

ORDER NO. 13 132

ENTERED: APR 11 2013

**BEFORE THE PUBLIC UTILITY COMMISSION
OF OREGON**

UE 233

In the Matter of

IDAHO POWER COMPANY,

Request for General Rate Revision.

ORDER

**DISPOSITION: RECOVERY FOR COAL PLANT INVESTMENT
ALLOWED; MANAGEMENT DISALLOWANCE
IMPOSED**

I. INTRODUCTION

In Order No. 12-055, we adopted a stipulation resolving all but two issues regarding Idaho Power Company's 2011 application for a general rate revision. In this order, we resolve one of the two remaining issues: Idaho Power's request for rate recovery for its investment in environmental upgrades to Unit 3 of the Jim Bridger Station generating facility (Bridger 3). Although we find that the decision to invest in the upgrades was prudent, we conclude that Idaho Power's management oversight of the investment was deficient, and we accordingly impose a one-time utility management expense disallowance. We will address the second issue, regarding Idaho Power's tax benefit, in dockets UM 1562 and UM 1582.

II. PROCEDURAL HISTORY

Idaho Power filed an application for a general rate revision on July 29, 2011, seeking to revise its rates and charges for electric service in Oregon. The Citizens' Utility Board of Oregon (CUB), the Industrial Customers of Idaho Power (OICIP), and the Oregon Irrigation Pumpers Association (OIPA) intervened in the proceedings and, along with Commission Staff, filed opening testimony on December 7, 2011. After a number of settlement conferences, the parties resolved all but two contested issues. On February 1, 2012, the parties filed a partial stipulation, supported by joint testimony. On February 23, 2012, we issued Order 12-055, adopting the parties' partial stipulation and approving Idaho Power's general rate revision as revised by the terms of the partial stipulation.

The two remaining issues left unresolved by the partial stipulation are (1) the treatment of two one-time tax benefits Idaho Power received from changes in tax methodologies, and (2) the recovery of Idaho Power's investment in Bridger 3 pollution control equipment. To examine the first issue, the treatment of Idaho Power's tax benefits, we opened

dockets UM 1562 and UM 1582. To address the second issue, we initiated Phase II of this docket.

Idaho Power filed supplemental testimony regarding Bridger 3 on February 1, 2012. Staff, CUB, and Idaho Power filed two subsequent rounds of testimony. The parties waived a hearing, and filed briefs in October and December 2012. Finally, we held oral argument on January 29, 2013.

II. DISCUSSION

A. Background

Jim Bridger Unit 3 is one of four pulverized coal units making up the Jim Bridger Station generating facility, located in Wyoming. Bridger 3 is co-owned by Idaho Power and Pacific Power, and is operated by Pacific Power. Idaho Power has a 33.3 percent share in the unit.

In 2008, Idaho Power and Pacific Power determined that upgrades were needed to the existing scrubbers for Bridger 3 in order to improve removal of sulfur dioxide (SO₂) from plant emissions. In 2008, Pacific Power issued a request for proposals to complete the project, and in December 2008, entered into a contract for the upgrade.

In 2011, Pacific Power and Idaho Power initiated work upgrading the existing scrubbers to reduce emissions to an estimated rate of 0.10 lb/MMBtu. The work was completed in the spring of 2011, and Idaho Power's share of the capital investment in the project is \$8.2 million. The Oregon portion of the investment is approximately \$400,000, which equates to a \$27,500 annual revenue requirement for Idaho Power's Oregon operations.

In Order No. 12-055, we adopted the parties' proposal that the stipulated rates include the Bridger 3 investments as filed, with Idaho Power deferring the variance of the amount, and refunding to customers through its Power Cost Adjustment (PCA) true-up balancing account any money collected from customers for any investment we determined to be imprudent.

B. Procedural Issues

We address in this order only the prudence of the specific environmental upgrades at issue for Bridger 3. We do not address the prudence of any future investments for which Idaho Power may seek recovery in future rate proceedings. We will address requests for recovery of other investments as they are introduced.

Idaho Power, Staff, and CUB filed requests that the Commission take official notice of a number of documents. No party objected to the requests for official notice.¹ We grant the parties' requests.

¹ CUB initially objected to Idaho Power's motion for official notice, but later withdrew its objection.

C. Parties' Positions

1. Idaho Power

Idaho Power argues that its investment in Bridger 3 was prudent and beneficial to ratepayers, and that it properly reviewed Pacific Power's investment actions. While acknowledging that it did not review all documents underlying Pacific Power's analysis of the Bridger 3 upgrade, Idaho Power nevertheless argues that it did what it was required to do under the parties' operating agreement and that the investment was one that a reasonable utility would have made in Idaho Power's circumstances.

Idaho Power first states that under the operating agreement between Idaho Power and Pacific Power, Pacific Power is the designated plant operator for the Jim Bridger plant, and as such is responsible for the day-to-day activities that are required to ensure the continued operation of the plant. These activities include scope and scheduling of plant outages, planning for and undertaking routine maintenance, coordinating and overseeing capital projects, and environmental compliance strategies. Idaho Power notes the operating agreement "also specifically provides that [Pacific Power] is responsible for ensuring that the plant is run in a prudent and skillful manner consistent with prevailing utility industry standards and in accordance with all applicable laws and regulations, including all relevant environmental regulations."²

Idaho Power adds that Pacific Power is an expert in the operation of coal plants, and that while Pacific Power is governed by the same regulatory requirements as Idaho Power, as a majority owner, Pacific Power has even more at stake than Idaho Power in operating the resource prudently. Idaho Power states that it oversees and reviews all major decisions made by Pacific Power in the operation of the plant, meets with Pacific Power personnel regularly to discuss Bridger 3 operations, and performs audits at the plant and corporate level. Idaho Power argues that if both Idaho Power and Pacific Power had independent responsibility to oversee the plant, costs to run Bridger 3 would be considerably higher.

Idaho Power next argues the investment in scrubber upgrades was required to comply with existing environmental regulations, construction and operating permits, and state implementation plans. Idaho Power states a consensus was reached between Pacific Power and the state of Wyoming to develop a plan to achieve required environmental milestones, and it was determined that each of the four Bridger units would need to meet an SO₂ emission limit of 0.15 lb/MMBtu, considered presumptive "best available retrofit technology," or BART, by the Environmental Protection Agency (EPA) in the EPA's Regional Haze Rules. Idaho Power states Pacific Power completed detailed analyses of the appropriate technology to be applied to Jim Bridger to achieve established emissions control objections, and that the upgrade was a cost-effective method to bring Bridger 3 into compliance with environmental regulations, as well as being required by permits. Idaho Power cites to a study prepared by CH2M HILL that prepared a BART analysis for

² Idaho Power/1500, Carstensen/2 (Jul 19, 2012).

Bridger 3, and notes that its \$8.2 million investment in Bridger 3 scrubber upgrades was consistent with the recommendations reached in the CH2M HILL reports, as well as the permit issued in December 2009 by the Wyoming Division of Air Quality.

Finally, Idaho Power argues the economics of the scrubber upgrade project demonstrate that the investment was prudent: Bridger 3 was among the company's lowest cost resources even with the upgrades, and Pacific Power's Present Value Revenue Requirement Differential (PVRR(d)) analysis showed by a wide margin that it was beneficial to customers to invest in emissions control equipment. Further, Idaho Power argues its flexibility in analyzing compliance options was limited because it owns only a partial stake in one coal plant, rather than a fleet of plants. Idaho Power argues the decision to move forward with upgrades was a reasonable response to the possibility of external environmental costs.

2. Staff

After reviewing the applicable regulatory requirements, Staff finds that the investment to upgrade SO₂ capture from Bridger 3 emissions was required for the unit to continue operation until 2018, and appears to have been the most cost-effective alternative for compliance. Staff further finds that the scrubber upgrade will support compliance with post-2018 Regional Haze Rule requirements, and with other regulatory requirements. Staff also notes that not only did Pacific Power's 2008 CAI Capital Projects Study PVRR(d) analysis show a strong economic benefit for upgrading Bridger 3 rather than idling it in 2008, Pacific Power's subsequent updated analysis in its 2011 IRP showed that the economic benefit remained strongly positive even with updated price curves and a later idling date.

Staff finds, however, several infirmities in Idaho Power's decision-making process with regard to the investment, including failure to be aware of Pacific Power's 2008 CAI PVRR(d) analysis, failure to re-evaluate the decision to invest as significant milestones were reached, and failure to include, at the time of its decision, sensitivity cases for variations in fuel, electricity, and CO₂ regulatory cost. Staff argues that Idaho Power's lack of awareness of Pacific Power's PVRR(d) analysis at the time that it was reviewing the decision to upgrade Bridger 3 did not meet the standard of what a utility would do to inform a reasonable decision, because it was unaware of the key life-cycle economic study justifying its decision. Staff also faults Idaho Power for failing to re-evaluate its investment decision as significant milestones were reached, because the first documented update to the initial 2008 analysis occurred in 2011, when the scrubber upgrade project was nearly complete.

Staff concludes that while there were infirmities in Idaho Power's decision-making process, correcting for those infirmities would not have changed a reasonable utility's decision to proceed with the investment, because the investment was so strongly beneficial to customers.

3. CUB

CUB argues that Idaho Power was imprudent for several reasons. First, CUB argues Idaho Power delegated both its management of Bridger 3 and its defense of the unit upgrades to Pacific Power. CUB maintains that Idaho Power has an independent duty to meet the Commission's burden of proof, and that instead Idaho Power ties its case to Pacific Power's plant operation and decision-making. CUB states the record in this case shows Idaho Power's lack of involvement in the contemporaneous decision-making regarding whether and how to upgrade Bridger 3. CUB notes that Idaho Power was unaware of Pacific Power's PVRR(d) analysis—the only analysis that evaluated the cost-effectiveness of the investment in Bridger 3 before the investment was made—until 2012, four years after the analysis was conducted. CUB also notes Idaho Power's lack of familiarity with the details of the investment, including the dates of the competitive bidding process related to the upgrade, when the work on the project began, or the dates of the planned outage during which the upgrade was completed.

Second, CUB argues the analysis supporting the upgrades to Bridger 3 was inadequate. CUB first cites to the tipping point analysis (TPA) relied on by Idaho Power in its testimony, which considered both the Bridger and Valmy plants rather than examining just Bridger. CUB notes that Pacific Power's 2012 IRP Update demonstrates Bridger is on the line between continuing operation and converting to natural gas. CUB argues that there are several serious flaws with the PVRR(d) analysis Idaho Power relies on to demonstrate the prudence of the upgrades to Bridger 3, primarily a flawed alternative closure date, failure to update the analysis when electricity prices changed, and failure to consider alternatives to plant closure such as conversion to gas.

CUB further states Idaho Power and Pacific Power should have conducted a Boardman-style analysis that considered early plant closure as an option for meeting pollution control requirements. CUB notes that Idaho Power, as co-owner of the Boardman coal plant operated by Portland General Electric Company (PGE), should have been aware of PGE's BART analysis for the Boardman plant, which included early shut-down as a way to reduce the costs of pollution control.

Finally, CUB argues the scrubber upgrade investment is not used and useful without additional investments in a selective catalytic reduction (SCR), and that a proper analysis considers all investments required to make a plant used and useful, rather than reviewing each investment separately.

CUB urges us to deny rate recovery for the scrubber upgrade at Bridger 3, and to order Idaho Power to return the deferred costs to customers. In the alternative, CUB suggests we find that the scrubber upgrade will not be used and useful without the addition of the SCR, and deny rate recovery until the investment is found to be used and useful.

D. Resolution

In this order, we address two questions: the prudence of Idaho Power's investment in environmental upgrades to Bridger 3 and the reasonableness of Idaho Power's conduct and decision-making as a minority shareholder.

In docket UE 246, we addressed the prudence of Pacific Power's investment in a series of upgrades to its coal fleet, including the upgrade to Bridger 3 at issue in this docket. We found that, while a reasonable utility faced with emerging state and federal regulations would take at least some action to comply with those rules, Pacific Power's actions caused harm to ratepayers, for two reasons. First, we found Pacific Power failed to explore alternative courses of action, both in terms of the mix of compliance actions and, particularly, in the timing of those actions, that would have allowed Pacific Power to meet its air quality requirements at a lower cost and risk to Oregon ratepayers. Second, we found that Pacific Power's failure to perform appropriate analyses to determine the cost-effectiveness of its investments was imprudent.³ For those same reasons, and because Pacific Power's upgrades and analyses were conducted on a fleet-wide basis, we were unable to quantify, with any precision, the amount of harm caused to ratepayers by Pacific Power's actions. As a result, we chose to impose a one-time 10 percent disallowance to the investments associated with Pacific Power's rate base.⁴

With regard to the prudence of Idaho Power's investment in Bridger 3, we find that both the contemporaneous and updated analyses of the cost-effectiveness of the Bridger 3 investment were inadequate. As in docket UE 246, the analysis supporting Bridger 3 was overly narrow and failed to consider the breadth of input assumptions and updates that we expect when a utility makes a significant resource decision. Nevertheless, in this instance, we cannot conclude that an alternative course of action would have been lower cost or lower risk to Oregon customers. Unlike our review in docket UE 246, which covered a fleet-wide investment in a number of plants, both the contemporaneous and the updated analyses for Bridger 3 showed benefits of such magnitude for the investment, as compared to a shutdown, that we cannot conclude that Idaho Power's actions caused harm to Oregon ratepayers. Even with more rigorous analyses, the investment would have still been the economic choice. We find that the investment in Bridger 3 was prudent.

With regard to Idaho Power's position as a minority owner of Bridger 3, we reject the argument that the minority shareholder agreement shields Idaho Power from all liability for decision-making affecting the rates of its customers. A minority owner who seeks to pass through to its ratepayers the costs of environmental upgrades may not sign away its independent duty to review and carefully consider a majority owner's decision-making. While a minority owner is not required to conduct independent studies that duplicate the work of the majority shareholder, in this case Idaho Power admits it was unaware of the

³ See Docket UE 246, In the Matter of PacifiCorp, dba Pacific Power, Request for a General Rate Revision, Order 12-493 at 27-31 (Dec 20, 2012).

⁴ *Id.* at 32.

existence of the key study underlying the decision to upgrade Bridger 3. This level of oversight is inadequate.

We conclude that Idaho Power's management failures are grounds for disallowance to management expense included in revenue requirement. Although Idaho Power's improper conduct did not, by providence, harm ratepayers, its lack of management oversight put ratepayers at risk. It failed to exercise the reasonable standard of care we expect utilities to exercise as co-owners of a generation facility. To ensure future compliance with this standard, we find a one-time disallowance to management expense of \$40,000, equivalent to 10 percent of the Oregon portion of the investment, to be appropriate. We note that Idaho Power's 2011 application for a general rate revision involved many instances of management decision-making. Because we isolate only this instance as demonstrating inadequate management, we find the 10 percent disallowance to be appropriate. Our decision in this docket is not precedential for future Bridger investments.

We now turn to the question how to implement this decision. In their stipulation, the parties agreed that the rates implemented on March 1, 2012, would include Idaho Power's Bridger 3 investments as filed, but that Idaho Power would request to defer the variance between revenues resulting from rates that include the investments and revenues resulting from rates without the investments. Under this proposal, Idaho Power would refund to customers any money collected from ratepayers for investments found by this Commission to be imprudent.

Because we find no investment to be imprudent, the provision in the stipulation is moot. Therefore, to implement our decision regarding Idaho Power's management failures, we direct Idaho Power to deduct the \$40,000 from the outstanding balance to the utility's 2007-2008 net variable power cost deferral.

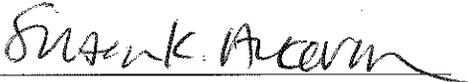
Finally, we reject CUB's argument that the scrubber upgrade investment is not used and useful because more controls may be required in the future. As we held in docket UE 246 with regard to scrubber upgrades made by Pacific Power, "[t]hese investments are placed in service and are useful to ratepayers."⁵

⁵ See *Id.* at 32, citing ORS 757.355(1).

V. ORDER

IT IS ORDERED that Idaho Power Company must deduct \$40,000 from the outstanding balance for its 2007 Net Variable Power Cost deferral.

Made, entered, and effective APR 11 2013



Susan K. Ackerman
Chair



John Savage
Commissioner



Stephen M. Bloom
Commissioner



A party may request rehearing or reconsideration of this order under ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-001-0720. A copy of the request must also be served on each party to the proceedings as provided in OAR 860-001-0180(2). A party may appeal this order by filing a petition for review with the Court of Appeals in compliance with ORS 183.480 through 183.484.