DECISION MEMORANDUM

TO: COMMISSIONER REDFORD
COMMISSIONER SMITH
COMMISSIONER KEMPTON
COMMISSION SECRETARY
COMMISSION STAFF
LEGAL

FROM: NEIL PRICE
DEPUTY ATTORNEY GENERAL

DATE: FEBRUARY 20, 2009

SUBJECT: IDAHO POWER COMPANY'S APPLICATION FOR APPROVAL OF A SPECIAL CONTRACT TO SUPPLY ELECTRICAL POWER TO HOKU MATERIALS, INC.; CASE NO. IPC-E-08-21

On October 24, 2008, Idaho Power Company ("Idaho Power" or "Company") filed an Application with the Commission seeking approval of a special contract to supply electrical power to Hoku Materials, Inc. ("Hoku"). On November 6, 2008, Staff submitted production requests to the Company and Idaho Power submitted written responses to those requests on November 28, 2008.

On December 3, 2008, the Commission issued a Notice of Application and Notice of Modified Procedure and established a 60-day open comment period. Order No. 30697. Commission Staff, Idaho Irrigation Pumpers Association, Inc. ("IIPA") and an individual Idaho Power customer all filed written comments within the established comment period.

THE AGREEMENT

The Energy Sales Agreement ("ESA") entered into between Idaho Power and Hoku dictates that Idaho Power will sell and Hoku will purchase in excess of 25,000 kW. Application at 2. The parties have entered into a special contractual arrangement that comports with the requirements outlined in Commission Tariff No. 101. *Id.* Idaho Power has also agreed to construct, at Hoku's expense, certain interconnection facilities necessary to enable delivery of electrical service to Hoku's facilities. *Id.*

The effective date of the ESA begins on June 1, 2009 and concludes on May 31, 2013. *Id.* at 3. Under the terms of the special contract, either party can terminate the ESA by issuing prior written notice to the other party within one year of the effective termination date. *Id.* The Application stipulates that if the effective termination date occurs prior to the implementation of a subsequent ESA between the parties then Hoku's energy and demand rates will be equivalent to the Company's Schedule 19-T rates until a replacement contract is approved by the Commission. *Id.*

Under the ESA, Hoku's demand will vary during the summer and non-summer seasons. *Id.* Hoku's peak demand during the term of the ESA will not exceed 82 MW. *Id.* The parties have agreed that Hoku's scheduled load demand for the summer of 2012 is contingent upon Idaho Power's ability to integrate "major transmission and generation projects" into its system. *Id.*

The parties have agreed to divide Hoku's demand and energy requirements into "two blocks for pricing purposes." *Id.* at 4. The first block is equivalent to the Company's "current Commission-approved avoided cost rates." *Id.* Any change to the avoided cost rate during the term of the Agreement will not affect the first block energy rate contained in the Agreement. *Id.* The second block rates, 25 MW or more, are consistent with the Company's approved Schedule 19-T rates. *Id.*

Hoku is required to "take-or-pay" a certain amount of energy from Idaho Power every month but it is also allowed to "request a release of all or part of its first block energy purchase commitment." *Id.* Idaho Power states that it will "make a commercially reasonable effort to absorb or resell the released energy and provide a credit to Hoku." *Id.* The amount credited will depend upon the rate period during which the Company receives timely notice of Hoku's request to release its energy demands as well as the Company's ability to "manage and supply commitments to serve Hoku's load." *Id.*

In addition, if Hoku wishes to procure additional power during the summer rate period then Idaho Power is obligated to make the same "commercially reasonable efforts to obtain proposals to supply Hoku's additional energy request." *Id.* at 5. Hoku will be responsible for the costs of these "purchases and any associated transmission and ancillary service expense to transport such purchase to the Hoku Facility." *Id.* Hoku's ability to expand its first block up to 175,000 kWs hinges upon the Company's ability to supply and deliver additional power. *Id.*

Idaho Power's Application states that it is seeking an effective date of June 1, 2009 to coincide with the effective date of the parties' ESA. *Id.* The Application asks that the first block revenues and expenses be treated similarly to wholesale purchases and sales and thus not be included under the Company's yearly PCA. *Id.* Finally, the Application states that the ESA will only become effective if all of its "terms and provisions" are approved by the Commission "without change or condition." *Id.*

In support of its Application, the Company submitted testimony from Ric Gale, Vice President of Regulatory Affairs. Mr. Gale's testimony explains, in greater detail, the Company's rationale for the specific elements of its ESA with Hoku.

IIPA COMMENTS

IIPA's comments focused primarily on the "large rate of growth on the Idaho Power system" and what the group characterizes as the "unfair shifting of marginal cost associated with this growth" to customer groups like the IIPA. IIPA Comments at 1-2. IIPA supports the proposed ESA between Idaho Power and Hoku and lauds the Company's "efforts to mitigate the rate impact to existing customers of the marginal costs of adding new load." *Id.* at 4.

INDIVIDUAL COMMENTS

On January 11, 2009, the Commission received an e-mail from a resident of Boise, Idaho. This individual expressed generalized support for the contract and what he viewed as "out of the box solutions to energy supply and demand."

STAFF COMMENTS

Staff noted that the "first block energy pricing is critical because, at the rates contained in the Agreement, first block energy charges comprise over 77 percent of the total value of the contract." Staff Comments at 3. The first block energy price is tied to the PURPA avoided cost rate for a levelized four-year contract with a 2009 online date – currently $61.66 per MWh. The parties chose this pricing method in lieu of a market-based approach because it would afford Hoku the certainty associated with a fixed price during the life of the contract. Staff believes that "avoided cost rates are a reasonable proxy for establishing a rate to be paid by new customers who place large loads on the utility's system. . . ." *Id.* Staff also believes that it is reasonable for Hoku's second block, equal to 25 MW, to be priced commensurate with Idaho Power's current Schedule 19-T rate. Staff reasoned that "Hoku should be entitled to the benefit of embedded rates for at least some part of its load. . . ." *Id.* at 4.

In its quest to evaluate the reasonableness of the contract rates, Staff asked the Company "to use AURORA to compute marginal energy prices for a four-year future period assuming an addition of load equal to Hoku's expected load." *Id.* The results of the statistical modeling revealed that the overall average price of the combined blocks was lower than the marginal energy cost estimated by AURORA, $52.69 and $55.94, respectively. *Id.*

Staff also considered the transition of Hoku's first block energy rate from "marginal cost-based rates . . . to embedded cost-based rates at the end of the four-year contract term." *Id.* at 5. Staff supports the four-year transition period to an embedded rate for Hoku's entire load embodied in the parties' Agreement because, *inter alia*, it allows Idaho Power adequate time to incorporate the new load into its next Integrated Resource Plan and will likely allow "for at least one or two rate cases to be processed with Hoku as a customer." *Id.* at 6.

According to Staff, immediately charging an embedded rate for such a large single new load would likely place enough "upward pressure . . . on rates to cause Idaho Power to seek an increase in all customers' rates through a general rate case." *Id.* at 5. In Staff's opinion, existing customers should not have to bear the burden of a rate increase "just because of a single large new customer." *Id.* However, charging Hoku a marginal cost-based rate forever would be "equally unreasonable" because it would unfairly deprive Hoku "the benefit of lower embedded rates that all other customers . . . enjoy." *Id.* at 5-6.

Staff agrees with the Company's proposal to "treat first block revenues and expenses as if they were wholesale purchases and sales" and the second block as retail load. *Id.* at 6. According to Staff, Idaho Power's proposed ratemaking treatment is similar to the authorized ratemaking approach for a former special contract customer, FMC, served under a similar two-block (embedded and market) rate structure. *Id.* Finally, Staff believes that the remaining terms and conditions governing Hoku's ability to either opt out of its first block energy requirements or request additional power are reasonable. *Id.* at 7.

Staff has reviewed the Company's Application and recommends that the Commission approve the ESA between Idaho Power and Hoku. *Id.* Further, Staff recommends that any future amendments to the ESA as well as "any decision to supply more than 82 MW to Hoku be subject to Commission approval." *Id.*

COMMISSION DECISION

Does the Commission wish to approve Idaho Power's Application for Approval of its Special Energy Sales Agreement with Hoku?

Neil Price
Deputy Attorney General

M:IPC-E-08-21_np2