existing QFs could have significant and unnecessary harm on these projects, the utilities, and ratepayers.*[1] And,

> *This need for long term assurance of capital recovery is the same for QFs as it is for a utility that proposes to build a new power plant and seeks Commission*

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[1]Direct Testimony of Mark Van Gulik, Intermountain Energy Partners, March 23, 2015, IPC-E-15-01, p. 2.

approval for long-term recovery of the plant's costs by including them in rate base. This history suggests that, without long-term, 20-year contracts, QFs will not be developed in Idaho. [3]

The Commission Staff, while recommending five year contracts for IRP method based PURPA contracts, also acknowledged,

Q. But won't a five-year limit on maximum contract length, if approved, limit the ability of projects to obtain financing, thus making extensive project development unlikely?
A. Yes, I agree that development would likely slow considerably, at least under PURPA.[4]

Also Snake River Alliance witness Ken Miller said,

I think this application, if approved, will cause further migration of solar developers away from Idaho, as the proposed reduction in contract terms to two years is tantamount to a freeze on future solar PURPA projects.[5]

Q. DR. READING, I REALIZE YOU ARE AN ECONOMIST NOT A LAWYER, BUT DID ONE OF THE INTERVENORS EXPRESS SOME LEGAL CONCERNS ABOUT SHORTER CONTRACTS FAILING TO MEET FERC'S PURPA REQUIREMENTS?

A. Yes. ICL/Sierra witness Adam Wenner stated in his direct testimony,

In the electric utility industry, and as discussed in my testimony, a two-year term fails to permit a QF to estimate, with reasonable certainty, the expected return on its potential investment in a QF, and would frustrate the requirement of section 210 of PURPA that FERC's rules, as implemented by state commissions, encourage cogeneration and small power production.[6]

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[3] Direct Testimony of R. Thomas Beach, Idaho Conservation League and Sierra Club, March 23, 2015, IPC-E-15-01, p.10.

[4] Direct Testimony of , Rick Sterling, Idaho Public Utilities Commission Staff, March 23, 2015, IPC-E-15-01, p. 8.

[5] Direct Testimony of Ken Miller, Snake River Alliance, March 23, 2015, IPC-E-15-01, p.10.

[6] Direct Testimony of Adam Wernner, Idaho Conservation League and Sierra Club, March 23, 2015, IPC-E-15-01, p.10.

The alternative proposal offered here is aimed at finding a balance among the parties' concerns about a QF's ability to obtain financing, FERC's legal requirements under PURPA and the risks of longer term fixed contracts in an uncertain world.

Q. YOU JUST USED THE TERM "BALANCE" AMONG THE VARIOUS VIEWS OF THE PARTIES. WHY DO YOU BELIEVE YOUR ALTERNATIVE PROPOSAL HELPS ALLEVIATE SOME OF THOSE CONCERNS?

A. The alternative proposal offered here maintains a fixed capacity component of the rate for the full 20-year duration, which more closely matches the fixed capacity length of a utility-built facility. A QF, under current Commission policy, does not receive capacity credits until the utility's IRP shows a capacity deficit, therefore putting a QF resource and a utility built resource on relatively equal footing. The energy component, on the other hand, will be updated annually over the last ten years of the contract, reducing the perceived risk to rate payers from fluctuating fuel costs. Because the contract length would remain at 20 years and have a fixed capacity component, it should give financiers an additional sense of confidence and also addresses FERC's legal requirements. Of course the most important aspect of this compromise is the incorporation of a variable component for energy, the most volatile portion of a utility's avoided cost.

Q. YOU MENTIONED ABOVE YOU WANT TO ADDRESS, IN ADDITION TO YOUR PROPOSED ALTERNATIVE, A SPECIFIC ASPECT OF A PARTY'S DIRECT TESTIMONY. WHAT ASPECT WOULD YOU LIKE TO ADDRESS?

A. Commission Staff witness Rick Sterling stated,

> *Q. Do you believe PURPA is an effective mechanism for utilities to acquire new generation?*

A. No, I do not. I believe PURPA was intended to permit relatively small, non-utility-owned projects to be developed and to compete on an equal footing with utility owned facilities. I do not believe PURPA was ever intended to serve as the primary, or even a major, mechanism for utility acquisition of new resources.[7]

I fundamentally disagree with Mr. Sterling's statement that PURPA was "intended primarily to permit relatively small non-utility-owned projects to be developed." Utilities can, and do, develop PURPA projects. It is true that in the early days, utilities could only own 50% of a PURPA project, but that restriction was repealed ten years ago. PURPA, arising out of the energy crises of 1970's was part of National Energy Act enacted in 1978. The law was aimed at both relatively small renewable energy projects and large projects with <u>no limit as to size</u>. These projects provide electrical energy at a more fuel efficient alternative to traditional fossil fuel utility base load plant.

In addition, it appears at odds with Staff's recommendations in this docket and Staff witness Sterling's statement that PURPA was intended to allow these projects to "be developed and to compete on an equal footing with utility owned facilities." For example, Idaho Power's certificate of public convenience and necessity (CPCN) for Langley Gulch does not expire after five years with capacity rates adjusted to lower ratepayer risk over the depreciated life of the plant. I would expect Idaho Power would have difficulty financing the project with a CPCN that expired after five years.

One of the concepts behind the creation of PURPA is that the market (a.k.a developers) could provide electric power at prices that are competitive with regulated utilities' resources. This has been proven to be true as I demonstrated in my direct

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[7] Direct Testimony of , Rick Sterling, Idaho Public Utilities Commission Staff, March 23, 2015, IPC-E-15-01, p. 24.

testimony. In addition as these facilities are added to a utility's resource stack, they delay or eliminate less fuel efficient future utility-built generation plant. PURPA therefore is indifferent to who provides the generation of electric power, the utility or a non-utility generator, only the avoided cost of providing the power should be the determining factor.

Q. DO YOU AGREE WITH MR. STERLING'S STATEMENT ON PAGES 20 – 21 THAT "AVOIDED COST RATES HAVE EXCEEDED COMPARABLE MARKET PRICES THROUGHOUT MOST OF THE HISTORY OF PURPA IN IDAHO"?

A. No I do not. As I pointed out in my direct testimony comparing long-term avoided cost estimates with current market prices is, from an economist's point of view, inappropriate and misleading. Long-term marginal cost rates (avoided cost rates) are not the same as short-term market prices. When this Commission approved the Langley Gulch plant for inclusion in Idaho Power's rates, it did so using long-term cost estimates over the expected life of the plant. Had the Commission used current market prices as the benchmark, that plant would probably not have been built.

Q. WHAT ARE YOUR RECOMMENDATIONS FOR THE COMMISSION?

A. While still maintaining the recommendation put forth in my direct testimony Simplot/Clearwater are offering an alternative proposal should the Commission decide alter the length of PURPA contracts. The alternative recommendation is that capacity and energy be treated differently within the term of a 20-year contract. Capacity would remain fixed, however the energy component would be recalculated each year beginning in the 11^{th} year for the remaining 10 years of the contract.

DOES THIS END YOUR TESTIMONY AS OF MAY 14, 2015? A. Yes

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 14th day of May, 2015, a true and correct copy of the within and foregoing REPLY TESTIMONY OF DR. DON READING ON BEHALF OF CLEARWATER PAPER CORPORATION and the J.R. SIMPLOT COMPANY was served as shown to:

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