**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UM 1610 (PHASE II)

In the Matter of PUBLIC UTILITY COMMISSION OF OREGON Investigation into Qualifying Facility Contracting and Pricing.	JOINT POST-HEARING BRIEF OF THE RENEWABLE ENERGY COALITION, COMMUNITY RENEWABLE ENERGY ASSOCIATION, OBSIDIAN RENEWABLES LLC, AND ONEENERGY, LLC

I. INTRODUCTION

One of the issues in Phase II of this UM 1610 proceeding is whether the Commission should revise its methodology for calculating avoided cost rates paid to qualifying facilities ("QFs") during periods in which the purchasing utility is resource sufficient. More than a decade ago, the Commission determined in Order 05-584 that it is appropriate to set avoided cost rates during sufficiency periods based on the purchasing utility's forecast of market prices. The Commission determined that market prices adequately compensated the QF for both energy and capacity. But a lot has changed over the past ten years.

The Renewable Energy Coalition, Community Renewable Energy Association, Obsidian Renewables, and OneEnergy (collectively the "Joint QF Parties") respectfully submit this Post-Hearing Brief to respond to the arguments made by the purchasing utilities on this issue.[1] The thrust of the purchasing utilities' arguments is that the Commission, having previously decided this issue way back in 2005, should therefore not decide the issue again.

[1] By focusing this Post-Hearing Brief on the issue addressed herein, more of the Joint QF Parties intend to waive their rights on arguments with respect to any other issues in this proceeding.

As this Commission has noted numerous times, its prior policy decisions are not immutable and the Commission can and will revisit prior decisions when the circumstances warrant. The Joint QF Parties submit that the following market changes that have occurred since 2005 warrant revisiting the issue:

- Since 2005, new environmental regulations—particularly those applicable to coal—create a new opportunity for valuing capacity.
- Since 2005, the wholesale power markets in the Pacific Northwest have been flooded with thousands of megawatts of wind generation that skew the prevailing market prices by operating in otherwise uneconomic market conditions in order to collect production tax credits ("PTCs").
- As compared to 2005, the purchasing utilities' projected periods of resource sufficiency are substantially longer. Market purchases are no longer being used to "bridge the gap" until the next resource acquisition, and they are being used *in lieu of* the next resource acquisition.

Based on these and other fundamental market changes that have occurred since 2005, the Joint QF Parties submit that it is appropriate for the Commission to revisit this issue of whether market prices still adequately compensate QFs for capacity.

II. DISCUSSION

The purchasing utilities universally oppose the Joint QF Parties' arguments for revising sufficiency period capacity rates based on the conclusory statement that the issue was previously decided by the Commission in 2005. For example, PacifiCorp writes "Order 05-584 makes clear that the Commission carefully considered whether market prices sufficient compensate QFs for capacity during times of resource sufficiency. It appropriately concluded that they do." According to PacifiCorp, therefore, because the Commission already addressed this issue more than ten years ago, the Commission should not revisit the issue now.

This position stands in stark contrast to PacifiCorp's petition in UM 1734 in which it asked the Commission to upend decisions that it made in this very docket only one year prior. PacifiCorp wrote that it "recognizes that the Commission affirmed the 10

MW eligibility cap in Order No. 14-058 in Phase I of docket UM 1610. PacifiCorp also acknowledges that the Commission did not revisit the 15-year fixed price term, which was briefed by the parties, in Phase I of UM 1610."[2] Nevertheless, PacifiCorp asked the Commission to revise both the eligibility cap and contract term based on an alleged change in circumstances.

Several interveners in UM 1734 vigorously asserted the same position on which the purchasing utilities now rely. The interveners' motion to dismiss PacifiCorp's petition was rebuffed by the Commission:

> We deny the motion to dismiss. Because this Commission acts in a legislative capacity when it establishes general policies to implement PURPA, we are not precluded from revisiting those policies when the conditions under which they were adopted may have changed. To the contrary, we have a duty to reexamine all PURPA policies, when necessary, to promote QF development while also ensuring that ratepayers pay no more than a utility's avoided costs. Indeed, since 2005, we have conducted three multi-phase proceedings to revamp, clarify, and refine our QF policies to address changing market conditions.[3]

By the Commission's own reasoning in UM 1734, therefore, its decision concerning sufficiency period rates in Order 05-584 is not sacrosanct. Indeed, the Commission recognized there have been "changing market conditions" since 2005. The Commission therefore has a "duty to reexamine all PURPA policies," including whether current market energy prices fully compensate QFs for capacity.

a. New environmental compliance costs create new ways to measure the value of existing capacity.

In its Order 05-584, the Commission decided to base sufficiency period rates on projections of energy market prices only because there were no better alternatives at the time. The Commission acknowledged, for example, that it would be preferable to rely on capacity market prices if viable capacity markets existed. The Commission explained

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[2] http://edocs.puc.state.or.us/efdocs/HAA/haa162242.pdf

[3] http://apps.puc.state.or.us/orders/2015ords/15-209.pdf

that "[a]lthough valuation of QF capacity based on the market price of capacity itself has significant appeal, we are concerned about inconsistent evidence regarding the viability of the market for capacity." The Commission left the door open for alternative methods that would better value capacity than market purchases. "To the extent that a party can provide evidence regarding the market pricing of capacity, however, we remain open to reconsideration of this decision in the next phase of this proceeding."

The Joint QF Parties have submitted extensive testimony in this proceeding showing that, since 2005, environmental regulations have created different alternatives for valuing generating capacity. Specifically, even while it is "resource sufficient," PacifiCorp is planning on making a series of significant investments in environmental upgrades to retain its coal generating capacity. Joint QF Parties/100; Higgins/5. These are not hypothetical costs for environmental externalities; these are planned investments on existing capacity. As a practical matter, this means that PacifiCorp's ratepayers do not just have to pay for incremental increases in capacity, they have to pay to retain the capacity of existing generating units. In review of the Joint QF Parties' proposal, the Oregon Department of Energy ("ODOE") concluded: "Without endorsing the particular values used in Higgins' calculations, the reasoning seems sound." ODOE/900; Carver/8.

In response to the Joint QF Parties' testimony, Staff incorrectly suggests that the proposal is to monetize PacifiCorp's future Section 111(d) risk.[4] Mr. Higgins' proposal relies on actual, planned capacity investments that will occur due to *existing* environmental regulations. Joint QF Parties/200, Higgins/8. The proposal includes only "real costs" that are currently planned. *Id.* at 7-8. That EPA's newly promulgated Section 111(d) rules are likely to impose *additional* environmental costs on PacifiCorp makes the Joint QF Parties' proposal conservative because it does not include those *additional* costs.

[4] *Staff's Prehearing Brief* at 27.

Staff ultimately found that capacity retention costs are "real costs."[5] In Joint QF Parties Exhibit 300, Staff agrees that "PacifiCorp's prudent investments in environmental upgrades have been and will likely continue to be included in rate base to enable the Company to earn a return on and of these investments."[6] Staff's witness, Ms. Brittany Andrus, also indicated that all of the environmental upgrades used in calculation of the Joint QF Parties' proposal would be "real costs" to PacifiCorp.[7] These are "real costs" for purposes of calculating avoided cost rates and the Joint QF Parties' proposal does not therefore include an "environmental adder" to the avoided costs.

The Joint QF Parties' proposal is that PacifiCorp's capacity retention costs are a viable indicator of how the company values capacity in 2015. If PacifiCorp could acquire incremental capacity cheaper than the cost of retaining its existing capacity, it would do so. Thus, the amount of compensation paid to QFs for capacity should be no less than the amount that PacifiCorp's ratepayers would have to pay to retain the existing coal capacity. The Joint QF Parties' intent in providing this testimony is to demonstrate that there are transparent, objective and sound methods for valuing capacity other than relying on the purchasing utility's own self-serving forecast of market purchase prices.

b. Energy markets are now diluted by uneconomic generation.

Commission's decision in Order 05-584 also contains a fundamental assumption about rational market behavior that no longer holds true. The Commission found that it would be reasonable—albeit not preferable—to derive sufficiency period avoided costs from forward market price forecasts. In reaching this decision, the Commission stated that "this approach embeds the value of incremental QF capacity in the total market-based avoided cost rates." This statement, which goes without further explanation or support, was probably derived from the assumption that a rational market seller would

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[5] *Id.* at 28.

[6] Joint QF Parties/300, Hearing Exhibit 1 (quoting Joint QF Parties/200, Higgins/6:1-2).

[7] Joint QF Parties/300, Hearing Exhibit/2.

not offer to sell power for a price that did not capture some or all of the capacity costs of its generation. In other words, it would be irrational for a seller to sell power at or below its operating costs. The premium above the operating costs demanded by a rational seller would reflect the "capacity value" of the generating resource.

It is no longer reasonable to conclude that capacity value is embedded in market-based rates. Between 2005 and 2015 the wholesale energy markets in the Pacific Northwest have been flooded with thousands of MWs of new wind projects. Installed wind capacity has increased by an order of magnitude over the past ten (10) years. By way of illustration, there is now as much installed wind generation in the Pacific Northwest as the output of the entire Federal Columbia River Power System.

What is peculiar about the wind generation, from a market standpoint, is that it derives significant economic value from the PTC. The PTC is only paid when the project is actually producing electricity. Thus, unlike other resource types such as hydroelectricity and natural gas that were more prevalent in 2005 wholesale markets, a wind project has an incentive to produce electricity even when market prices are *below* its incremental operating costs so that it can collect the PTC. In such case, the capacity value of the generating resource may be reflected in the PTC rather than the market purchase price. The net effect of this behavior is a dilution of market prices through an almost ubiquitous surplus of wind power. In other words, the 2015 wholesale energy markets are sending and responding to different economic signals than they did in 2005. At the very least, this massive proliferation of surplus wind generation warrants the Commission revisiting the assumption that capacity value is embedded in forward market prices.

c. Resource sufficiency is now the rule rather than the exception.

Another very significant change in circumstances since 2005 is that purchasing utilities are now extending their resource sufficiency periods to an exaggerated degree.

In Order 05-584, the Commission's determination was based at least in part on its view that utilities would use market purchases only as a stop-gap measure. The Commission explained that "[w]e find this valuation mechanism to be appropriate given the likelihood that a utility will address probable gaps between increasing demand and actual resources, in the absence of incremental QF capacity, with purchases of energy and capacity on the market." In other words, back in 2005 the Commission presumed that any resource sufficiency period would be short-lived. The Commission selected market energy prices as a substitute for market capacity prices because it anticipated that such market-based rates would only be paid on an interim basis to fill the "gaps" between increased load and new generation.

Changes in market conditions over the past 10 years have flipped on its head any presumption that resource deficient avoided cost rates would be predominant. For example, when the Commission issued its decision in Order 05-584, PacifiCorp's resource sufficiency period was only expected to last for a year or two. PacifiCorp's 2004 resource acquisition action plan anticipated signing a contract to acquire a new generating resource within one or two years.[8] Now, however, PacifiCorp's Schedule 37 rates project a resource sufficiency period of at least nine (9) years. Under current circumstances, the QF is receiving forecasted market prices for the vast majority of the QF fixed-price contact term. This change in circumstances is inconsistent with the Commission's intent in Order 05-584, and highlights the importance of revisiting the Commission's compromise on capacity value.

III. CONCLUSION

At issue here is a policy decision made by the Commission more than 10 years ago based on then-existing market conditions. The Commission concluded that

[8] http://www.pacificorp.com/content/dam/pacificorp/doc/Energy_Sources/Integrated_Resource_Plan/2004IRP/2004IRP_Vol1_1-20-05.pdf

calculating avoided cost rates based on forecasts of market prices would adequately compensate QFs for capacity. The Commission reached this decision not because it was the best methodology for valuing capacity, but because it lacked sufficient information about actual capacity prices. The Commission also reached this conclusion based on a number of assumptions about prevailing market conditions in 2005. The purchasing utilities would, of course, be delighted for the Commission to continue this policy because it means paying artificially low market prices for energy and capacity for the foreseeable future.

The Joint QF Parties submit that it is time for the Commission to revisit this policy decision. As the Commission noted in UM 1734, the Commission has a duty to revisit prior policy decision when there has been a change in circumstances. The Commission has also recognized that there have been a number of changed circumstances since 2005. As the Joint QF Parties point out, these changes include: (i) new environmental compliance costs offer different ways to value capacity; (ii) the explosion of PTC-seeking wind generation in the Pacific Northwest undermines the assumption that capacity value is embedded in prevailing energy market prices; and (iii) the dramatic extension of resource sufficiency periods from a short-term condition to the default position for long-term resource planning.

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The Joint QF Parties respectfully submit that the Commission's decade-old decision in Order 05-584 no longer adequately compensates QFs for capacity during resource sufficiency periods.

Respectfully submitted, this 13th day of October, 2015.

RICHARDSON ADAMS, PLLC

/s/Gregory M. Adams
Gregory M. Adams, OSB No. 101779
515 N. 27th Street
Boise, ID 83702
Telephone: (208) 938-2236
greg@richardsonadams.com

Of Attorneys for the Community Renewable Energy Association

CABLE HUSTON LLP

/s/Richard G. Lorenz
Richard G. Lorenz, OSB No. 003086
1001 SW Fifth Ave., Suite 2000
Portland, OR 97204-1136
Telephone: (503) 224-3092
rlorenz@cablehuston.com

Of Attorneys for
Obsidian Renewables LLC

LOVINGER KAUFMANN LLP

/s/Kenneth E. Kaufmann
Kenneth E. Kaufmann, OSB No. 982672
825 NE Multnomah, Suite 925
Portland, OR 97232-2150
Telephone: (503) 595-1867
kaufmann@LKlaw.com

Of Attorneys for OneEnergy, Inc.

SANGER LAW PC

/s/Irion A. Sanger
Irion A Sanger, OSB No. 003750
1117 SE 53rd Avenue
Portland, OR 97215
Telephone: (503) 756-7533
irion@sanger-law.com

Of Attorneys for the Renewable Energy Coalition